

# 2018

## Annual Report

Federal Financial  
Supervisory Authority



BaFin

Bundesanstalt für  
Finanzdienstleistungsaufsicht



# Annual report 2018

Federal Financial Supervisory Authority  
(Bundesanstalt für Finanzdienstleistungsaufsicht – BaFin)



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# Opinion

## BaFin President Felix Hufeld on digitalisation in financial supervision and the financial industry

While a good ten years ago it was still said that banks' last true innovation was the ATM<sup>1</sup>, the whole financial industry is now transforming with considerably more momentum. The key driver of this transformation is digitalisation, a word which has undergone a shift in meaning in recent years. While digitalisation originally meant the conversion of analogue information into digital form and the transfer of tasks previously carried out by people to the computer, we now often speak of the digital transformation: by this, we mean the fundamental and continual digital shift that is reflected in all aspects of life and is constantly bringing about change, not least in the financial sector. Some people

call this trend "disruptive"; others talk of "creative destruction". Whichever words we use to describe it, digitalisation has the potential to break apart entire value chains and give rise to new business models. Such times of upheaval result in brand new opportunities, but it is clear that they also cause new risks.

One of BaFin's key aims is to ensure the functioning, stability and integrity of the German financial market, including in these times of progressive digitalisation. And this means that we cannot simply allow digitalisation to wash over us like an act of God; we have a duty to play a part in shaping the digital transformation within our remit and to ensure that we ourselves are fully ready for the digital age. In order to give structure to this process, we have developed a digitalisation strategy. This consists of three elements:

<sup>1</sup> Paul Volcker: "The only thing useful banks have invented in 20 years is the ATM", in the New York Post, 13 December 2009, retrieved on 8 February 2019.

With regard to the first element, which centres around supervision and regulation, our focus is on understanding the developments in the financial markets and addressing the recurring questions about how to deal with the market changes caused by digitalisation in supervision and regulation. These changes are driven primarily by phenomena such as big data and artificial intelligence (BDAI) and distributed ledger technology (DLT). The first step is to classify and assess digitalisation and its impact on the financial markets appropriately. From this, we then need to deduce the implications for supervision and regulation. We as supervisors must anticipate future developments as early as possible and monitor them. It goes without saying that to do this we are in regular contact with companies, industry associations, academia, politicians and the international community of regulators, and that we share information and ideas with them.

And we have already made some significant progress on this point: to allow us to keep pace with the digitalisation-driven market developments, we have established a BaFin-wide network of experts, with the Division for Innovations in Financial Technology (SR 3) at its heart. In close cooperation with the individual specialist divisions, SR 3 records and assesses innovations in financial technology and their consequences, including for consumers, and draws up scenarios for the immediate future. Another milestone was the report "Big data meets artificial intelligence"<sup>2</sup>, which we compiled jointly with academics and consulting firms and opened up to consultation in July 2018. Since then, we have received a wide variety of interesting contributions from the industry and beyond. A number of distinct themes are emerging, and we intend to prioritise and deal with these based on their urgency and significance.

Another area of focus is the newly emerging issues surrounding crypto tokens. The trend on the crypto markets remains highly volatile. It is therefore difficult at present to make a conclusive judgment on the future significance of these markets. Initial ideas for how regulators should classify this phenomenon are being discussed at both a national and an international level.

The second element of the digitalisation strategy revolves around security in the technologies and IT systems of supervised companies. As great as the opportunities are that these innovative technologies offer to companies and consumers alike, it would be careless to dismiss cyber risks – or any other potential risks such innovations could entail. Moreover, the highly interconnected nature of the financial industry can mean that the effects of failures in the IT infrastructure of one institution can spread to other market participants and have large-scale consequences, and potentially even consequences of systemic importance. And companies in the financial industry are already among the favoured targets for cyber attacks. These risks need to be recognised and addressed by supervisors – and not just nationally, but at a European or even a global level.

At the moment, BaFin is focusing primarily on prevention, from IT governance, to information and security management, to the outsourcing of IT services. We have achieved our first interim goals, such as establishing the Directorate for IT Supervision, Payment Transactions and Cyber Security (GIT). As well as combining cross-sectoral expertise on fundamental issues of IT supervision, this directorate also increasingly carries out its own IT security inspections.

We are leading the way in the European regulatory community by creating a set of framework documents to formulate comparable IT requirements for companies across the different supervisory areas. This includes the Supervisory Requirements for IT in Financial Institutions (*Bankaufsichtliche Anforderungen an die IT – BAIT*) and the Supervisory Requirements for IT in Insurance Undertakings (*Versicherungsaufsichtliche Anforderungen an die IT – VAIT*). We are currently writing corresponding requirements for asset management companies (*Kapitalanlagegesellschaften*) ("KAIT"), which we intend to publish by mid-2019 at the latest. And we have also set out our expectations for other areas, such as the use of cloud services.

But given that the threat level is constantly on the rise, we cannot stop there. Increasingly, questions of resilience and crisis management are coming into the spotlight. An important role will be played here by cyber stress tests for the German financial sector, known as "red teaming" in the field.

And last but not least, the third element: digitalisation within BaFin itself. Specifically, the question we must ask ourselves now is how does BaFin need to adapt and evolve – both internally and at its points of interaction with the market? For us, "digitalisation within BaFin"

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<sup>2</sup> BaFin, Big data meets artificial intelligence – Challenges and implications for the supervision and regulation of financial services. The report was prepared in collaboration with PD – Berater der öffentlichen Hand GmbH, Boston Consulting Group GmbH and the Fraunhofer Institute for Intelligent Analysis and Information Systems.

does not just mean digitalising existing paper-based processes. It involves rethinking and defining processes in their entirety, optimising workflows within them, and using the best possible digital tools.

This transformation does not have to start from square one. Since it was founded in May 2002, BaFin has already digitalised a substantial portion of its supervisory and support processes. Without the appropriate IT infrastructure, projects the scale of the Solvency II implementation or BaFin's integration into the Single Supervisory Mechanism (SSM) would have been impossible. A wide variety of specialist applications have now been developed to carry out procedures more efficiently, to speed up and improve data analysis, and to enable the electronic submission of notifications.

While a large number of partial processes have already been digitalised, BaFin is still midway through its transformation into a fully digitalised supervisory authority. The newly created position of Chief Digital Officer (CDO) is intended to accelerate this transition.

The "Zeus" project to implement an electronic file management system will play a vital role; it is a pivotal tool that underpins almost all supervisory and administrative processes and is a key project in BaFin's internal digitalisation. Another example is the "Gaia" project, which focuses on the processing of details about individuals, for instance members of supervisory boards and senior management.

Another objective within this third element is to use digital technologies to improve BaFin's analytical abilities in the evaluation of large quantities of data, for example in market surveillance.

Our digitalisation strategy and the realisation of all the objectives contained within it may be quite a feat for BaFin, but it is one that we are facing up to, and one that will open up a range of opportunities for us. Nevertheless, we are aware that the strategy as it is now is not set in stone, and we will need to keep adapting it to new developments. But this too is a challenge that we will overcome. The future of the financial markets is digital, and so is BaFin's.





# Key figures at a glance



## 2014-2018 key figures at a glance

	2014	2015	2016	2017	2018
<b>Credit institutions<sup>1,2</sup></b>					
<b>Capital resources<sup>3</sup></b>					
Tier 1 capital (€ billion)	453.0	473.1	489.6	491.2	514.7
Own funds (€ billion)	526.6	544.6	562.0	559.7	580.5
Tier 1 capital (% ratio)	14.7%	15.3%	15.7%	16.6%	16.8%
Own funds (% ratio)	17.1%	17.7%	18.0%	18.9%	18.9%
<b>Asset structure and portfolio quality</b>					
Total assets (€ billion) <sup>4</sup>	8,199.8	8,000.7	8,024.3	8,411.2	8,329.80
Total assets (€ billion) <sup>5</sup>	8,176.0	7,975.9	7,995.3	8,379.5	8,303.30
<b>Structure of loans and advances to banks and non-banks (%)<sup>6</sup></b>					
Domestic banks	16.2%	15.9%	16.5%	21.4%	19.8%
Foreign banks	12.3%	12.3%	10.9%	9.3%	9.2%
Non-banks – other financial institutions	2.3%	2.4%	2.5%	2.6%	2.7%
Non-financial companies	16.0%	15.9%	16.2%	15.8%	16.7%
Private households	29.9%	30.0%	30.7%	29.3%	30.2%
Private non-profit organisations	0.3%	0.3%	0.3%	0.3%	0.3%
Public-sector households	6.1%	5.8%	5.5%	5.2%	4.8%
Foreign non-banks	16.9%	17.4%	17.4%	16.0%	16.2%
Amounts due to non-banks as a proportion of loans and advances to non-banks (%) <sup>7</sup>	102.1%	103.4%	104.3%	104.3%	103.0%
Proportion of foreign-currency loans to private households (%) <sup>8</sup>	0.5%	0.5%	0.4%	0.3%	0.2%
Loans in default plus loans on which specific allowances have been recognised before deducting specific allowances as a proportion of loans and advances to banks and non-banks <sup>9</sup>	3.2%	2.4%	2.2%	1.6%	1.1%
<b>Structure of equity and liabilities (proportion in %) <sup>10</sup></b>					
Amounts due to domestic banks	13.8%	13.4%	13.0%	12.6%	12.3%
Amounts due to foreign banks	6.8%	7.6%	8.2%	7.5%	6.8%
Deposits from domestic non-banks	38.1%	40.3%	41.5%	40.9%	42.2%
Deposits from foreign non-banks	6.0%	6.4%	6.5%	6.4%	6.0%
Securitised debt incl. subordinated capital	12.4%	11.7%	11.3%	15.3%	11.8%
<b>Income statement structure (in % of average total assets)<sup>11</sup></b>					
Net interest income	1.10%	1.11%	1.09%	1.03%	1.01%
Net commissions received	0.35%	0.35%	0.36%	0.37%	0.34%
General administrative expenses	1.01%	1.05%	1.06%	1.09%	1.05%
Net trading income	0.04%	0.04%	0.04%	0.07%	0.04%
Operating profit/loss before measurement gains/losses	0.45%	0.44%	0.47%	0.37%	0.34%
Measurement gains/losses	-0.08%	-0.04%	-0.11%	-0.02%	-0.07%
Operating profit/loss	0.37%	0.40%	0.37%	0.36%	0.27%
Net amount of other and extraordinary income and expense	-0.08%	-0.09%	-0.03%	n/a	n/a

	2014	2015	2016	2017	2018
Profit for the year before tax	0.30%	0.31%	0.33%	n/a	n/a
Profit for the year after tax	0.21%	0.21%	0.24%	n/a	n/a

1 For the number of undertakings under supervision. see Appendix.

2 For further information on credit institutions in Germany. see chapter III.

3 Including financial services institutions.

4 Assets based on balance sheet statistics (Bilanzstatistik – BISTA) and data provided under the German Financial and Internal Capital Adequacy Information Regulation (Verordnung zur Einreichung von Finanz- und Risikotragfähigkeitsinformationen – FinaRisikoV) (including financial services institutions).

5 Assets based on BISTA.

6 Structure in accordance with BISTA.

7 Based on BISTA and FinaRisikoV data (including financial services institutions).

8 Information based on external status.

9 Based on FinaRisikoV data.

10 Based on BISTA only. The „Securitized debt incl. subordinated capital“ item also includes the FinaRisikoV data (financial services institutions etc.).

11 For the years 2013 to 2017, the data has been taken from publications of the Deutsche Bundesbank (results of operations of German credit institutions). The data in the 2018 annual financial statements is not yet available in full, so the figures have been based on the preliminary FinaRisikoV notifications and an approximate income statement structure has been shown.

### Insurance undertakings and Pensionsfonds<sup>1, 5</sup>

		Life insurers			Private health insurers			Property and casualty insurers		
		2016	2017	2018 <sup>2</sup>	2016	2017	2018 <sup>2</sup>	2016	2017	2018 <sup>2</sup>
Gross premiums written	(€ billion)	85.7	85.6	87.4	37.2	39	39.7	71.0	76.0	78.2
Investments	(€ billion) <sup>3</sup>	877.7	906.1	949.2	260.1	272.9	287.7	164.9	171.2	175.8
Average SCR coverage	(in %) <sup>4,6</sup>	316.3	382.1	448.3	418.6	495.5	430.3	288.3	284	283.1

#### Pensionskassen

		2016	2017	2018 <sup>2</sup>
Gross premiums earned	(€ billion)	6.9	7.3	7.2
Investments	(€ billion) <sup>3</sup>	154.1	162.2	170.4
Average solvency	(%)	131.2	133.7	132.1

#### Pensionsfonds

		2016	2017	2018 <sup>2</sup>
Gross premiums written	(€ billion)	2.7	2.4	10.2
Investments	(€ billion) <sup>3,7</sup>	35.4	36.9	42.7
Beneficiaries		924,074	942,782	1,058,215
Benefit recipients		297,370	291,165	373,134

1 The figures provided here have been determined on the basis of the Solvency II supervisory regime, which entered into force on 1 January 2016. Due to the associated fundamental change in the system, comparable figures are not always available for the years up to 2016.

2 The data provided is only preliminary, because it is based on interim reports and forecasts.

3 Carrying amounts in accordance with the German Commercial Code.

4 A few undertakings are exempt from some of the interim reporting requirements in accordance with section 45 of the Insurance Supervision Act.

5 For information on key figures of the Insurance and Pension Funds Supervision Sector, see also chapter IV 2.4.

6 Fourth-quarter figure.

7 Total investments.

	2014	2015	2016	2017	2018
<b>Capital market companies<sup>1,3,4</sup></b>					
Supervised financial services institutions	676	674	708	722	722
Supervised branches	80	86	94	106	110
Total number of approvals <sup>1</sup>	1,642	1,682	1,652	1,405	1,174
of which prospectuses	377	399	348	301	303
of which registration documents	34	32	33	38	35
of which supplements	1,231	1,251	1,271	1,066	836
German asset management companies with authorisation <sup>2</sup>	113	138	136	142	139
Registered German asset management companies <sup>2</sup>	143	218	260	309	365
Number of investment funds <sup>2</sup>	5,410	5,649	6,122	5,752	5,917
Assets managed by those funds (€ billion) <sup>2</sup>	1,421	1,743	1,908	2,062	2,062

1 Due to a change in the data collection method during the period under review, there is only limited comparability between different periods.

2 „German asset management company“ (*Kapitalverwaltungsgesellschaft* – KVG) has only been a defined term in accordance with section 17 of the German Investment Code (*Kapitalanlagegesetzbuch* – KAGB) since 2013, when the German Investment Act (*Investmentgesetz*) expired. Due to the associated fundamental change of system, comparable figures are not available for the years up to 2013.

3 For the number of undertakings under supervision, see the Appendix.

4 For information on key figures of the Securities Supervision/Asset Management Sector, see also chapter VI.

**Legend:**

n/a: not available

Tier 1: highest category of own funds

KVG: German asset management company (*Kapitalverwaltungsgesellschaft*)

SCR: solvency capital requirement

FinaRisikoV: German Regulation on the Submission of Financial and Risk-Bearing Capacity Information under the Banking Act (*Verordnung zur Einreichung von Finanz- und Risikotragfähigkeitsinformationen nach dem Kreditwesengesetz*)

BISTA: Balance sheet statistics (*Bilanzstatistik* – BISTA)

GuV: income statement (*Gewinn- und Verlustrechnung*)

I

# Spotlights





## 1 Brexit

**T**he lack of clarity about the date and terms of the United Kingdom's (UK) possible departure from the European Union (EU) also posed considerable challenges for regulatory and supervisory authorities<sup>1</sup>.

Given the uncertainty, supervisory authorities and policymakers also had to prepare for a no-deal scenario. On 29 March 2019, the German Tax Act relating to Brexit (*Brexit-Steuerbegleitgesetz*) entered into force. The act is aimed at minimising any possible negative effects a hard Brexit may have on the functioning and stability of the financial markets and in this way also at protecting consumers. BaFin was involved in drafting the act right from the start.

<sup>1</sup> The UK had originally been scheduled to leave the EU in the night from 29 to 30 March 2019. On 29 March 2019, the British House of Commons again rejected the agreement Prime Minister Theresa May had negotiated with the EU. At the time of going to press, the alternatives facing the UK were its departure from the EU without a deal on 12 April 2019 or a lengthy delay to Brexit, which would require the country to take part in European elections at the end of May.

### EU passporting rights

The act allows BaFin to permit companies based in the UK that have so far conducted business in Germany in the context of the freedom of establishment or the freedom to provide services to continue using their EU passporting rights in Germany for a transitional period, where this is necessary to prevent disadvantages for the functioning or stability of the financial markets.

On this basis, BaFin can, if appropriate, give undertakings until the end of 2020 to wind up existing contracts in an orderly manner or to transfer them to new structures with a legally viable future. It goes without saying that BaFin expects all affected companies to deploy all the resources at their disposal to help this process along.

### Hundreds of discussions

In preparation for Brexit, BaFin conducted hundreds of one-on-one discussions and held several workshops at which it explained to financial services undertakings contemplating relocation to Germany what to expect here from a regulatory perspective as well as the requirements that BaFin has set as supervisor. BaFin repeatedly emphasised in this process that applicable standards would not be allowed to be diluted, let alone ignored. It made clear that licences must be deserving of their name and that BaFin would refuse to accept letterbox companies.

## 2 Reforms at European level

### 2.1 The European Supervisory Authorities

The planned reform of the European Supervisory Authorities (ESAs) also featured high on the list of topics to which BaFin gave detailed attention in 2018.<sup>2</sup> In September 2017, the European Commission had submitted draft amendments to the ESA regulations, which envisaged far-reaching centralisation of, and thus a fundamental change to, the EU's existing supervisory architecture. The amendments focused on, among other things, changes to the internal governance and funding of the ESAs. Another objective was the transfer to the ESAs of direct supervisory powers that have to date been a national responsibility. The intention was to empower ESAs to intervene in national supervisory strategies and supervision processes.

#### **BaFin critical of the plans**

BaFin took a critical view of the European Commission's plans from the start. BaFin President Felix Hufeld, for example, put the question "Why fix something that is essentially working?" at BaFin's annual press conference on 3 May 2018. The ESAs only needed very few new powers, he explained. Those who want to strengthen them, he continued, "should above all ensure that they can make better use of the extensive powers they already have".

The European System of Financial Supervision, of which the ESAs form part, was created in 2010 specifically as a network of national and European supervisory authorities. Hufeld warned against turning the ESAs into supervisors of the national competent authorities, and pointed out that there was no factual justification for such a move. The member-driven character of the ESAs had proven to be successful, he maintained.

#### **Strengthen the EBA in the fight against money laundering**

In September 2018, The European Commission updated its draft amendments to the ESA regulations, adding a call to strengthen the EBA in the fight against money laundering. Following a string of scandals, the ESAs' anti-money laundering powers for the entire financial

market are to be expanded and bundled at the EBA. For example, the EBA is to be able to enforce investigations at the national level. Furthermore, the efforts of the national competent authorities in tackling money laundering are to be reviewed.

The separate deliberations of the Council of the European Union and the European Parliament on the European Commission's proposals lasted into December 2018. Agreement with the Council was only reached for the money laundering part. The trilogue started in the middle of February 2019, after the European Parliament had agreed on a reform text. After that, the Council adopted a "general approach" to the upcoming negotiations. The positions were far apart – particularly on some key issues. It was all the more surprising, therefore, that an agreement was reached on 21 March 2019, which adopts a number of the Council's proposals. As a result, many of the European Commission's ideas which BaFin had been critical of are no longer on the agenda.

### 2.2 Banking union

The work to strengthen the EU banking union made further progress in 2018. The risk reduction proposal, a comprehensive package of reforms aimed at reducing the risks in the European banking sector, is very close to completion. In addition, at the Euro Summit on 14 December 2018, the EU heads of state and government, on the basis of a report of the Eurogroup, adopted a declaration in which they endorse all the elements of the report, including the modalities of reforming the European Stability Mechanism (ESM) and the rules for the common backstop to the Single Resolution Fund (SRF). One of the aims of the reform: in the event that the resources of the SRF are not sufficient for a resolution, a backstop that is fiscally neutral over the medium term is to be developed for the SRF as a last-resort assurance. The backstop is to be provided as a credit line under the management of the ESM.

#### **Risk reduction is better than risk sharing**

"In principle it is the correct approach to work out crisis scenarios before the crisis even occurs", said BaFin President Felix Hufeld in his speech at BaFin's New Year press reception in January 2019. But it was clear, he added, that the backstop amounted to a deeper mutualisation of banking risks in the eurozone. An even better approach than sharing risks, Hufeld stated, was to reduce them. BaFin therefore welcomes the fact that the EU wants to strengthen the resilience of the European financial institutions further and improve the supervision of cross-border banking groups. There are

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<sup>2</sup> The European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA).

plans to introduce a mandatory unweighted equity ratio, also referred to as leverage ratio, as envisaged in the Basel III framework. It is to be set at a minimum of 3%. "A moderate figure, in my opinion", commented Hufeld.

#### **No ratios of 20% or more**

Hufeld rejected calls for ratios of 20% or more. Applied in moderation, the leverage ratio could act as an outer crash barrier and be a useful complement to the existing risk-sensitive requirements and a functioning risk management system, he said. If raised too high, Hufeld warned, one size fits all limits could actually increase the risks. If used as the only or even the primary tool for capital management, undifferentiated leverage ratios were counterproductive. "Allow me to caution against a knee-jerk yearning for simplicity, like that of Basel I, purported to be less prone to disruption", explained Hufeld. It was vital to defend the principle of risk sensitivity, he added.

#### **Greater proportionality**

BaFin welcomes the decisions that have been made on the issue of proportionality. For the first time, "small, non-complex institutions" have been given a clear definition in regulation, thus creating a reliable foundation on which these types of institutions can be granted specific relief in the future. BaFin, the Deutsche Bundesbank and the Federal Ministry of Finance have made the case for greater proportionality time and again over the past years. From BaFin's point of view, it is important that for small and medium-sized institutions, too, the level of supervisory requirements needs to be based on the respective risk. The Single Rulebook for all European banks will only be accepted in the long run if its requirements have been formulated such that they are proportionate and appropriate.

## 3 MiFID II – one year on

"Greater transparency, better investor protection" – five words give you the gist of "what MiFID II<sup>3</sup> alone spells out over hundreds of pages", remarked BaFin President Felix Hufeld only a few days after the Directive entered

into force on 3 January 2018, assigning MiFID II to the "regulatory super heavyweight division".

#### **Positive result overall**

It is all the more remarkable, therefore, that BaFin is able to conclude from its market surveys that the first year under MiFID II has delivered positive results overall. Although a few isolated implementation problems occurred on 3 January 2018 and further implementation was required even a year after the new regulations came into force, neither came as a surprise, given the extent of the new regulations.

#### **Two market surveys relating to conduct of business rules**

As soon as MiFID II had entered into force, BaFin launched its first market survey questioning credit institutions in relation to the various new conduct of business rules. BaFin's aim was to get an early overview of the status of implementation. A total of 20 private and foreign banks and 10 savings and cooperative banks from each of the regional associations participated in the surveys on a voluntary basis. In the second half of 2018, BaFin extended its survey by adding financial services institutions to the scope as part of another market survey in order to obtain an overview of the market as a whole. 25 financial services institutions and 5 securities trading banks took part in this survey.

Both market surveys in relation to the conduct of business rules focused on the record-keeping obligations (taping), the suitability statement and ex-ante cost information, and thus new conduct of business rules that are particularly relevant for consumers. The institutions deployed significant financial and personnel resources and went to considerable effort to implement the new regulations of MiFID II. This finding was made for the entire market, irrespective of the size or business models of the institutions concerned.

It was encouraging that the institutions were meeting their obligation to record telephone conversations (taping) and the technical implementation had largely been successful. On the other hand, there were also incidents where the institutions had failed to record parts of conversations that they should have recorded. In isolated cases, it was noted that a summary of the conversation had been recorded subsequently, which was not sufficient. The sample-based analysis of the cost statements also revealed weaknesses with regard to their completeness and mathematical accuracy.

#### **Market survey into product governance**

In the second half of 2018, a market survey was conducted in relation to the new product governance

<sup>3</sup> Markets in Financial Instruments Directive (MiFID II), Directive 2014/65/EU, OJ EU L 173/349. MiFID II was implemented by way of the German Second Act Amending Financial Markets Regulations (*Zweites Finanzmarktnovellierungsgesetz*) of 23 June 2017, Federal Law Gazette I, page 1693.

requirements of MiFID II. In this survey, BaFin questioned 55 institutions, including 25 financial services institutions, 5 securities trading banks and 25 banks and savings banks, on the status of implementation. The focus was on the processes the institutions had established in their role as manufacturers and distributors.

The overall results of this survey were likewise encouraging: the implementation of product governance was largely successful. As for the determination of the target market, in individual cases, the statements made in relation to certain target market categories were in need of improvement. Many samples across all classes of financial instruments indicated that the institutions had specified the client's investment objectives as "asset accumulation or optimisation". Greater differentiation for some of these products would have been desirable. However, BaFin expects that the determination of the target market will increasingly take shape as time progresses.

The market survey revealed that smaller institutions are finding it increasingly difficult to meet the complex and extensive regulatory requirements in addition to carrying on their day-to-day business. By contrast, the larger firms considered it challenging to integrate the new processes within the framework of existing processes. For this reason, BaFin provides guidance in documents such as MaComp, the Minimum Requirements for the Compliance Function and the Additional Requirements Governing Rules of Conduct, Organisation and Transparency.<sup>4</sup> It will also call on the European Securities and Markets Authority (ESMA) for guidance documents.

## 4 Three years of Solvency II

The European supervisory regime Solvency II was, and continues to be, reviewed, as planned (see info box "Solvency II review" on page 25). BaFin believes that, three years after it entered into force at the beginning of 2016, the progress made due to Solvency II outweighs its alleged limiting effects. Critics argue that it takes too

much effort to meet the reporting obligations or that smaller insurers are put at a disadvantage.

Dr Frank Grund, Chief Executive Director of Insurance and Pension Funds Supervision, commented as follows: "I want to counter the criticism by saying something positive: the entirety of reporting obligations arising from the Solvency and Financial Condition Report (SFCR), the Regular Supervisory Reporting (RSR) and the Own Risk and Solvency Assessment (ORSA) force insurance undertakings to take a close look at the key elements of their activities – their customers, their governance system and their risk profile."

### **Blanket accusation**

Even the accusation that the regulations are disproportionate was too general, said Grund. A differentiated approach was needed to analyse the challenges posed to undertakings by Solvency II. The background is that Solvency II only applies to insurers that reach certain thresholds. What is more, the principle of dual proportionality means that regulation and its application in supervisory practice must take the nature, scale and complexity of an undertaking's risks into account. In the supervised undertaking, too, there should be a reasonable balance between the effort needed to meet regulatory requirements and the undertaking's own risk profile.

### **Benefits for the European market**

Grund believes that the achievement of Solvency II for the European market is that the risk management systems of insurers have been strengthened and the requirements for such systems have been standardised throughout Europe. He admitted, however, that not everything was perfect. Some reporting requirements, for example, would benefit from being simplified and reduced in scale.

He also voiced support for the recommendation EIOPA had made to the European Commission during the SCR review that the interest rate risk should be reassessed (see info box "2020 Review" on page 25). The current standard formula did not recognise negative interest rates and had therefore grown out of touch with both reality and internal models. If legislators use the Solvency II review as an opportunity to introduce capital relief for long-term business as an incentive to promote sustainability projects, for example, it would have to be ensured from a supervisory perspective that appropriate risk management remained the ultimate benchmark.

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<sup>4</sup> Circular 5/2018 (WA) – Minimum Requirements for the Compliance Function and Additional Requirements Governing Rules of Conduct, Organisation and Transparency – MaComp.



At a glance

## Solvency II review

As part of the Solvency II review launched in 2018, the European Commission presented a revised version of the Delegated Regulation, which contains the implementing provisions for Solvency II. In this context, the European Commission did not adopt the recommendations on interest rate risk made by the European Insurance and Occupational Pensions Authority (EIOPA). Interest rate risk is now to be subjected to the general review process in 2020 (2020 Review). BaFin continues to consider it urgently necessary to update interest rate risk and therefore supports EIOPA's proposal. The revised version of the Delegated Regulation provides for the recalibration of various risk factors. BaFin welcomes that it also envisages simplifications for individual risk modules such as counterparty default risk. The European Commission submitted the revised Delegated Regulation to the European Council and the European Parliament on 8 March 2019. The latter then have the right to object for a three-month period.

## 2020 Review

The components of Solvency II that the European Commission will have to review from 2020 onward include the long-term guarantees and measures against equity risk, the methods, assumptions and standard parameters to be used when calculating the solvency capital requirement (SCR) according to the standard formula, and the rules and supervisory authorities' practices for calculating the minimum capital requirement (MCR). In addition, the benefit of intensifying the supervision of groups and investment management within a group are being investigated. The European Commission has issued a corresponding call for advice to EIOPA.

# 5 Digitalisation

## 5.1 IT supervision at banks and insurance undertakings

Increasing digitalisation is making undertakings in the financial sector vulnerable. Since the industry is closely interconnected, IT infrastructure failures in one undertaking may spread to other market participants and, in extreme cases, even threaten financial stability. In order to engage in effective prevention measures in cooperation with undertakings in the financial sector, BaFin pooled key skills throughout its organisation to establish the IT Supervision, Payment Transactions and Cyber Security Directorate (GIT) in 2018. This Directorate, which acts across all BaFin sectors, focuses on, among other matters, policy issues relating to cyber security in digitalisation, operational supervision of payment institutions and e-money institutions, policy issues relating to IT supervision and the inspection regime as well as IT inspections at banks, insurance undertakings and German asset management companies.

### Three-stage plan for IT supervision

BaFin has developed a three-stage programme for its IT supervisory practice. Stage 1 involves a set of frameworks in which comparable IT requirements are formulated for the undertakings in the different supervisory areas. In addition to the Supervisory Requirements for IT in Financial Institutions (BAIT) published back in November 2017, this also includes the Supervisory Requirements for IT in Insurance Undertakings (VAIT) (see info box "VAIT – Supervisory Requirements for IT in Insurance Undertakings" on page 26).

BAIT and VAIT set out in detail what BaFin expects banks and insurers to do in selected areas of IT security. The requirements under VAIT are similar to those under BAIT. In both documents, BaFin clearly states that IT security is a management issue. Among other things, the circulars therefore also aim to increase awareness of IT risks among members of the management board, including of risks that may arise when IT services are spun off or procured.

To minimise uncertainty when outsourcing or spinning off activities to cloud providers, BaFin published additional guidance on outsourcing to cloud providers in November 2018 to supplement BAIT and VAIT (see info box "Guidance on outsourcing to cloud providers" on page 26). Another document planned to be circulated for consultation in the course of 2019

At a glance

## VAIT – Supervisory Requirements for IT in Insurance Undertakings

BaFin published VAIT on [www.bafin.de](http://www.bafin.de) in July 2018. It contains guidance on interpreting the requirements for the system of governance in the Insurance Supervision Act, to the extent that they relate to the technical and organisational resources of the undertakings. With VAIT, BaFin aims to specify a flexible and practice-based framework for the IT structure, in particular for the management of IT resources and for IT risk

management, for the management of the undertakings. The Circular is applicable to all insurance undertakings and *Pensionsfonds* subject to supervision by BaFin. It does not apply to special purpose insurance vehicles within the meaning of section 168 of the Insurance Supervision Act and guarantee schemes within the meaning of section 223 of the Insurance Supervision Act.

are the Supervisory Requirements for IT in Asset Management Companies (KAIT), which set out more detailed requirements for German asset management companies.

Stage 2 is aimed at making banks more resilient to cyber attacks and underpinning their ability to maintain business continuity. At this stage, the focus will shift to the effectiveness of the existing safeguards. Since the end of 2018, BaFin and the Deutsche Bundesbank have been working on the possible implementation of cyber stress tests (red teaming tests).

Stage 3 involves improving the crisis management of banks: not only the institutions but BaFin, too, must be prepared for a cyber attack or IT security incident at all times. BaFin is therefore planning to expand BAIT by adding a module on emergency management, including

emergency tests. Cyber drills will also be covered: they involve all relevant players acting in concert in crisis situations – both nationally and internationally.

In a speech he held in November 2018, BaFin President Felix Hufeld was critical of the banks: “Many institutions in Germany, as well as in other European countries, are still struggling with cyber hygiene. IT systems are outdated, third-party service providers are not always adequately monitored, processes and technologies are often not tested sufficiently.” Another issue was that not all banks were spending enough money on enabling them to detect cyber attacks and identify threats before it was too late. In addition, cyber risk management left much to be desired in many cases. It was also noticeable that, when banks dealt with IT risk, they focused primarily on technology rather than people.

At a glance

## Guidance on outsourcing to cloud providers

In November 2018, BaFin published its guidance on outsourcing to cloud providers on its website. In this Guidance Notice, BaFin and the Deutsche Bundesbank explain their current supervisory practice in these cases of outsourcing. The supervisory authorities also set out clearly how they rate the different kinds of wording in contract clauses. In addition, they want to create awareness among the supervised undertakings of problems that may arise when using cloud services and what supervisory requirements may arise as a result.

The Guidance Notice on cloud services does not contain any new requirements; the existing requirements for outsourcing therefore remain unchanged. For example, outsourcing to cloud providers is also subject to the general rule that the management’s responsibilities must not be transferred to the cloud services provider when data is outsourced. The guidance is intended for credit institutions, financial services institutions, insurance undertakings, pension funds, investment firms, asset management companies, payment institutions and e-money institutions.

## 5.2 BaFin's digitalisation strategy

Increasing digitalisation and the big data and artificial intelligence (BDAI) phenomenon are visibly changing the financial market. This market is, however, regulated and supervised using traditional methods because, more than other markets, it relies on the ability to trust its functioning, stability and integrity. BaFin's role is to create a solid basis for this trust. For this reason, it adopted a digitalisation strategy in August 2018 in which it defines three basic issues:

- What should the supervisory and regulatory response be to the market changes triggered by digitalisation?
- How can BaFin ensure that the innovative technologies, IT systems and data used by the supervised undertakings are secure?
- How should BaFin itself continue to develop – both internally and at the interfaces with the market – in the light of the ongoing digitalisation process?

In its digitalisation strategy, BaFin reveals what direction it is planning to take in these three fields of action. It is not starting from zero in any of them. BaFin is already working and thinking digitally in many areas, but to stand still would be a mistake, especially in the field of digitalisation. This is why the digitalisation strategy is not cast in stone, and BaFin will rethink and revise it at regular intervals. An important role in this regard will be played by the new Chief Digital Officer, who will drive BaFin's internal digitalisation forward and coordinate the further development of the overall strategy.

## 5.3 BaFin report "Big data meets artificial intelligence"

What then should the response be to the market changes triggered by digitalisation? Among other measures, BaFin looks into this issue in its report "Big data meets artificial intelligence – Challenges and implications for the supervision and regulation of financial services", which it published in June 2018. The report contains the findings of a study on which experts from Partnerschaft Deutschland, the Boston Consulting Group (BCG) and the Fraunhofer Institute for Intelligent Analysis and Information Systems (IAIS) also collaborated. The objective was to obtain a comprehensive picture to enable BaFin to identify strategic trends, market developments and newly emerging risks at an early stage and to respond appropriately. The report looks into the implications of technology-driven market developments from a number of regulatory and supervisory perspectives – including that of consumers.

"The results clearly show how important it is for us to address these issues from a supervisory and regulatory perspective", emphasised BaFin President Felix Hufeld. The race to innovate in the field of financial data had already begun. And it was already becoming obvious that systemic dependencies on BDAI companies could arise outside the regulatory framework.

### Ultimate responsibility is always carried by people

In the report, BaFin makes it clear once again that management carries the responsibility, even in times of the accelerated automation of processes. BaFin also believes that important conclusions can be drawn with a view to consumer protection: customers need to be made more aware of the value of the data they reveal and who is able to use that data. Users of BDAI must also bear that in mind, since consumer trust is key to the success of BDAI innovations.

From a market perspective, the study shows that big data and artificial intelligence offer significant competitive opportunities for both existing and potential new market participants. These opportunities result primarily from the increased disaggregation of the value chain that is now enabled by these technologies.

### Report consultation

BaFin submitted its report "Big data meets artificial intelligence" and the key questions it contains for public consultation until the end of September 2018.

BaFin received a large amount of feedback on its report. Participants in the consultation process included advocacy groups as well as individual institutions, national and international authorities and representatives of the academic community. A summary of the responses can be found in the second issue of the BaFinPerspectives series, which was published at [www.bafin.de](http://www.bafin.de) on 28 February 2019. In this issue, BaFin President Felix Hufeld provides an initial assessment in an interview.

## 5.4 BaFinPerspectives publication series

In August 2018, BaFin published the first issue of its BaFinPerspectives series, which deals with the increasing digitalisation and issues around BDAI from a number of different perspectives. The issue focuses on, among other topics, the supervisory and regulatory treatment of big data and artificial intelligence. The second issue of BaFinPerspectives was published on 28 February 2019. It is also dedicated to the topic of digitalisation. The next issue – on sustainable finance – is scheduled for 9 May.

### **Making an impact**

The BaFinPerspectives series contains contributions from internal and external authors and interviews. The series is published in German (*BaFinPerspektiven*) and English on BaFin's website. BaFin President Felix Hufeld wants BaFinPerspectives to make an impact, saying that the major regulatory frameworks of the post-crisis era have now been finalised, but the change in the financial sector is still ongoing. In the era of globalisation and digitalisation, he argues, this will even gain momentum. As a result, supervisors and regulators are faced with ever more complex questions and are being led beyond the traditional fields of law and economics into new areas, such as information technology.

"In such a complex and interconnected environment, we need an even greater exchange of information regarding fundamental issues in supervision and regulation with representatives of the financial sector and their industry associations, in addition to consumer protection organisations, experts from academia, journalists and, of course, politicians." The articles in BaFinPerspectives are intended to bring strategic issues and regulatory projects into the spotlight and to analyse them from different points of view, beyond daily reporting.

## **6 Combating money laundering**

### **6.1 "Upward potential" in the fight against money laundering**

In his speech at BaFin's New Year press reception in January 2019, BaFin President Felix Hufeld emphasised once again how seriously BaFin takes the issue of money laundering prevention: "For me, (it) is an urgent priority, and I would like it to be evident from the way that all institutions conduct business that it is a very high priority for them, too."

Chief Executive Director Dr Thorsten Pötzsch believes that there is "upward potential" in the fight against money laundering. "Some institutions can certainly do better here", he explained in an interview. Banks had to recognise that successful money laundering prevention comes with a price tag, he said. Pötzsch stressed that he wants all banks to realise, not least in their own interest, the importance of preventing money laundering and terrorist financing. He pointed out that cases of money laundering are a problem for banks in many respects:

"They can lead to financial penalties such as fines.

Banking supervisors can impose higher minimum capital ratios on banks. And these kinds of scandals can cause massive reputational damage to banks and even lead to situations where their continued existence is under threat."

### **6.2 Deutsche Bank**

#### **Special representative appointed**

On 21 September 2018, BaFin appointed a special representative for money laundering prevention at Deutsche Bank AG – for the first time ever. To prevent money laundering and terrorist financing, BaFin ordered the bank to take appropriate internal safeguards in selected areas and to comply with general due diligence obligations. It appointed the auditing firm KPMG as special representative to monitor compliance with the order. Chief Executive Director Dr Thorsten Pötzsch commented on this in the above-mentioned interview: "It was good and proper to employ the instrument of the special representative, which had been dormant until then. I am confident that, in cooperation with the bank and our organisation, the special representative will bring about significant improvements in money laundering prevention."

#### **Mandate expanded**

On 15 February 2019, BaFin ordered Deutsche Bank to review and – where necessary – adjust its group-wide risk management processes in the area of correspondent banking. In order to monitor the implementation of this measure, BaFin expanded the mandate of the special representative, who is to report on and assess the progress of implementation.

### **6.3 Money laundering prevention in correspondent banking relationships**

Under the heading "Danske Bank", the media reported on a money laundering scandal. Between 2007 and 2015, an Estonian branch of Danske Bank A/S, Copenhagen, is said to have laundered amounts running into several billion for customers resident outside Estonia. The media reports also highlighted German banks that had correspondent banking relationships with Danske Bank in Estonia.

BaFin investigated to what extent transactions were in fact executed via German banks and whether these point to shortcomings in money laundering prevention, especially with regard to the general requirements for correspondent banking relationships. BaFin is in constant contact with both the competent German

prosecuting authorities and a number of foreign supervisory authorities. In 2019, one of the priority areas will be a review of the requirements under anti-money laundering legislation for the correspondent banking business in banks with international operations.

#### 6.4 BaFin's role in money laundering prevention

In his speech in January 2019, President Hufeld underlined once again that it is not BaFin's job to investigate and prosecute suspected cases of money laundering. That task lies in the hands of the law enforcement agencies, which is why they have access to other sources of information and are able to use police resources and investigation methods, he said.

BaFin plays a different role, Hufeld explained: it has to ensure that institutions have appropriate systems for money laundering prevention in place and that these at least comply with the legal requirements. If BaFin finds that that is not the case at an undertaking, it intervenes

and requires that the procedures be changed. But that is not enough, according to Hufeld: "Better coordination is needed in Europe", he pointed out and emphatically welcomed the steps that have been taken so far in this respect.

Hufeld stressed that both the banking supervisory level and the level of the Financial Intelligence Unit (FIU)<sup>5</sup> and the law enforcement agencies have to be taken into account in this context. All possibilities for managing risk need to be applied, combined with the latest technologies, to achieve the best prevention possible, he maintained. "That occasional misuse cannot be ruled out even with the best prevention methods, and that substantial amounts of money flow outside of the financial system, does not, of course, justify failing to put the greatest amount of effort possible into preventing money laundering."

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<sup>5</sup> FIU is commonly used internationally to refer to the German Financial Intelligence Unit (*Zentralstelle für Finanztransaktionsuntersuchungen*).

## 7 Timeline of important events in 2018

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January	<ul style="list-style-type: none"><li>▪ BaFin becomes the <b>national resolution authority</b> in Germany on 1 January 2018. The legal basis is the German Recovery and Resolution Act (<i>Sanierungs- und Abwicklungsgesetz</i>).</li><li>▪ The European <b>PRIIPs Regulation</b> enters into force on 1 January 2018. It requires manufacturers of packaged retail and insurance-based investment products (PRIIPs) to publish a three-page key information document (KID) for these products.</li><li>▪ BaFin repeals the <b>Country Risk Regulation</b> with effect from 1 January 2018.</li><li>▪ The German Regulation Governing Large Exposures and Loans of 1 Million Euros or More (<i>Großkredit- und Millionenkreditverordnung</i>) is updated by means of an amending regulation, which enters into force on 1 January 2018.</li><li>▪ The provisions of the second Markets in Financial Instruments Directive (<b>MiFID II</b>) apply as from 3 January 2018. In Germany, MiFID II is implemented by way of the Second Act Amending Financial Markets Regulations (<i>Zweites Finanzmarktnovellierungsgesetz</i>), large parts of which also enter into force on 3 January 2018.</li><li>▪ Since 3 January 2018, the Market Abuse Regulation (<b>MAR</b>) has required issuers whose financial instruments are listed, with their consent or approval, on an organised trading facility (OTF) to publish, without delay, any inside information directly relating to those issuers.</li><li>▪ As from 3 January 2018, new requirements apply to securities trading firms and banks when they apply to BaFin for a <b>business authorisation</b>.</li><li>▪ The new German Payment Services Supervision Act (<i>Zahlungsdiensteaufsichtsgesetz</i>) enters into force on 13 January 2018.</li><li>▪ On 18 January 2018, BaFin publishes an interpretative decision on the requirements of the European Capital Requirements Regulation (CRR) for reviewing <b>property valuations</b>.</li></ul>
February	<ul style="list-style-type: none"><li>▪ On 8 February 2018, BaFin imposes a ban on disposals and payments by <b>Dero Bank AG</b> because of a risk of excessive balance sheet leverage and orders the bank to be closed for business with customers. Payments not intended for the fulfilment of debt to Dero Bank AG must not be accepted (moratorium).</li><li>▪ BaFin publishes an advisory letter on 20 February 2018 on the regulatory classification of tokens and virtual currencies underlying initial coin offerings (<b>ICOs</b>).</li><li>▪ On 20 February 2018, BaFin publishes a Circular on the <b>solvency of financial conglomerates</b>.</li><li>▪ The German Act Implementing the Insurance Distribution Directive (<i>Gesetz zur Umsetzung der Versicherungsvertriebsrichtlinie</i>) enters into force on 23 February 2018.</li></ul>
March	<ul style="list-style-type: none"><li>▪ On 8 March 2018, the European Commission presents its proposal for a European <b>Crowdfunding Regulation</b>, which is intended to create a common European regulatory framework for crowdfunding.</li><li>▪ Also on 8 March 2018, the European Commission unveils its <b>FinTech Action Plan</b>. This is meant to help the financial sector to harness the opportunities of technology-enabled innovation in the provision of financial services.</li><li>▪ BaFin determines that a compensation event has occurred at <b>Dero Bank AG</b> on 14 March 2018. The institution is no longer able to repay all deposits.</li><li>▪ The first <b>authorisation procedure</b> in connection with <b>Brexit</b> is successfully completed.</li></ul>
April	<ul style="list-style-type: none"><li>▪ The takeover bid of <b>E.ON Verwaltungs SE</b>, Düsseldorf, to the shareholders of <b>innogy SE</b>, Essen, which has a transaction volume of approximately €21bn, is the year's largest takeover bid by transaction volume.</li><li>▪ BaFin imposes a turnover-based <b>administrative fine</b> of €1.34m relating to a breach of a credit institution's supervisory duty in relation to voting rights notifications.</li><li>▪ On 19 April 2018, BaFin publishes the new version of its Circular entitled Minimum Requirements for the Compliance Function (<i>Mindestanforderungen an die Compliance-Funktion – MaComp</i>).</li><li>▪ BaFin issues notices on the <b>bank levy</b>.</li></ul>

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May	<ul style="list-style-type: none"> <li>▪ On 4 May 2018, BaFin publishes „Circular 6/2018 (BA and WA) on the minimum requirements for <b>complaints management</b>“.</li> <li>▪ BaFin and the Deutsche Bundesbank define their <b>annual priority areas</b> in banking supervision. In 2018, banking supervision focuses mainly on profitability and interest rate risks as well as on the banks' lack of appropriate and secure IT systems.</li> <li>▪ The European Commission publishes a number of proposals for <b>sustainable finance</b> on 24 May 2018. Their core element is the proposal for a unified classification system of sustainable economic activities in the European Union (EU).</li> <li>▪ In Guidelines published on 24 May 2018, BaFin announces its criteria and standards for the supervisory assessment of banks' internal <b>capital adequacy concepts</b>.</li> </ul>
June	<ul style="list-style-type: none"> <li>▪ The product intervention measures adopted by the European Securities and Markets Authority (ESMA) in May in relation to <b>binary options</b> and contracts for difference (<b>CFDs</b>) are published in the Official Journal of the EU on 1 June 2018. The distribution and sale of binary options to retail investors are prohibited as from 2 July 2018.</li> <li>▪ BaFin issues <b>the first MREL decisions</b>.</li> <li>▪ On 15 June 2018, BaFin publishes its study entitled „Big data meets artificial intelligence – Challenges and implications for the supervision and regulation of financial services“, prepared in cooperation with PD – Berater der öffentlichen Hand GmbH, Boston Consulting Group GmbH and the Fraunhofer Institute for Intelligent Analysis and Information Systems (IAIS).</li> <li>▪ On 27 June 2018, the Financial Stability Committee (<i>Ausschuss für Finanzstabilität</i>) presents its fifth report on <b>financial stability in Germany</b> to the German Bundestag; the report deals with issues such as risks in the property market and cyber risks.</li> <li>▪ The Federal Ministry of Finance (<i>Bundesministerium der Finanzen</i>) publishes the evaluation report on the review of the effectiveness of the Life Insurance Reform Act (<i>Lebensversicherungsreformgesetz</i>) on 28 June 2018.</li> <li>▪ BaFin revises the guidance for calculating the effects of a sudden, unexpected change in interest rates (Basel standard shock) in „Circular 9/2018 (BA) <b>Interest rate risk in the banking book</b>“.</li> </ul>
July	<ul style="list-style-type: none"> <li>▪ On 2 July 2018, BaFin publishes a Circular on the Supervisory Requirements for IT in Insurance Undertakings (<i>Versicherungsaufsichtliche Anforderungen an die IT – VAIT</i>).</li> <li>▪ The Second Regulation Amending the Financial and Internal Capital Adequacy Information Regulation (<i>Zweite Verordnung zur Änderung der Finanz- und Risikotragfähigkeitsinformationenverordnung</i>) enters into force on 13 July 2018.</li> <li>▪ In the period from 16 July to 30 September 2018, BaFin holds a consultation on the report on the study entitled „<b>Big data meets artificial intelligence</b> – Challenges and implications for the supervision and regulation of financial services“.</li> <li>▪ On 17 July 2018, BaFin publishes Circular 11/2018 (VA), which contains information on <b>cooperation with insurance intermediaries</b> and on risk management in distribution.</li> <li>▪ On 20 July 2018, BaFin submits Circular 13/2018 for consultation, which deals with the issue of when customers should be combined into a „<b>group of connected clients</b>“ as a result of interconnectedness.</li> <li>▪ Also on 20 July 2018, BaFin circulates a draft Circular on the <b>disclosure of the liquidity coverage ratio</b>.</li> <li>▪ On 21 July 2018, part of the Act Exercising Options of the <b>EU Prospectus Regulation</b> and Amending Other Financial Market Laws (<i>Gesetz zur Ausübung von Optionen der EU-Prospektverordnung und zur Anpassung weiterer Finanzmarktgesetze</i>) enters into force. At the same time, certain provisions of the Prospectus Regulation enter into effect.</li> <li>▪ In the period from 31 July to 30 October 2018, the International Association of Insurance Supervisors (IAIS) holds consultations on the <b>Insurance Capital Standard 2.0 (ICS 2.0)</b>.</li> </ul>

August	<ul style="list-style-type: none"> <li>▪ The first issue of a new series of publications, „BaFinPerspectives“, appears on 1 August 2018. The issue’s main focus is on digitalisation.</li> <li>▪ On 28 August 2018, the European Commission invites comments on <b>sustainability in Solvency II</b> from the European Insurance and Occupational Pensions Authority (EIOPA).</li> </ul>
September	<ul style="list-style-type: none"> <li>▪ BaFin submits for consultation a draft regulation amending section 16 of the Solvency Regulation (<i>Solvabilitätsverordnung</i>), which deals with the materiality threshold.</li> <li>▪ On 27 September 2018, BaFin holds its conference on <b>IT Supervision in the Banking Sector</b> in Frankfurt am Main, where it is host to approximately 400 representatives of the finance industry and IT security experts.</li> </ul>
October	<ul style="list-style-type: none"> <li>▪ The <b>Insurance Distribution Directive</b> (IDD) applies in all EU member states as from 1 October 2018.</li> <li>▪ The Third Regulation Amending Regulations under the Insurance Supervision Act (<i>Dritte Verordnung zur Änderung von Verordnungen nach dem Versicherungsaufsichtsgesetz</i>) is promulgated in the Federal Law Gazette on 22 October 2018 and enters into force on 23 October 2018. The regulation represents the Federal Ministry of Finance’s amendment of the rules governing the additional interest provisions (<b>Zinszusatzreserve</b>).</li> <li>▪ Amendments to the German <b>Securities Trading Reporting Regulation</b> (<i>Wertpapierhandelsanzeigeverordnung</i>) and to the German <b>Voting Rights Notification Regulation</b> (<i>Stimmrechtsmitteilungsverordnung</i>) enter into force on 30 October 2018.</li> <li>▪ BaFin publishes „Circular 13/2018 on implicit credit support for <b>securitisation transactions</b>“.</li> </ul>
November	<ul style="list-style-type: none"> <li>▪ The European Banking Authority (EBA) publishes the results of the EU-wide bank stress test on its website on 2 November 2018. The stress test, which was coordinated by the EBA, subjected the 48 largest institutions in Europe to a macroeconomic stress scenario. 33 of the institutions that were tested are subject to the Single Supervisory Mechanism (SSM), and 8 of these SSM banks are German credit institutions. The tested institutions account for approximately 70% of all bank assets in the eurozone.</li> <li>▪ The Council of the European Central Bank (ECB) nominates <b>Andrea Enria</b> as the new Chair of the Supervisory Board on 7 November 2018. His appointment by the European Council followed on 6 December 2018. He assumes office on 1 January 2019.</li> <li>▪ On 8 November 2018, BaFin publishes a Guidance Notice with guidance on <b>outsourcing to cloud service providers</b>.</li> <li>▪ On 14 November 2018, the IAIS publishes a consultation paper on the <b>Holistic Framework</b>, which enhances and supplements the existing framework for systemically important insurance groups (G-SIIs).</li> <li>▪ The <b>bank levy</b> specialised procedure, which undertakings can use to submit their reporting data on the bank levy electronically, is available for the first time on BaFin’s reporting and publishing platform.</li> <li>▪ On 27 November 2018, two constitutional complaints are brought before the Federal Constitutional Court (<i>Bundesverfassungsgericht</i>). The complaints are essentially directed against the two regulations on the <b>SSM</b> and the Single Resolution Mechanism (<b>SRM</b>).</li> </ul>
December	<ul style="list-style-type: none"> <li>▪ On 14 December 2018, EIOPA publishes the report on the <b>Europe-wide stress test for insurance groups</b>.</li> <li>▪ For the purpose of a public hearing, BaFin publishes a draft national product intervention measure relating to contracts for difference on 20 December 2018.</li> <li>▪ On 21 December 2018, EIOPA publishes the third report on the impact of <b>long-term guarantee</b> measures and of measures on equity risk under Solvency II.</li> <li>▪ The Act Implementing the <b>IORP II Directive</b> (<i>Gesetz zur Umsetzung der EbAV-II-Richtlinie</i>) is promulgated in the Federal Law Gazette. The new provisions governing the activities and supervision of institutions for occupational retirement provision (IORPs) come into effect in 2019.</li> </ul>



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- The Regulation Implementing the Insurance Distribution Directive (**IDD**) (*Verordnung zur Umsetzung der Versicherungsvertriebsrichtlinie*) enters into force as at 21 December 2018.
  - On 21 December 2018, BaFin publishes the Guidance Notice on the contractual recognition of the temporary suspension of termination rights in accordance with section 60a of the Recovery and Resolution Act (*Sanierungs- und Abwicklungsgesetz*), which it had circulated for consultation in the summer.
  - BaFin sends out a survey to selected banks to assess the nature of German banks' involvement in trading or issuing American Depositary Receipts (**ADRs**).
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# II

## Integrated supervision





## 1 Brexit

**B**y 31 March 2019<sup>1</sup>, there was still no clarity about the date or the terms of the United Kingdom's (UK) departure from the European Union (EU). The UK had originally been scheduled to leave the EU in the night from 29 to 30 March 2019. On 29 March 2019, the British House of Commons again rejected the agreement Prime Minister Theresa May had negotiated with the EU. The alternatives then facing the UK were its departure from the EU without a deal on 12 April 2019 or a lengthy delay to Brexit, which would require the country to take part in European elections at the end of May.

The persisting uncertainty until the last minute has posed considerable challenges for policymakers and supervisory authorities and necessitated preparations to be made also for a no-deal scenario. A disorderly exit by the UK from the EU could potentially give rise to significant risks. In the financial sector, this could mean that companies from the UK that have in the past notified BaFin of the cross-border conduct of banking business or insurance business or of the provision of financial services under European passporting rules would lose this right to market access.

However, many of the cross-border arrangements entered into before Brexit under European passporting rights are such that their obligations and effects will in some cases continue far beyond the leaving date. In the case of derivatives, for example, this applies to a large number of contracts with very large transaction volumes. What is more, long-term agreements in particular do not contain any special provisions for Brexit.

An issue of huge importance for companies, supervisory authorities and policymakers is how Brexit will affect future mutual market access in dealings between the UK and the remaining 27 member states of the EU. Just under half of the UK's total exports go to the EU, making it the UK's largest export market; looking at imports shows a similar picture. The situation in the financial sector is even more complex: not only is London a central hub for capital flows towards the EU, it is also a key clearing venue, which is used to settle approximately 90% of all euro-denominated interest rate swaps, for example.<sup>2</sup>

BaFin continued its active dialogue with interested companies in 2018 and again organised Brexit workshops, as in the previous year. BaFin has to date held discussions with over 200 companies in order to give them clarity, support and, above all, a reliable

<sup>1</sup> The time of going to press was 31 March 2019.

<sup>2</sup> See chapter VI 2.1.6.1.

framework that allows them to continue to provide financial services under the new political conditions. In this process, there must be assurances, of course, that all companies are supervised and regulated in accordance with the same standards.

Scores of banks and financial services institutions based in the UK are intending to move their offices to Germany and other countries because Brexit will mean that they will lose their European passporting rights that allow them to conduct business in the member states of the European Economic Area (EEA). BaFin and the federal government aim to provide these institutions with guidance for their projects in Germany, offer them legal certainty and, at the same time, ensure the stability of the German financial market. In this context, solutions at a European level are not only desirable, but an urgent necessity for some subsets, such as clearing. If solutions are not implemented, banks that continue to provide clearing services in the UK are at risk of a massive increase in capital requirements. In addition, derivative positions would have to be reallocated, i.e. revised and in some cases reconstituted. To prevent this from happening, the European Commission in December adopted an implementing decision determining temporary EMIR<sup>3</sup> equivalence for the UK in case of a no-deal scenario. In concrete terms, this means that the UK's regulations will be considered equivalent to EU regulations, and central counterparties (CCPs), with approval from the European Securities and Markets Authority (ESMA), will be able to continue their activities in the European Union as before for a limited period of one year.

The German Tax Act relating to Brexit (*Brexit-Steuerbegleitgesetz*) gives BaFin access to fast-acting tools with legal certainty. It is intended to mitigate or prevent the negative consequences for the functioning or stability of the financial markets in case of a disorderly exit because it allows BaFin to permit UK companies for a transitional period to continue using the European passporting rules for a branch or to provide cross-border services in Germany.

### Internal models

Many of the companies requested permission from BaFin for using their internal models to determine their capital requirements also in Germany. BaFin, together with the Deutsche Bundesbank and in accordance with the framework set out by the European Central Bank (ECB), has offered a two-stage approval process for this purpose:

- Stage 1: Temporary toleration of the internal models approved by the Prudential Regulation Authority (PRA) on the basis of European requirements
- Stage 2: Regular model approval based on a subsequent in-depth on-site inspection

In 2018, nine institutions with international operations applied for permission to use their internal models for market, counterparty and credit risk. BaFin granted temporary toleration to most of the models to which the applications related. It also began to examine the counterparty risk models of two of the institutions, a process it is continuing in 2019. The reviews will form the basis of decisions on regular model approvals.

## 2 Consumer protection

### 2.1 MiFID II – one year on

#### 2.1.1 Positive result overall

The Markets in Financial Instruments Directive (MiFID II)<sup>4</sup> brought about significant changes to conduct regulation in the German Securities Trading Act (*Wertpapierhandelsgesetz*).<sup>5</sup> Extensive changes were required specifically in the business that investment firms conduct with retail clients.

The institutions therefore began their preparations for MiFID II long before it entered into force. Given the extent of the implementation project and the fact that MiFID II was not the only major regulatory package that had to be implemented at the beginning of January 2018, BaFin concluded on the basis of its market surveys on MiFID II that the first year under the new regime had delivered positive results overall.

It was hardly surprising that, despite that, a few isolated implementation problems occurred on 3 January 2018. In certain areas, further implementation was required even a year after the new regulations entered into force. However, that did not come as a surprise either, given the extent of the new regulations.

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3 European Market Infrastructure Regulation.

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4 OJ EU L 173/349. MiFID II was implemented by way of the German Second Act Amending Financial Markets Regulations (*Zweites Finanzmarktnovellierungsgesetz*) of 23 June 2017, Federal Law Gazette I, page 1693.

5 For information on MiFID II, see also chapter VI 1.1.

A particular challenge is to develop consistent, workable solutions throughout Europe, which can only be achieved on the basis of continuous, trusting cooperation at the European level. BaFin is therefore in close consultation with other national competent authorities and the European Securities and Markets Authority (ESMA).

## 2.1.2 Market surveys relating to MiFID II

### 2.1.2.1 Market surveys relating to the conduct of business rules of MiFID II

As soon as MiFID II had entered into force, BaFin launched its first market survey questioning credit institutions in relation to the various new conduct of business rules. The aim was to get an early overview of the status of implementation. In the second half of 2018, BaFin extended its survey by adding financial services institutions to the scope as part of a second market survey in order to obtain an overview of the market as a whole.

Both market surveys focused on the record-keeping obligations (taping), the suitability statement and ex-ante cost information, and thus new conduct of business rules that are particularly relevant for consumers. A total of 20 private and foreign banks, 10 savings and cooperative banks from each of the regional associations, as well as 25 financial services institutions and 5 securities trading banks participated in the surveys on a voluntary basis.

The participating institutions deployed significant financial and personnel resources and went to considerable effort to implement the new regulations of MiFID II. This finding was made for the entire market, irrespective of the size or business models of the institutions concerned.

BaFin's first market survey of banks, savings banks and cooperative banks produced the results presented below, which were confirmed in general by the second survey.

#### **Record-keeping obligations**

Since the beginning of 2018, institutions have been required to record telephone conversations and other electronic communication, if they relate to client orders (taping). The first market survey already found that this requirement was being met and that the technical implementation had largely been successful.

Nevertheless, for 20.3% of the telephone records, parts of the conversation that should have been taped had been omitted. In isolated cases, it was noted that a summary of the conversation had been recorded subsequently, which was not sufficient.

At times, clients had responded with unease to the fact that telephone conversations were being recorded, although the survey found that, at 0.12%, the number of objections to this practice turned out very low.

#### **Suitability statement**

After having advised their clients on their investments, investment firms have to explain in writing to what extent their recommendation is suitable for the client – in particular with regard to their investment objectives, the investment period, their risk appetite and ability to bear losses, as well as their knowledge and experience.

Following BaFin's analysis, doubt as to whether the recommendation was suitable for the client remained in only a small number of cases (3.6%). However, the companies' suitability statements rarely documented the full extent of the comparison of the client information against the characteristics of the financial instrument recommended. The error ratio was 89.6%. In many cases, the statements only contained a formulaic statement that the product was suitable, which fell short of requirements.

It should also be highlighted that most institutions had inserted free text fields into the suitability statement to capture the content of the investment advice. This allows individual explanations, which is positive in terms of consumer protection.

#### **Ex-ante cost information**

The rules on ex-ante cost information specify that the costs of securities and investment services must be disclosed to clients in due time. This is intended to make it easier for clients to compare the different products and services and make an informed decision on this basis. The first market survey revealed already that no consistent market standards have established themselves in terms of composition, structure and calculation methods. This means that it remains difficult for clients to compare costs.

A positive aspect was, however, that the cost information used by the institutions related mainly to the specific security involved in the transaction concerned. Most of the institutions had based the cost information also on actual amounts invested, although it is also permissible

to calculate this information on the basis of assumed investment amounts.

A small number of institutions had exclusively provided generic information on costs and charges, indicating costs only on the basis of entire asset classes; this does not comply with the legal requirements. Moreover, this kind of generic information on costs and charges has an above-average error ratio.

The sample-based analysis of the information on costs and charges also revealed weaknesses with regard to their completeness and mathematical accuracy: there was evidence across the entire sample obtained that legally required cost elements had not been included in some cases. In addition, 13% of the samples taken showed significant variances between the amounts in the information on costs and charges and those in the securities statement.

### 2.1.2.2 Market survey in relation to product governance under MiFID II

A third market survey, also conducted in the second half of 2018, was dedicated to the new product governance requirements under MiFID II. 55 institutions, including 25 financial services institutions, 5 securities trading banks and 25 banks and savings banks, were asked to provide information on the status of implementation. This involved BaFin investigating the institutions' processes in their role as manufacturers and distributors – based on a sample of 187 transactions in total.

#### **Implementation largely successful**

This third market survey showed that the product governance requirements had largely been implemented successfully. Most of the institutions based their implementation firstly on the ESMA Guidelines on MiFID II product governance requirements and the Minimum Requirements for the Compliance Function and the Additional Requirements Governing Rules of Conduct, Organisation and Transparency (MaComp) (BT 5)<sup>6</sup>.

Secondly, the institutions were able to base the determination of the target market for securities on the Common Standard of the German Banking Industry Committee (*Deutsche Kreditwirtschaft*), the

German Investment Funds Association (*Bundesverband Investment und Asset Management*) and the *Deutscher Derivate Verband* (German Derivatives Association). This standard makes the process of identifying the target market, which is done by the manufacturers, as well as the process of defining the target market and matching the client to the target market, which are done by distributors, easier. The standard format allows smooth communication between manufacturers and distributors. In addition, it enables the information on the target market to be integrated into the WM Datenservice's database, which is used by a large number of institutions.

#### **Details on some target market categories require improvement**

The survey revealed that the determination and identification of target markets is working well, thanks to standardisation. In individual cases, the statements made in relation to certain target market categories were in need of improvement: for example, many samples across all classes of financial instruments indicated that the client's investment objectives had been specified as "asset accumulation or optimisation". BaFin would have preferred greater differentiation for some of these products. However, BaFin expects that the determination of the target market will increasingly take shape as time progresses. For example, there are indications that the European Commission's sustainability initiative is expected to have an effect on the individual criteria of the target market, especially the client's investment objectives.

#### **Dealing with the negative target market**

BaFin will closely monitor how the negative target market will be dealt with in future and how the principle of proportionality will be implemented: only a minute number of manufacturers and asset managers for investment strategies had identified a negative target market for their products. In addition, in a small number of cases, it was not apparent that – for particularly high-risk, complex or illiquid products – manufacturers and distributors had applied a higher level of care in implementing the product governance processes than for other products, although they are required by law to do so.

#### **New processes pose a challenge for all institutions**

The market survey on the new product governance requirements under MiFID II revealed that smaller institutions are finding it increasingly difficult to meet complex and extensive regulatory requirements in addition to carrying on their day-to-day business. By contrast, the larger firms considered it challenging

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<sup>6</sup> Circular 5/2018 (WA) – Minimum Requirements for the Compliance Function and Additional Requirements Governing Rules of Conduct, Organisation and Transparency – MaComp.

to integrate the new processes within the framework of existing workflows, for example the new product process in accordance with the Minimum Requirements for Risk Management (*Mindestanforderungen an das Risikomanagement* – MaRisk) without losing sight of the new processes. To counter those trends, BaFin will work towards relevant guidance documents – such as ESMA’s product governance guidelines at the European level – and offer assistance at the national level, for example through MaComp.

## 2.2 PRIIPs Regulation – one year on

### 2.2.1 Current status and outlook

#### **PRIIPs Regulation has been applicable since the beginning of 2018**

Under the European PRIIPs Regulation<sup>7</sup>, manufacturers of packaged retail and insurance-based investment products (PRIIPs) have been required to publish a three-page key information document for these products since 1 January 2018. Anyone who sells, or gives advice on, such products will have to provide retail investors with a key information document before they commit themselves by a binding contract or offer.

The requirements of the PRIIPs Regulation relating to the form and content of this key information document are set out in the relevant delegated regulation<sup>8</sup>. In addition, since 2017, the Joint Committee of the European Supervisory Authorities (ESAs) has made available interpretive guidance in the form of questions and answers (Q&As) and flowcharts. Some aspects of these documents have since been amended by the Committee, most recently in July 2018.<sup>9</sup>

#### **Risk-based market supervision**

BaFin is responsible for monitoring compliance with the PRIIPs Regulation on the basis of risk-based supervision of impropriety. If it receives information on potential violations of the PRIIPs Regulation, it investigates them. In addition, it regularly takes samples and conducts market investigations. The first market investigation took place at the beginning of 2018.<sup>10</sup> Moreover, BaFin has begun to examine the use of methods for calculating individual actuarial disclosures in the key information documents.

#### **Open questions relating to scope**

There is still some uncertainty about the substantive scope of the PRIIPs Regulation. For example, it has not been conclusively clarified which features lead to a corporate bond being classified as a PRIIP. The European Commission delegated the decision on whether a product falls within the scope of the PRIIPs Regulation to the PRIIP manufacturers themselves<sup>11</sup> while making it clear that it applies a broad interpretation. In a letter addressed to the Commission in July 2018, the ESAs explained their understanding of the scope and asked the Commission to confirm this interpretation.<sup>12</sup> No reply had been received at the time of going to press<sup>13</sup>.

#### **Lack of comprehensibility**

In the opinion of consumer protection bodies, market participants and EU supervisory authorities, some disclosures required to be included in the key information documents under the PRIIPs Regulation, such as the presentation of the expected performance of the product (performance scenarios) or of the costs, are not comprehensible to retail investors. BaFin is therefore campaigning for this and other shortcomings to be rectified when the PRIIPs regime undergoes a comprehensive revision.

#### **Revision of Delegated Regulation**

In November 2018, the ESAs launched a consultation process for revising certain aspects of the Delegated Regulation<sup>14</sup>. The original aim was to facilitate the transition from product information to the key information document as at 1 January 2020.<sup>15</sup> This relates to UCITS funds<sup>16</sup> and alternative investment funds (AIFs), whose providers are still issuing “key investor information” documents. Now that key investor information documents are to be used for another two years, i.e. until 31 December 2021, the revision of the Delegated Regulation is expected to take the whole of 2019. In terms of content, detailed attention is to be given to the method and presentation of the performance of a PRIIP investment product, the calculation of transaction costs and issues relating to

<sup>7</sup> Regulation (EU) No 1286/2014, OJ EU L 352/1.

<sup>8</sup> Delegated Regulation (EU) No 2017/653, OJ L 100/1.

<sup>9</sup> Questions and Answers (Q&A) on the PRIIPs Key Information Document (KID) of 19 July 2018, doc. no JC 2017 49.

<sup>10</sup> See 2.2.2.

<sup>11</sup> Guideline No 5 of Commission Communication of 7 July 2017, OJ EU C 218/11.

<sup>12</sup> Letter of 19 July 2018, doc. no JC 2018 21.

<sup>13</sup> As at the time of going to press, 31 March 2019.

<sup>14</sup> Delegated Regulation (EU) No 2017/653, OJ L 100/1.

<sup>15</sup> See BaFinJournal November 2018, page 19 (only available in German).

<sup>16</sup> UCITS funds are funds that meet the requirements of the UCITS Directive (Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)).

the presentation of PRIIP insurance-based investment products with a range of investment options.

## 2.2.2 Market investigation into key information documents under the PRIIPs Regulation

To launch its supervision of compliance with the provisions of the PRIIPs Regulation, BaFin conducted a market investigation at the beginning of 2018. The first step was to identify just over 100 German undertakings and institutions that manufacture PRIIPs. The market investigation found that several of these PRIIP manufacturers had not met their obligation to publish key information documents, or had not met this obligation in full.

Some manufacturers responded to queries by BaFin by saying that they had initially had technical problems in providing the key information documents, but had soon been able to rectify them. Other manufacturers were found to have outdated websites. They had ceased to provide certain products as from 1 January 2018, and this meant that they were under no obligation to publish a key information document. Some PRIIP manufacturers had published the required key information documents in a hidden area of their website or in a section that was not freely accessible. BaFin informed these manufacturers that they had to make the key information documents available in a publicly accessible area of their website.

In the course of the market investigation, BaFin also examined key information documents of various PRIIP manufacturers on a sample basis. BaFin noted a number of shortcomings in this process, which the PRIIP manufacturers subsequently rectified. For example, they had failed to highlight the obligatory warnings in the key information documents or referred to documents that retail investors could not locate on the PRIIP manufacturer's website, or only with difficulty, without seeking assistance.

## 2.3 Market survey on indicative order value calculations

The market survey on indicative order value calculations conducted in 2018 looked into cases where the price indicated by online brokerage tools for the purchase of a security (indicative order value) varied significantly from the actual settlement price. Unlimited buy orders for securities trading at less than €1.00 face the risk that, to the detriment of the investor, the actual settlement price may be considerably higher. The survey

of providers of investment services showed that, for the most part, online brokerage tools do not use the current bid and ask prices to calculate indicative order values, although those prices reflect the current market situation. What is more, bid and ask prices provide the best possible basis for calculating indicative order values, because investors are shown a realistic order value in this way.

### Risk for investors

If, however, the calculation of the indicative order value is based on the last available exchange or market price, this may be a price determined without any actual turnover in the security concerned. If no trades are executed because the supply and demand situation does not permit this, a price without turnover (PWT) is determined for the information of trading participants. This price is based on the buy side of a quote, i.e. the bid price, and reflects the price at which investors can sell securities. For securities in low demand, it is often in the range of thousandths of a euro. The ask price, which is relevant if an investor is interested in buying, is often different from the bid price. This results in investors placing securities orders that they would not have placed if they had known the actual price; they are ultimately confronted with demands for buy prices they are unable to pay.

These types of situations, which mainly occur when buying securities trading below €1.00, can, however, be avoided by limiting the buy orders for securities. Since not all providers of investment services make limit orders mandatory, this safety mechanism cannot always protect the investor from these kinds of problems when buy orders are executed. For this reason, investors should set their own buy limits.<sup>17</sup> Future investigations will show whether the insights and recommended actions have contributed to improving the situation.

## 2.4 Consumer complaints and enquiries

### 2.4.1 Credit institutions and financial services providers

In 2018, BaFin processed a total of 5,791 submissions relating to credit and financial services institutions (previous year: 5,587 submissions), of which 5,539 were complaints and 252 general enquiries. The figure includes 25 cases where BaFin issued statements to the

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<sup>17</sup> See BaFinJournal September 2018, page 22 ff. (only available in German).



Petitions Committee of the Bundestag (the lower house of the German parliament). In addition, BaFin received 46 information requests about former banks, and especially their legal successors. The complaints were upheld in 771 cases, including 1 petition.

**Table 1: Complaints by group of institutions**

Group of institutions	Total number of submissions
Private banks	2,998
Savings banks	721
Public-sector banks	135
Cooperative banks	677
Mortgage banks	5
<i>Bausparkassen</i>	413
Financial services providers (e.g. leasing and factoring undertakings, etc.)	175
Foreign banks	415

The submissions made by consumers reflected the entire range of products offered by the institutions and undertakings subject to supervision in the year under review. They related in particular to the current account and to bank transfers or payment transactions. But BaFin also received queries regarding the termination of a business relationship, cancelling long-term savings schemes as well as general enquiries about whether and in what amounts certain fees are permitted.

When branches were closed, concern was expressed, especially by older consumers from rural areas, about their future access to the necessary financial services. Customers of online banks complained to BaFin in many instances about poor accessibility during technical problems or about having had to accept inappropriately long response or processing times for requests or complaints.

Consumers reacted particularly sensitively to attempts by banks to change the general terms and conditions – be it to bring them in line with changes to the legal framework or because they had redesigned their product offering. This applied especially where such amendments had the effect of changing the service offering or where the bank introduced or increased fees. Although BaFin cannot influence the nature of the product offering, it can – under its mandate for collective consumer protection – examine whether banks comply with the legal requirements when implementing such contract amendments.

An investigation conducted by BaFin on a sample basis found that the procedure used by the institutions had generally complied with the legal requirements. In most cases, for instance, the banks had notified customers of the intended amendments at least two months before they took effect. Furthermore, the banks advised their customers that they had the right, under section 675g (2) sentence 3 of the German Civil Code (*Bürgerliches Gesetzbuch*), to terminate their contract free of charge and with immediate effect.

Customers who receive a proposal from their bank to amend an existing payment services master agreement should always examine carefully whether they want to continue the contract under the amended terms and conditions. If not, they should review the products of other providers and consider switching to a different account. Although consumers can object to the proposed amendments, this will often not have the effect of indefinitely continuing the contract under unchanged terms and conditions: in most cases, the institutions will resort to terminating the contract by giving statutory notice.

## 2.4.2 Investment and asset management companies

As part of investment supervision, a total of 125 complaints and queries were received from consumers in 2018. They related to the investment tax reform, amendments to fund rules and the requirement on asset management companies to provide information to investors. Queries from investors about open-ended real estate funds mostly related to the liquidation of open-ended real estate funds for retail investors.

BaFin investigated the reports and invited comments from the supervised undertakings. It also explained the legal framework to the complainants, pointing out alternative ways of dispute resolution. There was rarely any need to take further supervisory measures.

## 2.4.3 Insurance undertakings

In 2018, BaFin completed the handling of a total of 8,097 submissions relating to insurance undertakings (previous year: 7,367 submissions). 33.3% (previous year: 32.0%) of these submissions ended in success for the parties that made them.

7,906 submissions (previous year: 7,212 submissions) were attributable to the insurance classes mentioned in Table 2 “Submissions received by insurance class since 2014” on page 42. This included 7,325 complaints,

**Table 2: Submissions received by insurance class since 2014**

Year	Life	Motor	Health	Accident	Liability	Legal expenses	Building/ contents	Other classes	Miscellaneous*	Total
2018	1,869	1,734	1,653	215	439	666	711	619	191	<b>8,097</b>
2017	1,825	1,508	1,433	219	400	591	603	633	155	<b>7,367</b>
2016	1,817	1,533	1,335	294	460	924	708	759	155	<b>7,985</b>
2015	2,113	1,778	1,267	294	505	722	470	769	1,558	<b>9,746</b>
2014	2,802	1,822	1,545	379	622	675	890	780	1,624	<b>11,139</b>

\* Until 2015: misdirected correspondence, intermediaries, etc.; since 2016: intermediaries

478 general enquiries and 94 petitions, which reached BaFin via the German Bundestag or the Federal Ministry of Finance (*Bundesfinanzministerium*).

The reasons for complaints from consumers vary. The most frequent reasons for complaints in 2018 are presented in Table 3.

**Table 3: Most frequent reasons for complaints in 2018**

Reason	Number
Claims handling process/delays	1,363
Sum insured	892
Issues of coverage	891

A number of complaints related to plans by life insurers to sell policy portfolios, i.e. to run-offs.<sup>18</sup> After the policies had been sold, many policyholders complained about the quality of the customer service. Uncertainty about Brexit was also the subject of a number of queries from consumers. Finally, a number of policyholders approached BaFin in connection with repayment claims based on the court rulings of the Federal Court of Justice (*Bundesgerichtshof*) on the "permanent right to object" in life insurance.<sup>19</sup>

The complaints about health insurers related primarily to premium adjustments made by private health insurers. In this context, consumers sought information about the trustees and their independence required by law<sup>20</sup>.

Many customers also complained to BaFin about the settlement conduct of property and casualty insurers. Consumers also submitted queries about the way motor insurance tariffs are calculated.

#### 2.4.4 Securities business

In 2018, investors filed a total of 676 complaints relating to securities transactions (previous year: 522 complaints) and submitted 396 written enquiries (previous year: 272 enquiries). They related mainly to management or customer service (including safe custody business), order execution, customer information and investment advice.

BaFin recorded a higher incidence of complaints at the beginning of the year. In many of these submissions, fault was found with the fact that some financial instruments could not be traded because there were no data on costs or the target market. Consumers also complained about new regulatory requirements, such as the PRIIPs Regulation and the reform of the German Investment Tax Act (*Investmentsteuergesetz*), which contributed to an increase in the number of complaints in the first quarter of the year under review.

As in the previous year, BaFin received a larger number of complaints about companies domiciled in Cyprus offering cross-border services in 2018. Most of them related to transactions involving financial contracts for difference (CFDs). In these cases, BaFin informs the Cyprus Securities and Exchange Commission, which is the competent authority in the country of origin and therefore responsible for supervising these companies.

#### 2.4.5 Consumer helpline

Citizens can call BaFin's consumer helpline at +49 (0) 800 2 100 500. They made frequent use of this facility in 2018: the consumer helpline advisers dealt

<sup>18</sup> See chapter V 2.6.1.1.

<sup>19</sup> See, among others, BGH judgement of 7 May 2014 – IV ZR 76/11.

<sup>20</sup> See BGH judgement of 19 December 2018 – IV ZR 255/17.

with 18,651 queries (previous year: 19,367 queries) about the financial market, specific issues relevant to consumer protection and problems with banks, insurance undertakings or financial services providers. Of this total, 34.4% was attributable to insurance supervision, 44.6% to banking supervision and 9.91% to securities supervision. Many callers requested information about ways of submitting complaints to BaFin.

## 2.5 Supervision of advice and distribution in the securities business

### 2.5.1 Employee and Complaints Register

The Employee and Complaints Register (see info box on page 44) is a key element in collective consumer protection. BaFin is able to check on the basis of complaints notified to the register whether investment firms are complying with the conduct of business obligations incumbent on them when advising retail clients. Complaints notified in this way allow BaFin to investigate both systematic and sporadic irregularities (such as undue pressure from individual sales employees).

In accordance with legal notification requirements, the complaints notified do not contain any information of their content or on whether the complaints are justified. Regarding complaint tendencies, it is therefore not possible to generalise on the basis of data in the Employee and Complaints Register<sup>21</sup>, but BaFin assesses individual complaints on an ongoing basis. These assessments always focus on whether the investment recommendation provided was in fact suitable for the investor concerned.

If an assessment gives rise to doubts about the expertise or reliability of an employee, or if attention is drawn to employees as a result of violations of supervisory requirements, BaFin will initiate investigations.<sup>22</sup>

<sup>21</sup> For information on objections raised in the securities business, see 2.4.4.

<sup>22</sup> See 2.5.2.

**Table 4: Number of employees<sup>23</sup>**

<b>Employees</b>		
<b>As at</b>	<b>31 Dec. 2017</b>	<b>31 Dec. 2018</b>
Private banks	41,234	37,631
Savings banks/Landesbanks	55,686	52,145
Cooperative banks	38,912	35,829
Financial services institutions	7,000	7,354
<b>Total</b>	<b>142,832</b>	<b>132,959</b>
<b>Investment advisers</b>		
<b>As at</b>	<b>31 Dec. 2017</b>	<b>31 Dec. 2018</b>
Private banks	40,617	37,008
Savings banks/Landesbanks	52,749	49,266
Cooperative banks	36,161	33,115
Financial services institutions	6,443	6,796
<b>Total</b>	<b>135,970</b>	<b>126,185</b>
<b>Sales officers</b>		
<b>As at</b>	<b>31 Dec. 2017</b>	<b>31 Dec. 2018</b>
Private banks	5,903	5,258
Savings banks/Landesbanks	9,196	8,872
Cooperative banks	6,404	6,160
Financial services institutions	370	356
<b>Total</b>	<b>21,873</b>	<b>20,646</b>
<b>Compliance officers</b>		
<b>As at</b>	<b>31 Dec. 2017</b>	<b>31 Dec. 2018</b>
Private banks	107	116
Savings banks/Landesbanks	394	390
Cooperative banks	876	847
Financial services institutions	693	700
<b>Total</b>	<b>2,070</b>	<b>2,053</b>

<sup>23</sup> Since employees may perform multiple activities, the total based on the activities performed exceeds the total number of employees. The dataset changes all the time as amendments and corrections are notified. Employees notified by investment firms that were no longer supervised in accordance with part 11 of the Securities Trading Act (sections 63 et seq.) at the time of the database query are not included. The figures presented here may therefore differ from data published previously.

**Table 5: Number of complaints notified<sup>24</sup>**

Complaints	Private banks	Savings banks/ Landesbanks	Cooperative banks	Financial services institutions	Total
2014	2,381	1,994	1,527	947	<b>6,849</b>
2015	1,546	1,691	1,299	104	<b>4,640</b>
2016	1,633	1,837	1,463	63	<b>4,996</b>
2017	1,298	1,701	1,283	71	<b>4,353</b>
2018	1,592	2,122	1,370	99	<b>5,183</b>

#### Legal background

### Employee and Complaints Register

All institutions which provide investment services are required under section 87 of the Securities Trading Act to report their investment advisers, sales officers and compliance officers, for inclusion in the Employee and Complaints Register maintained by BaFin. In the case of investment advisers, it should be noted that BaFin also receives reports whenever retail clients make a complaint about their investment advice.

## 2.5.2 Measures and administrative fine proceedings

In 2018, BaFin investigated in 35 proceedings any findings that investment advisers and sales officers were unreliable. In 13 of the above proceedings, the employees concerned are not subject to any notification requirements on the basis of their employment with an investment firm. BaFin uses the Employee and Complaints Register to monitor whether the employees in question are again employed as investment advisers or sales officers. In one of the proceedings, BaFin investigated whether an employee had to be prohibited

from working as an investment adviser. The proceedings have not yet been completed.

In 2018, BaFin initiated two warning procedures<sup>25</sup> for violations of requirements and prohibitions pursuant to section 11 of the Securities Trading Act. One of the procedures has not yet been completed; the other was discontinued for discretionary reasons.

In addition, BaFin launched 3 new administrative fine proceedings due to violations of the conduct of business rules and of organisational and transparency requirements applicable to investment firms.<sup>26</sup> It concluded 9 of these proceedings by imposing an administrative fine. A total of 7 proceedings were discontinued, 6 of them for discretionary reasons. A total of 34 proceedings were still pending from the previous year. The highest total administrative fine imposed on an institution in this area was €18,000.<sup>27</sup>

## 2.6 Consumer Advisory Council

BaFin's Consumer Advisory Council<sup>28</sup> was established in 2013. In 2018, the Federal Ministry of Finance appointed new members to 11 of the 12 positions on the Council, because their five-year term of office had expired in the year under review. The Council has three members representing the academic community, four members representing consumer and investor protection organisations, three members who are employees of out-of-court dispute settlement systems as well as one member each representing the Federal Ministry of Justice and Consumer Protection and the trade unions. The member representing the ombudsman of private banks was the only incumbent who was not

<sup>24</sup> The total number of complaints has been adjusted for the number of corrections reported. Complaints notified by investment firms that were no longer supervised in accordance with part 11 of the Securities Trading Act (sections 63 et seq.) at the time of the data query are not included. Moreover, entities can move from one group of institutions to another. Another factor is that – unlike the practice in the reports up to 2015 – the figures were produced on the basis of the respective quarterly totals. As a result, the totals for different reference periods (quarters, years or period as a whole) may vary. The figures presented here may therefore differ from data previously published or published elsewhere.

<sup>25</sup> Section 56 of the German Act on Breaches of Administrative Regulations (*Ordnungswidrigkeitengesetz – OWiG*).

<sup>26</sup> For information on sanctions imposed by the Securities Supervision Directorate, see 4 and chapter VI 2.6.

<sup>27</sup> See 4.

<sup>28</sup> See Appendix, page 171.

replaced, because he had been appointed to the Council as recently as 2016 to succeed a member who had left the Council.

BaFin's Consumer Advisory Council held the first meeting in its new composition on 28 September 2018. From among its members, the Council re-elected Dorothea Mohn from the Federation of German Consumer Organisations (*Verbraucherzentrale Bundesverband e. V.*) as Chair.

The Consumer Advisory Council advises BaFin on the performance of its duties from the perspective of consumers. It is an important source of information for BaFin.

## 2.7 International developments

### 2.7.1 Product intervention

With effect from 3 January 2018, the European Markets in Financial Instruments Regulation (MiFIR) made new product intervention tools available to ESMA and the national competent authorities, i.e. including BaFin. In response, German legislators repealed section 4b of the Securities Trading Act, old version, which had brought forward those powers at the national level. Features of national law – specifically product intervention powers in relation to capital investments – have since then been governed by section 15 of the Securities Trading Act.

ESMA has already made use of the new powers: since 2 July 2018, the marketing, distribution and sale of binary options to retail investors has been prohibited. Since 1 August 2018, CFDs offered to retail investors have been subject to a bundle of measures consisting of leverage limits, automatic loss limits, negative balance protection and an obligation to issue firm-specific risk warnings.

Product intervention measures specified by ESMA are only valid for three months. ESMA has extended the adopted measures, meaning that they remain in force beyond the end of 2018. BaFin has meanwhile made preparations for the expiry of ESMA's measures: in December 2018, it published proposals for measures of its own applicable to binary options and CFDs, which will be valid indefinitely.<sup>29</sup>

<sup>29</sup> See BaFinJournal January 2019, page 33 and BaFinJournal November 2018, page 20 (both only available in German).

### 2.7.2 World Investor Week

The second World Investor Week (WIW), an initiative of the International Organization of Securities Commissions (IOSCO), was held in October 2018. This event was aimed at educating consumers around the world about financial issues. BaFin again took part in the WIW. At the beginning of October 2018, it published two new simple-language documents, which explain important concepts from the banking and insurance sector.<sup>30</sup> During the WIW, BaFin was also represented at the *Börsentag* in Berlin held on 6 October. During the week of events, BaFin experts also informed consumers by video link about "Big Data and Artificial Intelligence" at one of the regular *Digital Stammtische* (get-togethers) hosted by Digital-Kompass.

## 2.8 Dispute resolution

Consumers can approach BaFin's Arbitration Board with applications to resolve disputes with credit institutions and financial services providers, if there is no competent private consumer dispute resolution entity.<sup>31</sup>

## 2.9 Basic payment account and Payment Accounts Act

According to a survey conducted by BaFin as at 30 June 2018, basic payment accounts are offered by approximately 1,300 credit institutions in Germany. Over 566,000 applications for opening basic payment accounts were made between the effective date of the regulations on 18 June 2016 and the date of the survey. Institutions rejected almost 15,000 of these applications. There were a total of 497,000 basic payment accounts as at 30 June.

Approximately 580 consumers contacted BaFin during the period covered by the survey because a bank had rejected their application for opening a basic payment account. BaFin was able to help around 200 of these consumers to open a basic payment account. In those cases, the institutions had refused to open an account without providing a reason recognised under the German Payment Accounts Act (*Zahlungskontengesetz*). In 22 cases, BaFin formally instructed the institution to open a basic payment account.

<sup>30</sup> [www.bafin.de/dok/11529872](http://www.bafin.de/dok/11529872) and [www.bafin.de/dok/11529884](http://www.bafin.de/dok/11529884) (both only available in German).

<sup>31</sup> The activity report of the BaFin Arbitration Board is published at [www.bafin.de/schlichtungsstelle](http://www.bafin.de/schlichtungsstelle) (only available in German).

Between 19 September 2016, when these provisions entered into force, and the survey date, the possibility provided for under the German Payments Account Act to get help with switching accounts was used by consumers on 705,000 occasions. In the same period, customers made complaints about this to BaFin on more than 120 occasions.<sup>32</sup>

### Greater fee transparency

The last part of the Payment Accounts Act entered into force on 31 October 2018. It governs the transparency and comparability of fees for payment accounts: according to its provisions, payment service providers are obliged to provide their customers with standardised fee information that must be easy to understand and easily accessible.<sup>33</sup>

## 3 Market integrity

### 3.1 Authorisation requirement

Germany's banking business, financial services, payment services, e-money business, investment business and insurance business are subject to supervision by BaFin (see info box "Authorisation requirement").

In 2018, BaFin recorded another increase in the number of new authorisation queries it received – from 1,208 to 1,397 queries (see Table 6). They focused primarily on fintech companies, initial coin offerings (ICOs) and new payment services.

**Table 6: New authorisation queries**

	2016	2017	2018
New authorisation queries	1,022	1,208	1,397

### Exemption from the authorisation requirement

Under section 2 (4) of the Banking Act, BaFin can determine in particular circumstances that an institution should be exempted from the authorisation requirement and certain provisions of ongoing supervision (see Table 7 on page 47). This exemption is only valid for as long as the institution does not require supervision due to the type of business it conducts. Exemptions granted to third-country institutions may only be granted if BaFin does not also have to supervise that institution's domestic business because it is supervised in its home country. Section 2 (5) of the Banking Act provides specific guidance for such cases.

#### Legal background

### Authorisation requirement

BaFin's responsibilities include examining the business of new market participants or new business models of established providers to determine whether they require authorisation under supervisory laws. Providers conducting banking business or providing financial services under the German Banking Act (*Kreditwesengesetz*), conducting insurance business under the German Insurance Supervision Act (*Versicherungsaufsichtsgesetz*), providing payment services or conducting e-money business under the German Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz*) or managing investment funds within the meaning of the German Investment Code (*Kapitalanlagegesetzbuch*) require authorisation for

this business. If providers have already commenced an activity requiring authorisation without having obtained authorisation from BaFin, the Supervisory Authority enforces the authorisation requirement and ensures that the business is discontinued and any transactions wound up immediately. BaFin provides information on this topic on its website at [www.bafin.de](http://www.bafin.de). Depending on the nature of the case, BaFin may file a complaint with the prosecuting authorities against the operators responsible. For providers of new business models, it is expedient to make an initial self-assessment. To help with this process, BaFin has published Guidance Notices about the various transactions requiring authorisation on its website.

<sup>32</sup> [www.bafin.de/dok/11672076](http://www.bafin.de/dok/11672076).

<sup>33</sup> [www.bafin.de/dok/10144346](http://www.bafin.de/dok/10144346).

**Table 7: Exemption of institutions**

	2016	2017	2018
Exempted institutions	355	358	368
Newly exempted institutions	15	1	10

In practice, exemptions can only be granted on application. However, BaFin does not often grant such exemptions as undertakings conducting activities that are classified as banking business or financial services under German law are, in most cases, subject to the authorisation requirement.

### Exemptions within the meaning of the Payment Services Supervision Act

When the Second Payments Services Supervision Directive (PSD2) was transposed into national law, the German Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz*) was comprehensively amended. One of the main aims of PSD2 is to clarify the scope of such exemptions for business models that do not require supervisory authorisation. The Payment Services Supervision Act was revised with effect from 13 January 2018 in accordance with the European requirements.

PSD2 brings, among other changes, a comprehensive redesign of such exemption for payment system networks. The previous rules for exemption have been replaced by a clear classification into limited networks and very limited ranges of goods and services.

Exemptions under section 2 (1) no. 10 of the Payment Services Supervision Act can only be applied by issuers marketing a payment instrument or using such an instrument for settlement if it is clear to customers that it can only be used in the premises of the issuer or within a limited network. An example of a limited network is a store card issued by a particular retail chain, which customers can use to make purchases in the individual stores belonging to the chain.

Another exemption under section 2 (1) no. 10 of the Payment Services Supervision Act applies if the payment instrument can only be used to acquire a very limited range of products or services. A very limited range can be assumed, for example, in the case of fuel cards, which customers can only use to purchase goods and services related to vehicles.

BaFin has developed a comprehensive guide with examples, which presents the different exemption scenarios; it can be found in the revised Guidance

Notice on the Payment Services Supervision Act<sup>34</sup>. This gives market participants, especially those offering customer cards in the retail and service sector or the oil industry, a quick, easy-to-follow guide with information on whether their planned business venture is possible without seeking authorisation or whether they have to submit an application for authorisation to BaFin.

### 3.2 Investigation of unauthorised business activities

Anyone who conducts or provides banking business, financial services, payment services or e-money business, investment business or insurance business subject to authorisation requirements without obtaining prior authorisation from BaFin commits a criminal offence. Any violation of the authorisation requirement undermines the integrity of the financial system. BaFin investigates such cases using the powers under commercial enforcement law.

The number of suspected violations rose again in 2018 – from 1,042 cases to 1,281 cases (see Table 8). BaFin took formal steps against unauthorised business activities in 87 cases – an unprecedented number. According to estimates, the loss caused by these violations amounted to a figure in the substantial three-digit million euro range. In most cases, however, the providers discontinued their unauthorised business voluntarily after a hearing with BaFin on this issue. This shows how important it is for BaFin to investigate every case of suspicion rigorously.

**Table 8: Investigation of unauthorised business activities**

	2016	2017	2018
New suspected violations	1,113	1,042	1,281
Searches	18	20	23
Formal measures (discontinuation, winding-up)	35	25	87

Irrespective of any formal measures, there were 15 cases in 2018 (previous year: 2 cases) where BaFin raised public awareness of undertakings that had contacted German customers anonymously or under a pseudonym by e-mail, telephone or online. As is common in such cases, the providers contacted the customers from abroad, untruthfully claiming or creating the impression

<sup>34</sup> [www.bafin.de/dok/7846622](http://www.bafin.de/dok/7846622) (only available in German).

that they are supervised by BaFin in order to lull customers into a false sense of security.

### Objection and court proceedings

Formal measures imposed by BaFin can be objected to by the parties concerned. The number of objection proceedings rose by 30% year-on-year, from 37 to 48 cases (see Table 9).

**Table 9: Objection proceedings**

	2016	2017	2018
New objection proceedings	72	37	48
Formal objection notices	49	21	34
Withdrawals/other discontinuances	28	22	19

The measures imposed by BaFin are immediately enforceable, however; this is why any objection raised has no suspensory effect. The parties for which the measures are intended can only apply to the Administrative Court (*Verwaltungsgericht*) of Frankfurt am Main in summary proceedings for an order that the legal remedy should have a suspensory effect. The number of summary proceedings increased from 4 to 8 in 2018 (see Table 10).

**Table 10: Summary proceedings – first instance**

	2016	2017	2018
New summary proceedings	8	4	8
Dismissal of application	15	1	7
Order of suspensory effect	2	1	0

If BaFin ultimately rejects the objection to a formal measure, the party for which the measure is intended can bring legal action before the Administrative Court of Frankfurt am Main. As in the previous year, there were 16 new legal proceedings in 2018 (see Table 11).

**Table 11: Legal proceedings – first instance**

	2016	2017	2018
New legal proceedings	27	16	16
Judgment entered in favour of BaFin	13	4	2
Actions allowed	1	1	1
Withdrawals of actions/other discontinuances	6	5	10

On appeal, the Higher Administrative Court (*Verwaltungsgerichtshof*) of Hesse concluded 2 appeal proceedings and 9 cases in interim relief proceedings,

compared with 6 cases in the previous year. It ruled in favour of BaFin in 9 cases (previous year: 6 cases). 2 cases were withdrawn.

### Selected issues

#### Trading in binary options/trading in financial instruments on online platforms

Together with the Federal Office of Criminal Investigation (*Bundeskriminalamt*), BaFin warns against fraudulent online trading platforms for contracts for difference (CFDs) and binary options on commodities, shares, indices, currencies (forex) or cryptocurrencies that do not have the required licence.<sup>35</sup> As soon as investors have registered on the trading platform and made their first investments, they are immediately phoned by someone claiming to be a qualified finance broker. On their investment accounts, to which the investors supposedly have online access, the trading platform's deception software is used to simulate account movements and high profits. They make the transactions seem so convincing that the investors make further investments. However, when they come to request payment of their credit balance, contact with the trading platform is lost. The victims' chances of recovering their money are remote. They face the total loss of the capital invested.

#### Initial coin offerings and crypto tokens

Initial coin offerings (ICOs), a relatively new instrument for raising capital to fund business projects, have attracted keen interest among the public. In ICOs, blockchain technology is used to generate new digital units, such as virtual currencies and tokens, which are then sold to investors, in most cases in an unregulated public bidding process. Since there is a risk of total loss in such cases, BaFin warns investors of the risks of ICOs on its website.<sup>36</sup>

The number of companies raising capital through ICOs continued to rise significantly in 2018 despite price falls for crypto tokens. This resulted in an increase in the number of queries submitted to BaFin about how these forms of funding should be treated from a supervisory perspective.

In addition, in March 2018, BaFin published an advisory letter<sup>37</sup> on the legal classification of ICOs and crypto tokens. The document deals with the respective token

35 [www.bafin.de/dok/11771618](http://www.bafin.de/dok/11771618) (only available in German).

36 [www.bafin.de/dok/10185906](http://www.bafin.de/dok/10185906).

37 [www.bafin.de/dok/10690958](http://www.bafin.de/dok/10690958).



categories in detail and gives market participants an overview of current administrative practice.

### 3.3 Contact point for whistleblowers

Since 1 July 2016, BaFin's contact point for whistleblowers has accepted information on actual or potential violations of supervisory requirements. Information can be submitted to the contact point for whistleblowers via the electronic whistleblowing system, by post, e-mail, telephone, or in person.

In 2018, the contact point for whistleblowers received 665 reports. Almost 50% of all reports (342) were submitted via the electronic system, which had been introduced on 1 January 2017. 33% of reports came in by e-mail (254). Reports sent in by post accounted for around 14%. About 2% of the submissions (19) were made by phone, while less than 1% were delivered in person.

Almost half of the reports related to alleged violations by supervised undertakings. Approximately a quarter of the reports related to potentially unauthorised business activities. 11 reports related to alleged money laundering activities. 10 reports related to complaints that were passed to the Consumer Protection Directorate for further processing. The remaining reports related to matters for which BaFin is not the competent authority or that did not contain any identifiable facts.

## 4 Sanctions

In 2018, BaFin initiated a total of 221 administrative fine proceedings<sup>38</sup> (see info box, "New administrative fine proceedings initiated by BaFin").<sup>39</sup> The proceedings concerned natural persons, payment agents, credit institutions, insurance undertakings, payment institutions and institutions engaged in finance leasing and/or factoring<sup>40</sup>, and, where applicable, also against their responsible persons. They were triggered by violations of provisions subject to an administrative fine laid down in the following German acts: Money Laundering Act (*Geldwäschegesetz*), Banking Act,

Insurance Supervision Act, Capital Investment Act (*Vermögensanlagengesetz*), Securities Trading Act, Securities Prospectus Act (*Wertpapierprospektgesetz*) and Payment Services Supervision Act.

#### Amount of the administrative fines

Administrative fines totalling **€13,338,650** were imposed across all of BaFin's sectors in 2018 (see info box "Administrative fines imposed by BaFin").

#### Note

### Administrative fines imposed by BaFin

In 2018, BaFin imposed administrative fines totalling **€13,338,650**.

- Administrative fines totalling **€5,538,650** were attributable to Banking Supervision, Prevention of Money Laundering and Insurance Supervision.
- The Securities Supervision/Asset Management Sector imposed a total of **€7,800,000** in administrative fines.

#### Note

### New administrative fine proceedings initiated by BaFin

- BaFin initiated 221 administrative fine proceedings in 2018.
- 86 of them were attributable to Banking Supervision, Prevention of Money Laundering and Insurance Supervision<sup>41</sup>.
- 135<sup>42</sup> were attributable to the Securities Supervision/Asset Management Sector.

#### Administrative fine proceedings – Securities Supervision

In 2018, BaFin's Securities Supervision/Asset Management Sector imposed administrative fines totalling €7.8 million<sup>43</sup> for violations of capital

38 Proceedings under the German Act on Breaches of Administrative Regulations (*Ordnungswidrigkeitengesetz*).

39 For information on the distinction between sanctions and measures, see 2016 Annual report, page 55 ff.

40 Section 1 (1a) sentence 2 nos. 9 and 10 of the Banking Act.

41 These proceedings were initiated by the Internal Administration and Legal Affairs Sector. Since the beginning of 2018, Prevention of Money Laundering has come under the Resolution Sector.

42 These include the figures stated in 2.5.2 and chapter VI 2.6.

43 The total includes the administrative fines stated in 2.5.2 and chapter VI 2.6.

markets law<sup>44</sup> (see info box “Administrative fines imposed by BaFin” on page 49). The sector launched 135<sup>45</sup> new administrative fine proceedings; a total of 869 proceedings were still pending from the previous year. It concluded a total of 322 proceedings, 126 of them by imposing an administrative fine. The prosecution ratio was 39.8%.<sup>46</sup>

### **Administrative fine proceedings initiated by Banking and Insurance Supervision**

Due to violations of provisions of the Money Laundering Act, the Payment Services Supervision Act, the Banking Act and the Insurance Supervision Act that are punishable by a fine, BaFin<sup>47</sup> initiated 57 proceedings under the Act on Breaches of Administrative Regulations in the year under review – against legal persons, including credit institutions, insurance undertakings, payment institutions and institutions that engage in finance leasing and/or factoring. It also initiated proceedings against management personnel, such as managing directors and money laundering reporting officers, of the undertakings concerned, as well as against other natural persons subject to professional supervision requirements.<sup>48</sup> In the year under review, BaFin issued 22 administrative orders imposing a fine in these proceedings and others pending from previous years. 20 of these administrative orders imposing a fine became final in 2018, including 4 in a preliminary hearing. 6 administrative fines were imposed as the result of a court decision, 1 administrative fine was confirmed by a court of first instance, and 1 other on appeal. In 1 case, the party concerned and an interested party appealed against the ruling of the court of first instance.

BaFin<sup>49</sup> launched 27 proceedings against agents within the meaning of section 1 (9) of the Payment Services Supervision Act in the year under review. BaFin issued 26 administrative orders imposing a fine in these 27 proceedings and other administrative fine proceedings pending from previous years against agents. 23 administrative orders imposing a fine on agents and another one involving a payment institution

domiciled abroad that provides remittance services in Germany through agents became final in 2018, including 4 in a preliminary hearing following an ordinary appeal. Another administrative order imposing a fine was upheld on its merits following a decision of the Local Court of Frankfurt am Main<sup>50</sup>. In another case, the party concerned lodged an appeal with the Higher Regional Court (*Oberlandesgericht* – OLG) of Frankfurt am Main<sup>51</sup> against the decision of the court of first instance handed down by the Local Court of Frankfurt am Main, which had upheld the administrative order imposing a fine on its merits. The appeal was rejected as unfounded.

Appeals were lodged against 3 administrative orders imposing a fine on agents. The decisions handed down by the local court in response to these appeals upheld the administrative orders imposing a fine on their merits; in 1 case, the fine imposed by BaFin was reduced. 14 other proceedings were discontinued by BaFin<sup>52</sup>; in 1 case, the proceedings were joined with other proceedings that had been brought separately.

A total of 32 proceedings were discontinued in the year under review, including some still pending from previous years, 12 of them for discretionary reasons.<sup>53</sup> 20 proceedings were terminated in other ways, for example by discontinuing proceedings in accordance with section 46 (1) of the Act on Breaches of Administrative Regulations, normally in conjunction with section 170 (2) of the German Code of Criminal Procedure (*Strafprozessordnung* – StPO).

### **Amount of the administrative fines**

Due to violations of provisions of the Banking Act, the Money Laundering Act and the Payment Services Supervision Act, BaFin imposed a total of 257 individual administrative fines in 2018; they amounted to €5,538,650 in total. The fines were imposed on credit institutions, insurance undertakings, payment institutions and institutions engaged in finance leasing and/or factoring, and – depending on the specific facts of the case – also against their responsible persons.

44 This total includes violations of the Securities Trading Act, the Securities Acquisition and Takeover Act and the Capital Investment Act. In 2018, 5 new proceedings were initiated in this segment.

45 These include the figures stated in 2.5.2 and chapter VI 2.6.

46 The statistical data include the administrative fine proceedings stated in 2.5.2 and chapter VI 2.6.

47 These proceedings were initiated by the Internal Administration and Legal Affairs Sector.

48 Or against their responsible persons.

49 These proceedings were initiated by the Internal Administration and Legal Affairs Sector.

50 946 OWi – 7521 Js 244431/17 re sentence 1.

51 2 Ss-OWi 187/18 re sentence 2.

52 Section 47 (1) of the Act on Breaches of Administrative Regulations.

53 Section 47 (1) of the Act on Breaches of Administrative Regulations.

## 5 Money laundering prevention

### 5.1 Bases of money laundering prevention

#### 5.1.1 Europeanisation of anti-money laundering supervision

To increase the effectiveness and convergence of anti-money laundering supervision, the European Commission proposed an amendment to the Regulation on the European Banking Authority (EBA) on 12 September 2018 in order to strengthen, among other things, the role of the EBA in anti-money laundering supervision.

In support of this, on 4 December 2018, the Council adopted conclusions on an action plan to better tackle money laundering and terrorist financing. It sets out a number of short-term non-legislative actions addressed to the European Supervisory Authorities (ESAs), the prudential supervisory authorities including the ECB, and the national anti-money laundering supervisory authorities.

##### **Multilateral agreement**

In addition, amendments to the Fourth Anti-Money Laundering Directive<sup>54</sup> established an obligation for the national anti-money laundering supervisory authorities to create a multilateral agreement on the exchange of information by 10 January 2019. BaFin signed the agreement in January 2019.

#### 5.1.2 EBA review of anti-money laundering supervision

BaFin belongs to the network of experts that assists the EBA in implementing its planned reviews of anti-money laundering supervision. The EBA aims in this process to investigate how effectively the national competent authorities conduct anti-money laundering supervision and the prevention of terrorist financing in relation to credit institutions. The review phase started in 2018 and is expected to continue until 2021.

#### 5.1.3 Supervisory colleges

In general, anti-money laundering supervision falls under the exclusive responsibility of the respective EU member states. Unlike prudential banking supervision, the ECB is not responsible for this. However, to be able to pursue cross-border money laundering, it is essential to have a holistic overview of a group of companies. This is why the national competent authorities have to exchange information on a regular basis. To facilitate this exchange of information, guidelines for the establishment of supervisory colleges have been developed under the leadership of the EBA and with the involvement of the national competent authorities.

In these colleges, the authorities regularly exchange information on the risk situation of a group with regard to money laundering and terrorist financing. In addition, the colleges improve direct communication among the competent supervisory authorities. Articles 50a and 75a of the Fifth EU Anti-Money Laundering Directive provide the legal basis<sup>55</sup>. The guidelines on supervisory cooperation underwent the ESAs' consultation process until 8 February 2019. They are expected to be published in the second quarter of 2019.

#### 5.1.4 Interpretation and application guidelines provided by BaFin

On 11 December 2018, BaFin published interpretation and application guidelines<sup>56</sup> in accordance with section 51 (8) sentence 2 of the Money Laundering Act. They apply to all entities obliged under the Money Laundering Act that are subject to supervision by BaFin. The interpretation and application guidelines contain explanatory details on the legal requirements. They are intended to help the obliged entities to duly meet the obligations incumbent upon them.

There is a special focus on customer due diligence and internal safeguards. The interpretation and application guidelines follow a risk-based approach. In particular, BaFin uses them to explain new legal requirements – such as the concept of a fictitious beneficial owner. The guidelines also explain the obligations relating to identifying the “person acting (on behalf of the contracting party)”. In addition, BaFin uses the interpretation and application guidelines to address current market trends and lays down requirements in this regard. One example is the question about the

54 Directive 2018/843/EU, OJ EU L 156/43, known as the Fifth Anti-Money Laundering Directive.

55 Directive 2018/843/EU, OJ EU L 156/43.

56 [www.bafin.de/dok/11794472](http://www.bafin.de/dok/11794472).

conditions under which such a person may be identified as a result of using or disclosing data already collected (originating from a previous identification process).

### 5.1.5 BaFin Circular on due diligence obligations for virtual currencies

How are credit institutions, financial services providers, payment institutions and e-money institutions expected to deal with payments received into an account that can be traced back to an exchange of virtual currencies? The planned BaFin Circular<sup>57</sup>, which went through the consultation process in the autumn, will provide assistance to institutions. They are to take these types of transactions into account using their own risk assessment in connection with virtual currencies. The Circular is intended for publication in the first quarter of 2019.

### 5.1.6 National Risk Analysis in Germany

As part of the National Risk Analysis (NRA), the investigation of Germany's exposure to money laundering and terrorist financing risk was begun in January 2018. The NRA process is conducted under the leadership of the Federal Ministry of Finance. It involves BaFin's Prevention of Money Laundering Directorate as well as all units and parties working in the area of the prevention of money laundering and terrorist financing. This means that, in addition to the competent authorities, representatives of the private sector, of its associations and of academia also contribute their expertise to the investigation. The results of the NRA analysis are expected in the summer of 2019.

## 5.2 Money laundering prevention in practice

### 5.2.1 Special representative at Deutsche Bank AG

In order to prevent money laundering and terrorist financing, BaFin ordered Deutsche Bank AG on 21 September 2018 to take appropriate internal safeguards and comply with general due diligence obligations.<sup>58</sup> At the same time, the auditing firm KPMG was appointed as special representative to monitor compliance with the order. This event is unprecedented; never before has a special representative been appointed in the context of money laundering prevention.

To prevent money laundering and terrorist financing, BaFin ordered Deutsche Bank AG on 15 February 2019 to review its group-wide risk management processes in the area of the institution's correspondence banking and make any necessary adjustments. The order was issued on the basis of section 51 (2) sentence 1 of the Money Laundering Act.

In order to monitor the implementation of the ordered measure, BaFin expanded the mandate of the special representative in accordance with section 45c (1) in conjunction with subsection (2) no. 6 of the Banking Act. The special representative is to report on and assess the progress of implementation.

#### History of the special representative

Section 46 (1) of the original version of the Banking Act of July 1961 already specified that a "supervisor" could be appointed as a provisional measure to avert threats. This related in particular to potential risks to the security of the assets entrusted to an institution – i.e. primarily the protection of customer deposits.

The term "special representative" was introduced into the Banking Act more than 40 years later, when the German Fourth Financial Market Promotion Act (*Finanzmarktförderungsgesetz*) of 2002 was adopted (section 36 (1a) of the Banking Act); this function existed alongside the supervisor until 2011. This has allowed BaFin not only to remove, but also to replace untrustworthy and/or unqualified senior managers and – from 2009 onwards – members of supervisory or administrative bodies in their governing body functions.

After the global financial crisis, the German Bank Restructuring Act (*Restrukturierungsgesetz*), which entered into force on 1 January 2011, merged the functions of supervisor and special representative. At the same time, it further enhanced the role of the special representative, who has since then been responsible for risk prevention and can be deployed in institutions as needed in any particular situation.

#### New powers

In addition to BaFin's option to replace some or all members of a governing body, the special representative can now also draft restructuring plans, address specific weaknesses in an institution's business organisation and monitor compliance with BaFin's orders. BaFin can commission the special representative accordingly and grant them the necessary powers. Depending on the particular case, the mandate may range from simply observing and reporting to fully replacing a governing body or one of its members. Their permanent

<sup>57</sup> [www.bafin.de/dok/11597264](http://www.bafin.de/dok/11597264).

<sup>58</sup> See also chapter I.

presence in the institution and their comprehensive rights to giving and receiving information make special representatives effective agents of supervision.

## 5.2.2 Money laundering prevention in correspondent banking relationships

Under the heading “Danske Bank”, the media reported on what is presumed to be a major money laundering scandal. Between 2007 and 2015, an Estonian branch of Danske Bank A/S, Copenhagen, is said to have laundered amounts running into several billion for customers resident outside Estonia. In this context, the reports also highlighted German banks that had correspondent banking relationships with Danske Bank in Estonia.

BaFin is investigating to what extent transactions were in fact executed via German banks and whether these point to shortcomings in money laundering prevention, especially with regard to the general requirements for correspondent banking relationships. The standards it applies in the process are mainly set out in section 15 of the Money Laundering Act, which codifies the international requirements of the Financial Action Task Force (FATF) and those of the current version of the European Money Laundering Directive<sup>59</sup>.

BaFin is in constant contact with both the competent German prosecuting authorities and a number of foreign supervisory authorities. In addition, in 2019 BaFin’s anti-money laundering reviews will focus on compliance with the requirements under anti-money laundering legislation for the correspondent banking business in banks with international operations.

## 5.2.3 High-volume cash withdrawals

In the summer of 2018, BaFin learnt that an institution was planning to withdraw hundreds of millions in cash from the Deutsche Bundesbank. Especially the planned transfer abroad of the banknotes in question caused a stir among the public. As soon as the transaction became known, BaFin carried out an on-site inspection at the institution concerned, focusing specifically on the internal safeguards and on compliance with appropriate due diligence obligations in connection with the planned transfer. The institution decided not to proceed with the planned withdrawal and transfer even before the result of the inspection was announced.

## 5.2.4 New electronic record sheets

For submissions under section 27 of the German Audit Report Regulation (*Prüfberichtsverordnung*), BaFin launched a modern, effective procedure for auditors in October 2016, allowing the electronic filing of the anti-money laundering audit report under section 27 of the Audit Report Regulation and of record sheets under section 27 (9) in conjunction with Appendix 5 of the Audit Report Regulation.

To make the process even more efficient for both auditors and BaFin, the supervisory authority developed an electronic record sheet in 2018. Since 4 February 2019, BaFin’s reporting and publishing platform (MVP Portal) can be used to enter the record sheet data or to upload the data with the audit report as an XML file. This change also supports BaFin’s risk-based supervision work since the system processes the data immediately. After the end of a transitional period, the new system will become binding on the types of institutions already included as from 1 May 2019.

## 5.2.5 On-site inspections of the video identification procedure

On the basis of Circular 3/2017 (GW) governing video identification procedures<sup>60</sup>, BaFin conducted six on-site inspections in 2018. Since the video identification procedure is usually outsourced to external service providers, the inspections focused mainly on compliance with the requirements for managing delegated services as set out in section 17 (5) and (6) of the Money Laundering Act. If credit institutions outsource this know-your-customer process to third parties, they are obliged to conduct their own monitoring of the implementation of video identification through spot checks.

As part of this process, BaFin also reviewed compliance with other requirements of the Circular relating to the storage of the video files and error-free collection of the data in the core banking system. BaFin also gained insights into the state of the art and the handling of regulatory requirements by specifically visiting individual service providers. The inspections showed that the stringent requirements laid down in the Circular are mostly complied with. BaFin has identified some areas for attention in the inspection of samples by the money laundering reporting officers.

<sup>59</sup> Directive (EU) No 2015/849, OJ EU L 141/73.

<sup>60</sup> [www.bafin.de/dok/9318762](http://www.bafin.de/dok/9318762).

The established practice of video identification includes a detailed verification of the security features of identity documents. This seems to be an effective tool against deception attempts using forged documents, as BaFin has clearly established in its on-site inspections. Recently, there have been indications, however, that attacks on the video identification process are shifting towards social engineering. This involves attempting to influence people and, for example, persuade them to open an account using video identification with the intention to use the account to transfer funds that are the proceeds of crime via the account and to conceal the origin of the funds.

## 5.2.6 Inspections

In the context of money laundering prevention, BaFin conducted or shadowed a total of 90 money laundering prevention inspections in 2018 (previous year: 44 inspections, see Table 12 “Ad-hoc inspections in 2018”).

BaFin uses the ad-hoc inspection tool to get a quick overview and formulate an appropriate supervisory response in cases of suspected material violations in money laundering prevention. Ad-hoc inspections may be triggered by reports in the press, submissions to the contact point for whistleblowers or information received from employees of the undertakings under supervision.

**Table 12: Ad-hoc inspections in 2018**

Type	Number
Credit institutions (routine inspections and shadowing)	57
Credit institutions (ad-hoc inspections)	8
Credit institutions (account information access procedures in accordance with section 24c of the Banking Act – routine inspections)	6
Insurers (routine inspections and shadowing)	2
Agents (routine inspections)	16
Financial services undertakings (shadowing of routine inspection)	1
<b>Total</b>	<b>90</b>

BaFin’s ad-hoc inspections are also conducted in addition to the routine inspections, which are planned annually in advance. Furthermore, BaFin checks whether the credit institutions maintain their information access file correctly in accordance with section 24c of the Banking Act. In this context, BaFin examines whether the institutions meet their identification obligations under

the Money Laundering Act and appropriately provide the data in the information access file.

The establishment of a dedicated group of auditors in 2017 helped BaFin to significantly increase the number of inspections in the context of money laundering in 2018. These inspections provide a direct insight into the prevention systems of the obliged entities and facilitate closer and more direct exchanges of information within the undertakings. BaFin identifies focus areas for its inspections, for example because of current events or abnormalities. Focus areas in 2018 included the implementation of group-wide due diligence obligations, account monitoring and the video identification process. In the course of its inspections, BaFin found that institutions had been late in implementing the new Money Laundering Act. It also found that new elements, such as the introduction of the fictitious beneficial owner, posed a challenge for institutions. Since 11 December 2018, BaFin’s interpretation and application guidelines<sup>61</sup> have provided concrete practical support.

## 5.2.7 Risk-based supervisory practice in money laundering prevention

In the context of money laundering, supervision should be based on the specific money-laundering risk. This risk-based approach is one of the requirements laid down in the Fourth EU Money Laundering Directive<sup>62</sup>. Guidance is also provided by the Risk-Based Supervision Guidelines issued by the three European Supervisory Authorities (EBA, ESMA and EIOPA). The starting point of risk-based supervisory practice is the regular risk classification by institutions and undertakings (see info box “Risk-based supervision in the non-banking financial sector” on page 55). On the basis of this risk classification, BaFin can see at a glance the specific risk potential and the quality of the individual preventive measures taken by each obliged entity. This determines the supervisory activities and the annual inspection schedule. The classification is normally based on the information provided in the audit report on the annual financial statements and the analysis of the questionnaire under Annex 5 to section 27 of the Audit Report Regulation. In addition, BaFin also takes into account findings from special audits and ongoing supervision.

<sup>61</sup> See 5.1.4.

<sup>62</sup> See BaFinJournal May 2018, page 23 ff. (only available in German).

## Note

## Risk-based supervision in the non-banking financial sector

As part of the reorganisation of the Prevention of Money Laundering Directorate as at 1 January 2018, BaFin bundled the anti-money laundering supervision of institutions and undertakings in the non-banking financial sector in a single Division. It covers investment firms as defined in the Capital Requirements Regulation (CRR)<sup>63</sup>, other financial services institutions, payment institutions, e-money institutions, asset management companies, insurance undertakings, agents and e-money agents. BaFin has restructured the supervision of these undertakings in order to introduce an intensified risk-based approach (RBA) to supervision – based on national and international requirements. The purpose of strengthening the RBA is to ensure that in the prevention of money laundering and terrorist financing the intensity of supervision is in accordance with the institution-specific risks in the non-banking financial sector.

### 5.2.8 Central contact points for foreign e-money institutions and payment institutions

On 10 August 2018, The European Commission published a delegated regulation<sup>64</sup> supplementing Article 45 of the Fourth EU Money Laundering Directive in the Official Journal of the EU. This allowed the tasks of a central contact point to be introduced and designed in accordance with section 41 (1) of the Payment Services Supervision Act.

In its capacity as host supervisor, BaFin started preparations to implement the new requirements. Undertakings that maintain a network of agents and e-money agents in Germany and meet the criteria must nominate a central contact point in Germany for BaFin, the Financial Intelligence Unit (FIU) and prosecuting authorities.<sup>65</sup>

63 Directive (EU) No 575/2013, OJ EU L 176/1.

64 Delegated Regulation (EU) No 2018/1108, OJ EU L 203/2.

65 See Article 4f of Delegated Regulation (EU) 2015/849, OJ EU L 203/2.

## 5.3 Account information access procedure

Under section 24c (1) of the Banking Act, credit institutions, asset management companies and payment institutions are required to maintain a data file in which they store certain account master data, such as the account number, name and date of birth of the account holders and authorised users as well as the date of opening and closure of the account. BaFin may retrieve individual items of information from this file if it needs them to perform its supervisory duties. Upon request, it also provides information from the account information access file to the authorities listed in section 24c (3) of the Banking Act. Table 13 provides statistical data on the number and breakdown of the queries.

**Table 13: Account information access procedures under section 24c of the Banking Act**

Recipient	2018		2017	
	absolute	in %	absolute	in %
BaFin	877	0.6	751	0.5
Tax authorities	13,249	9.3	13,690	10.0
Police authorities	87,931	61.5	84,092	61.5
Public prosecutors	30,671	21.5	27,812	20.3
Customs authorities	9,645	6.8	10,173	7.4
Other	515	0.4	327	0.2
<b>Total</b>	<b>142,888</b>		<b>136,845</b>	

## 6 Digitalisation

### 6.1 BaFin report on big data and artificial intelligence

In June 2018, BaFin published its report entitled “Big data meets artificial intelligence – Challenges and implications for the supervision and regulation of financial services”<sup>66</sup> prepared in collaboration with experts from Partnerschaft Deutschland, the Boston Consulting Group (BCG) and the Fraunhofer Institute for Intelligent Analysis and Information Systems (IAIS). The objective of the study was to give BaFin a comprehensive picture to allow it to identify strategic trends, market developments and newly emerging

66 [www.bafin.de/dok/11250046](http://www.bafin.de/dok/11250046).

risks at an early stage and to formulate an appropriate response. The report looks into the implications of technology-driven market developments from a number of regulatory and supervisory perspectives.

### Consultation

The report formed the basis of intensive dialogue on the group of issues around big data and artificial intelligence (BDAl). In July 2018, BaFin launched a consultation regarding the report and the key questions it raises. A summary and an initial assessment by BaFin President Felix Hufeld can be found in issue 1/2019 of the BaFinPerspectives publication series.<sup>67</sup>

## 6.2 Fintech companies

The definition of “fintech” given by the Financial Stability Board (FSB)<sup>68</sup> has widely established itself as standard. The FSB defines fintech as technology-enabled innovation in financial services that could result in new business models, applications, processes or products and could influence financial markets and institutions and the way in which financial services are provided.

Alongside this definition, the term is also used for mostly young undertakings in the financial services sector that use technology-enabled innovation in creating a service and/or at the interface with the customer. But even established undertakings in the financial services sector are making use of technology-enabled innovation, both to create a service and at the interface with the customer.

### No legal definition as yet

There is, however, no legal definition of the term “fintech” as yet. Due to BaFin’s technology neutrality, it is in any event immaterial to the authority whether the undertakings under its supervision use innovative financial technology, and what technology they employ.

On its website, BaFin provides information<sup>69</sup>, specifically tailored to start-up and fintech companies, on typical fintech business models and topics as well as a contact form<sup>70</sup>. In 2018, the contact form was used to submit queries in around 150 cases in total.

In addition, BaFin uses its “BaFin-Tech” event format to exchange views and information on innovative financial technologies with new and established undertakings in the finance industry as well as with associations and the scientific community. The next BaFin-Tech will be held on 11 September 2019 in Bonn.

Innovative financial technologies that were the centre of attention in 2018 and are expected to continue to be focal points in the coming years are BDAl<sup>71</sup> and the distributed ledger technology/blockchain group of issues.

## 6.3 Guidance Notice on outsourcing to cloud providers

The outsourcing of activities to cloud providers<sup>72</sup> has increasingly attracted attention in the financial sector in recent months – not only in Germany, but throughout Europe. This is why there are now regular exchanges on how outsourcing to cloud providers should be dealt with, not only between the EBA and the European Insurance and Occupational Pensions Authority (EIOPA) and within the Single Supervisory Mechanism (SSM), but also bilaterally between the national competent authorities. An important outcome of these exchanges is the publication by the EBA of the “Recommendations on outsourcing to cloud service providers” in December 2017<sup>73</sup>. The EBA has in turn been tasked with compiling the “Guidelines on Outsourcing” on the basis of these recommendations; they are currently being worked on and publication is planned for the middle of 2019.

An increasing number of undertakings have outsourced activities to cloud providers in recent years or are planning to do so in future. This also involves a check as to the conditions under which this kind of outsourcing is permitted under supervisory law. BaFin and the Deutsche Bundesbank discussed this issue in 2018 with both undertakings under supervision and cloud providers. A key aspect in this context was to determine how (standard) contracts and supplementary agreements must be worded so that they also meet and govern the requirements that are relevant under supervisory law. This includes information and inspection rights granted to the supervised undertakings and BaFin.

<sup>67</sup> [www.bafin.de/dok/11506586](http://www.bafin.de/dok/11506586).

<sup>68</sup> See Financial Stability Board (2017): Financial Stability Implications from FinTech: Supervisory and Regulatory Issues that Merit Authorities’ Attention, 27 June 2017, page 7, <http://www.fsb.org/2017/06/financial-stability-implications-from-fintech/>, as at 18 December 2018.

<sup>69</sup> [www.bafin.de/dok/8054672](http://www.bafin.de/dok/8054672).

<sup>70</sup> [https://www.bafin.de/SiteGlobals/Forms/Kontakt/Fintech\\_Integrator.html](https://www.bafin.de/SiteGlobals/Forms/Kontakt/Fintech_Integrator.html).

<sup>71</sup> [www.bafin.de/dok/11250046](http://www.bafin.de/dok/11250046).

<sup>72</sup> See chapter III 1.3.4.

<sup>73</sup> EBA/REC 2017/03.



### Guidance on outsourcing to cloud providers

To make the outcomes of the discussions transparent, BaFin published the Guidance Notice entitled "Guidance on outsourcing to cloud providers"<sup>74</sup> on 8 November 2018. Together with the Deutsche Bundesbank, BaFin explains in this document how it assesses outsourcing to cloud providers. The guidance is intended for credit institutions, financial services institutions, insurance undertakings, pension funds, investment firms, asset management companies, payment institutions and e-money institutions.

The Guidance Notice explains BaFin's current supervisory practice in these cases of outsourcing. It also sets out clearly how BaFin rates the different kinds of wording in contract clauses. In addition, it wants to create awareness among the supervised undertakings of problems that may arise when using cloud services and what supervisory requirements may arise as a result. However, since BaFin's Guidance Notice on cloud services does not contain any new requirements, the existing requirements for outsourcing remain unchanged. This means that outsourcing to cloud providers is also subject to the general rule that the managers' responsibilities must not be transferred to the cloud services provider when data is outsourced. The undertaking under supervision that has outsourced data remains responsible for ensuring that the applicable legal provisions are in fact complied with.

## 6.4 IT risks at banks and insurance undertakings

As the importance of information technology in the financial sector increases, so does the vulnerability of the undertakings. Since the industry is very closely interconnected, IT infrastructure failures in one undertaking may spread to other market participants and, in extreme cases, threaten financial stability. In order to engage in effective prevention measures in cooperation with undertakings in the financial sector, BaFin pooled key skills to establish the IT Supervision, Payment Transactions and Cyber Security Directorate (GIT) in 2018. The Directorate, which has four divisions and acts across all sectors, focuses on, among other matters, policy issues relating to cyber security in digitalisation, operational supervision of payment institutions and e-money institutions, policy issues relating to IT supervision and the inspection regime as well as specific IT inspections at insurance undertakings.

<sup>74</sup> See chapter I 5.1.

### Three-stage plan for IT supervision

BaFin has developed a three-stage programme for its IT supervisory practice. Stage 1 involves a set of frameworks in which comparable IT requirements are formulated for the undertakings in the different supervisory areas. In addition to the Supervisory Requirements for IT in Financial Institutions (BAIT) published back in November 2017, this also includes the Supervisory Requirements for IT in Insurance Undertakings published in July 2018 (VAIT). These documents set out in detail what BaFin expects insurers to do in respect of their IT security. The requirements under VAIT are similar to those under BAIT. BaFin clearly states that IT security is a management issue in both VAIT and BAIT. Among other things, these circulars therefore also aim to increase awareness of IT risks among members of management boards, including of risks that may arise when IT services are spun off or procured. To minimise uncertainty when outsourcing or spinning off activities to cloud providers, BaFin published additional guidance<sup>75</sup> on outsourcing to cloud providers in November 2018 to supplement BAIT and VAIT.

The Supervisory Requirements for IT in Asset Management Companies (KAIT) are expected to be published for consultation in the course of 2019.

Stage 2 is aimed at further strengthening the banks' resilience to cyber attacks and their ability to maintain business continuity. To this end, BaFin will shift the focus on the effectiveness of the existing safeguards. Since the end of 2018, BaFin and the Deutsche Bundesbank have therefore been cooperating in the area of banking supervision on the potential implementation of red teaming tests, i.e. cyber stress tests for the German financial sector.

Stage 3 involves improvements to crisis management: both institutions and BaFin must be prepared for a cyber attack or IT security incident at all times. BaFin is therefore planning to expand BAIT by adding a module on emergency management, including emergency tests. Cyber drills will also be covered: they involve all relevant players acting in concert in crisis situations – both nationally and internationally.

<sup>75</sup> See also 6.3.

## 6.5 Crypto tokens

BaFin is closely following developments in the area of crypto tokens<sup>76</sup>, acting in accordance with its legal mandate and the principles of proportionality and technology neutrality. This is because crypto tokens are also subject to the general rule that, although innovation should not be hindered, the integrity of the financial market place – which includes maintaining a level playing field – and collective consumer protection must be guaranteed.

### Cooling observed

Following a boom phase at the beginning of 2018, some cooling was experienced in the market capitalisation of crypto tokens such as bitcoins around the world. After an all-time high in January 2018, the total market capitalisation of all crypto tokens worldwide declined sharply. Likewise, publicly available sources indicate that there were more ICOs around the world in 2018 than in the previous year.

Following its warning to consumers on the risks of ICOs<sup>77</sup> in 2017, BaFin published an advisory letter on 20 February 2018 that deals with the supervisory classification as financial instruments<sup>78</sup> of the crypto tokens and cryptocurrencies underlying the ICOs.<sup>79</sup> In 2018, market participants made extensive use of the option to contact BaFin to clarify specific supervisory issues.

BaFin also contributed to European and international work on crypto tokens, for example at ESMA, the EBA, the ECB and ISO (International Organization for Standardization)<sup>80</sup>.

# 7 Market-based financing

## 7.1 Capital Markets Union

Established in 2015, the Capital Markets Union is aimed at further integrating and deepening the capital markets in the EU. Three years on, there are increasing signs that the Capital Markets Union is a long-term project that will extend beyond the current legislature of the European Parliament.

### New market segment

A priority area in 2018 was to support small and medium-sized entities (SMEs) by making it easier for them to gain access to capital market-based financing. To this end, MiFID II has created the “SME growth market” segment, which is aimed at lessening administrative burdens for issuers with activities there. In May 2018, the European Commission proposed further improvements to market access for SMEs by removing or scaling back supervisory requirements. One aspect being discussed is the extent to which these entities will have to continue to keep insider lists of individuals with access to price-sensitive information. From BaFin’s perspective, this process should not only focus on the issuers’ interest in minimising red tape, but also pay attention to aspects such as consumer protection and effective market supervision to a significant degree.

### Pan-European personal pension product

As part of the Capital Markets Union, the EU Commission has for some time been working on developing a simple, efficient and competitive EU product for personal pension provision. On 29 June 2017, it proposed a regulation for a pan-European personal pension product (PEPP).

On 19 June 2018, the Council agreed a general approach on creating a Council compromise text and gave the go-ahead for trilogue negotiations. In September 2018, the European Parliament (EP) submitted its proposed amendments to the Commission’s proposal in a report of the ECON<sup>81</sup> committee.

In autumn 2018, informal trilogue negotiations began between the Council and the EP about a possible compromise text.

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76 For information on the types of crypto tokens identifiable in the market, their supervisory classification and conclusions, see: BaFinPerspectives issue 1/2018, page 48 ff.

77 [www.bafin.de/dok/10185906](http://www.bafin.de/dok/10185906).

78 [www.bafin.de/dok/10690958](http://www.bafin.de/dok/10690958).

79 [www.bafin.de/dok/10692226](http://www.bafin.de/dok/10692226).

80 ISO is developing an international blockchain standard in Technical Committee 307 (ICO TC 307).

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81 ECON is the European Parliament’s Committee on Economic and Monetary Affairs.

One of the major points of discussion in the negotiations was the role to be played by EIOPA. Both the EP and the European Commission saw a key function for EIOPA as a PEPP licensing authority in future. The Council, by contrast, argued for the integration of PEPP into the existing supervisory system and wanted to assign these tasks to the national competent authorities. BaFin provided advice to the Federal Ministry of Finance during the trilogue negotiations.

A provisional political agreement was reached in December 2018, according to which the Council opinion prevailed on key points, so that the existing supervisory structure will remain in place. The technical finalisation and formal Council and EP approval are scheduled for 2019.

## 8 International supervision

### 8.1 ESA review

In September 2017, The European Commission presented its draft amendments to the Regulations governing the ESAs. The draft proposed far-reaching centralisation of the existing supervision architecture in the EU, resulting in a fundamental reorganisation. This was to be achieved by changing the internal governance and financing, as well as by creating new powers for the ESAs.<sup>82</sup> It involved the transfer of direct supervisory powers, which have to date been a national responsibility, to ESMA for example, giving the authority the option to intervene in national

supervisory strategy or national supervision processes, for example in relation to outsourcing.<sup>83</sup>

BaFin took a critical view of the European Commission's plans from the start, because the European System of Financial Supervision (see info box) was created in 2010 specifically as a network of national and European supervisory authorities and this approach has proven to be successful. Of course, BaFin strongly supports the role of the ESAs when it comes to creating supervisory convergence and a shared supervisory culture in the EU. But it was not without reason that BaFin President Felix Hufeld put the question "Why fix something that is essentially working?" at BaFin's annual press conference on 3 May 2018. Those who want to strengthen the ESAs, he continued, should above all ensure that they can make better use of the powers they already have.<sup>84</sup>

#### Expansion of ESA review

In September 2018, the European Commission made additions to its draft amendments to the Regulations governing the ESAs. The intention is to strengthen the EBA in the fight against money laundering. Following a string of scandals, the European Commission's idea is to expand and bundle the ESAs' anti-money laundering powers for the entire financial market at the EBA. The Commission wants the EBA to be able to insist on investigations at the national level, for example. Furthermore, the efforts of the national competent authorities in tackling money laundering are to be reviewed and the results published.

The separate deliberations of the Council of the European Union and the European Parliament on the European Commission's proposals lasted into December

#### Definition

### European System of Financial Supervision

The start of 2011 brought the creation of the three European Supervisory Authorities (ESAs): the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the European Securities and Markets Authority (ESMA). The European Systemic Risk Board (ESRB) had started operating just a short time earlier,

at the end of 2010. Together, the ESAs and the ESRB form the European System of Financial Supervision (ESFS), the purpose of which is to harmonise supervisory practice in Europe and improve the integration between macro-prudential analysis and micro-prudential supervision.

<sup>82</sup> See 7.1.

<sup>83</sup> See 2017 Annual Report, pages 60/61.

<sup>84</sup> [www.bafin.de/dok/10840856](http://www.bafin.de/dok/10840856).

2018; agreement, initially only for the money laundering part of the ESA review, was reached with the Council. The trilogue started in the middle of February 2019, after the European Parliament had agreed on a reform text, followed by a “general approach” to the upcoming negotiations adopted by the Council. The positions were far apart – particularly on some key issues. It was all the more surprising, therefore, when the political conclusion to the trilogue came on 21 March 2019. Many of the Council’s proposals have been adopted; this means that a number of the ideas put forward by the European Commission, of which BaFin had been critical, are no longer on the agenda.

## 8.2 Bilateral and multilateral cooperation

### Memoranda of understanding

BaFin again agreed memoranda of understanding (MoUs) with other supervisory authorities in the year under review.<sup>85</sup> The main focus was on agreements relating to securities supervision. BaFin signed an MoU with the Hong Kong Securities and Futures Commission (SFC) on cooperation between cross-border institutions. BaFin entered into agreements with the Ontario Securities Commission (OSC) and the Monetary Authority of Singapore (MAS) on undertakings acting as securities clearers and central counterparties (CCPs). In these agreements, the supervisory authorities set out rules for exchanging information that is relevant to the respective other authority.<sup>86</sup>

### Technical cooperation

Together with the German Society for International Cooperation (*Gesellschaft für Internationale Zusammenarbeit GmbH – GIZ*), BaFin hosted a seminar at the Central Bank of the Republic of Kosovo on the state of development of a future system for banking and securities trading supervision. In addition, BaFin provided support for the ongoing development of the Sino-German joint exchange venture CEINEX in Frankfurt am Main. BaFin also welcomed a number of delegations from China, in particular representatives of the China Securities Regulatory Commission (CSRC) and the National Development and Reform Commission of the People’s Republic of China (NDRC).

## 8.3 Montenegro twinning project

In the EU Twinning Project for the Republic of Montenegro, BaFin has assumed the project lead. Together with the supervisory authorities of Croatia, Nederlandsche Bank and the Deutsche Bundesbank, BaFin is providing support to Montenegro in the two-year project aimed at aligning its legislation with the totality of EU law. In addition to steering the project, BaFin’s key task involves supporting the country in creating a supervisory system for the insurance and securities sector.

BaFin provided training to the Montenegrin partner authorities in certain areas of securities and insurance supervision – such as the Alternative Investment Fund Managers (AIFM) Directive and issues relating to market abuse and Solvency II. The training is intended to enable the Montenegrin supervisory authorities to prepare their own national EU-compliant laws and to establish adequate ongoing supervision.

# 9 Risk modelling

## 9.1 Targeted Review of Internal Models

As part of the European Single Supervisory Mechanism (SSM), a project entitled “Targeted Review of Internal Models (TRIM)” was launched in 2015, in which the model experts of the national competent authorities and the ECB are working to ensure that within the SSM similar exposures are subject to the same capital requirements. Another objective of TRIM is to standardise and strengthen SSM model supervision. The intention is to restore trust in the use of internal model approaches, which was shaken by the financial crisis.

### Significant outcomes

TRIM achieved significant outcomes in all areas in 2018. For example, standardised supervisory expectations have been formulated for banks using models and the approaches to model reviews to be adopted by the supervisory authorities’ auditors have been harmonised.

The supervisory expectations developed during the project have been published in a draft “ECB Guide to Internal Models” as part of the consultation process with the banks. Consultation on the general model topics chapter has been completed; the revised version of this chapter has already been adopted and published

<sup>85</sup> See Appendix, page 193.

<sup>86</sup> For information on MoUs that BaFin entered into with supervisory authorities in China in January 2019, see BaFinJournal February 2019, page 7 (only available in German).

by the Supervisory Board and the Governing Council of the SSM.<sup>87</sup>

### Reviews as part of the TRIM project

The model reviews under the TRIM project are conducted in stages by model type. The process kicked off in 2017 and 2018 with models for market and counterparty risk and credit risk in high-default portfolios, such as residential mortgages and consumer loans. This was followed in 2018 with model reviews for credit risk in low-default portfolios, such as loans to banks. These reviews are continuing in 2019. A total of 200 reviews are planned as part of the TRIM project; by the end of 2018, over 60% had been completed.

The project work continues in 2019. Moreover, the conditions are to be created for continuing and enhancing the cooperation between the model experts of the national competent authorities and the ECB established in the TRIM project.

## 9.2 EIOPA comparative studies on internal models

Together with the national competent authorities, EIOPA organises comparative studies to enhance the consistency and convergence of internal model supervision.

### Market and Credit Risk Comparative Study

The second comparative study on internal models (Market and Credit Risk Comparative Study – MCRCS) in 2018 covered market and credit risk for investments. A total of 19 participants, primarily insurance groups from eight European countries, took part in the study as at 31 December 2017, thus achieving almost full coverage of the relevant models approved by the supervisory authorities. All relevant models approved in Germany were represented in the study.

These studies are carried out on a regular basis with the primary objective of conducting a systematic analysis of the model calibrations using synthetic financial instruments, which are suitably combined into portfolios. In simplified form, they represent the structure of investments of the entire European insurance market and of individual national markets. The study is based on a deliberate abstraction from the specific investment and the particular features of the specific business model. The individual risk profiles are, however, taken into account when the results are interpreted, and this is

in turn incorporated into BaFin's ongoing supervision of internal models. EIOPA published a summary of how the study was conducted and its results on 18 March 2019.<sup>88</sup>

### Non-Life Underwriting Risk Comparative Study

Another comparative study, which was conducted in 2018, analysed the model results from the underwriting risk category in property and casualty insurance (Non-Life Underwriting Risk Comparative Study – NLCS). Being the first study of its kind, it can be considered a pilot. Its participants comprise 35 insurance undertakings from 14 countries.

The scope of the study excludes catastrophe risk and focuses on analysing four segments: motor third party liability, other motor (in Germany this is normally collision damage insurance), fire and other damage to property and general third party liability. The project group requested the submission of data as at 31 December 2016 and 31 December 2017. In this process, it placed particular emphasis on including background information that can explain the differences between the segments. The NLCS differs in structure from the MCRCS in that it compares model results of segments that vary considerably in some cases, for example with regard to insurance products, the portfolio mix – i.e. retail, commercial and industrial customers – or liability limits. It is not possible to abstract from the specific portfolios in the same way as in the MCRCS study without sacrificing substantial informative value. The project group will complete the study by the middle of 2019. Future editions with an enlarged group of participants are already in the pipeline. Both studies should be understood in the context of the "EIOPA Supervisory Convergence Plan", which EIOPA first published in 2018. Internal models are one of the priority areas of this plan.<sup>89</sup> BaFin actively supports this work.

## 10 Sustainability

Major climate, environmental and also social change may hold material risks for financial undertakings or the financial market as a whole. BaFin resolved an initial sustainability programme in March 2018 that deals with these issues, with a focus on the core topics of information, risk management and regulation. BaFin also

<sup>87</sup> ECB guide to internal models, General topics chapter, March 2018.

<sup>88</sup> [https://eiopa.europa.eu/Pages/Supervision/Insurance/Data\\_request\\_for\\_MCRCS.aspx](https://eiopa.europa.eu/Pages/Supervision/Insurance/Data_request_for_MCRCS.aspx).

<sup>89</sup> <https://eiopa.europa.eu>.

established an internal cross-directorate network that deals with the issue of sustainability.

In May 2018, the European Commission published a number of legislative proposals, which focus mainly on a taxonomy<sup>90</sup>, disclosure requirements, sustainability benchmarks and the inclusion of ESG preferences in distribution activities in accordance with the Insurance Distribution Directive (IDD)<sup>91</sup> and MiFID II. BaFin generally takes a positive view of these proposals. It welcomed in particular the taxonomy and the disclosure requirements, even though it believed there was room for improvement in the detail, for example with regard to proportionality, the level of detail of the taxonomy and consistency with existing regulations.

In addition, BaFin assisted EIOPA and ESMA in fulfilling an assignment of the European Commission that required a response by April 2019. It involves the question of how sustainability risks should be incorporated into the business organisation, business operations and risk management of insurance undertakings and investment firms. Sustainability factors should also be considered when determining the target market in accordance with MiFID II.

BaFin also cooperated on preparing an EIOPA opinion on quantitative issues under Solvency II in 2018. The opinion, which is scheduled for completion in 2019, is meant to take a closer look at, among other aspects, existing incentives or possibly misplaced incentives for sustainable investments and the underwriting policies of insurance undertakings.

As part of the Network for Greening the Financial System<sup>92</sup>, BaFin deals with microprudential issues relating to climate risk and the effects climate change and the transformation of the energy system have on the macroeconomy and financial stability.

On 9 May 2019, BaFin will host a conference on "Sustainable Finance" to which high-ranking politicians, representatives of the scientific community and the finance industry will be invited. To accompany the event, a new issue in the BaFinPerspectives publication series featuring articles on sustainability by internal BaFin and external authors will be published at [www.bafin.de](http://www.bafin.de).

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90 A classification system for economic activities that are sustainable from an ecological perspective.

91 Directive (EU) 2016/97, OJ EU L 26/19.

92 The Central Banks and Supervisors Network for Greening the Financial System.

## 11 Financial accounting and reporting

### IFRS 9

In 2018, the European Banking Authority (EBA) surveyed credit institutions on the impact of the new financial reporting standard IFRS 9<sup>93</sup> and published the results in a report<sup>94</sup> released on 20 December 2018. The EBA had previously conducted impact assessments on IFRS 9<sup>95</sup> in 2017 and 2016, although they had been based on estimates.

For the first time since IFRS 9 entered into force on 1 January 2018, the analysis was based on actual data in the supervisory reporting system. The analysis of the data broadly confirmed the estimates provided by the institutions in the second impact assessment in 2017. The change in the CET1 ratio<sup>96</sup> following application of IFRS 9 declined by an average of 51 basis points; the average increase in provisions at credit institutions was 9% (previous year: -42 basis points and +13%). The EBA is planning to continue to analyse and report on the application of the new standard and its impact on the supervisory key figures. BaFin will be involved in these follow-up investigations as part of the relevant EBA working groups.

### IFRS 17

IFRS 17 has been a controversial debate topic ever since the International Accounting Standards Board (IASB) published the standard in May 2017.

The IASB is trying to win approval for and establish trust in its implementation by providing training and information material and setting up a Transition Resource Group. The members of this global group include representatives of insurance undertakings and auditing firms, as well as one observer each from the International Organization of Securities Commissions (IOSCO), the International Association of Insurance Supervisors (IAIS) and the International Actuarial Association (IAA).

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93 The abbreviation stands for "International Financial Reporting Standard". IFRSs are international reporting standards issued by the International Accounting Standards Board (IASB).

94 EBA report, First observations on the impact and implementation of IFRS 9 by EU institutions.

95 See 2017 Annual Report, page 64.

96 CET1 stands for Common Equity Tier 1 capital.

By the time of going to press<sup>97</sup>, the discussions have prompted the IASB to make substantive and technical changes to the standard to make it easier for insurance undertakings to implement it and to facilitate communication with investors and other stakeholders. The IASB is planning to publish a document in the middle of 2019 with information on the specific amendments.

In addition, the IASB has resolved to postpone the initial application date of IFRS 17 from 1 January 2021 to 1 January 2022. For insurance undertakings, this also means the postponement of the initial application date of IFRS 9 to prevent inconsistencies and contradictions in recognition and measurement and to allow matters to be presented as closely as possible to reality in the annual financial statements.

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<sup>97</sup> As at the time of going to press, 31 March 2019.

# III

## Supervision of banks, financial services providers and payment institutions





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# 1 Bases of supervision

## 1.1 Implementation of the Second Payment Services Directive

### Payment services

On 13 January 2018 the new German Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz – ZAG*) largely entered into force. It transposes the portion of the Second Payment Services Directive (PSD2) dealing with supervisory law into German law. PSD2 and the amended ZAG are intended to reflect the progressive digitalisation of payment transactions in the legal framework. Both are also intended to define the exemptions provided for in this context more clearly, and in doing so contribute to a consistent interpretation and application of the requirements across Europe.

### Security and competition in payment transactions

Among other things, the new provisions include the requirement to establish strong customer authentication in certain circumstances and – with the customer’s consent – to allow access to online payment accounts for regulated, supervised payment initiation and account information service providers. They also include the

supervisory requirements for controlling operational and security risks in payment transactions together with the related reporting obligations. The new provisions are intended to increase competition in payment transactions, enhance the security of payment services and improve protection for customers.

### Strong customer authentication

The provisions of the ZAG relating to strong customer authentication which will come into effect in September 2019 (see info box “Strong customer authentication” on page 66), will make the use of online banking services and payments via the internet in particular more secure in electronic payment transactions.

The new requirements for strong customer authentication are supplementary to a European Delegated Regulation. Application of these requirements is mandatory for payment service providers from 14 September 2019.

The ZAG and the Delegated Regulation specify when strong customer authentication is required. For example, strong customer authentication must be provided when the payer initiates an electronic payment transaction or accesses their payment account online.

## Definition

### Strong customer authentication

All computer users are familiar with authenticating themselves on a computer or a website – for example by entering a password. The requirement for strong customer authentication, however, demands authentication consisting of at least two elements. Those elements must belong to two of the three categories “knowledge”, “possession” and “inherence”. An example of the “knowledge”

category is a password. The mobile phone is a well-known example of the “possession” category: Possession of the device can be proved simply by entering a transaction authentication number (TAN) which has been received on the personal phone. Elements in the “inherence” category are personal or physical identifying features of the users, such as a fingerprint.

### Initiation of electronic payments

A payer initiates an electronic payment, for example, if they pay at the supermarket checkout using their card and personal identification number (PIN) – which is in principle sufficient to meet the requirements for strong customer authentication in this particular application.

If the electronic payment initiated constitutes a remote payment transaction, for example if the payer makes a credit transfer using online banking or a credit card payment on the internet, the strong customer authentication must also include a dynamic link. This takes the form of “dynamically linking” the payee and the amount. This means linking the payment transaction to a specific payee and a specific amount. This further means that a payment service provider, for example, when transmitting a TAN by SMS, must inform the payer of the amount and payee for which the TAN is valid. Any modification of this payment data renders the TAN transmitted invalid.

The Delegated Regulation also defines circumstances in which the payment service providers can dispense with strong customer authentication. Contactless card payments, which are increasingly being used at the point of sale, for example in supermarkets, in Germany and other countries, are an example of such an exemption – subject to certain preconditions.

### Reporting system

The new reporting system for serious security incidents in payment transactions has been available for use since 13 January 2018. More than 650 reports relating to nearly 300 incidents had been submitted via the system by the year-end. It replaced the previous reporting system under the minimum requirements for the security of internet payments (*Mindestanforderungen an die Sicherheit von Internetzahlungen*). Serious security

incidents should now only be reported using the new reporting forms and via BaFin’s reporting and publishing platform, the MVP Portal. The European Banking Authority (EBA) has also published guidelines<sup>1</sup> on the issue of when a security incident is regarded as serious and therefore has to be reported. BaFin has incorporated these guidelines into its supervisory practice by means of Circular 08/2018 (BA)<sup>2</sup>.

## 1.2 Developments at global level

### 1.2.1 Changes to the Basel framework from 2022

The oversight body of the Basel Committee on Banking Supervision, the Group of Governors and Heads of Supervision (GHOS), decided on changes to the Basel market risk framework with effect as at 1 January 2022 at its meeting in mid-January 2019. The framework contains the revised standards for calculating market risk<sup>3</sup> for banks and was published on the same day.

The newly agreed framework includes changes compared with the draft from 2016. For the purpose of the revisions, the GHOS took into account the data from the 2017 and 2018 Basel impact studies (Basel III monitoring exercise). The most significant changes consist of the introduction of a simplified standardised approach for banks with a low level of trading activity, a clearer definition of the trading book boundary, the adjustment of risk weights in the standardised approach

1 [https://eba.europa.eu/documents/10180/2081899/Guidelines+on+the+security+measures+under+PSD2+%28EBA-GL-2017-17%29\\_EN.pdf/c63cfcfb-7412-4cfb-8e07-47a05d016417](https://eba.europa.eu/documents/10180/2081899/Guidelines+on+the+security+measures+under+PSD2+%28EBA-GL-2017-17%29_EN.pdf/c63cfcfb-7412-4cfb-8e07-47a05d016417).

2 Circular 8/2018 (BA).

3 <https://www.bis.org/bcbs/publ/d457.pdf>.

and updated requirements for the identification of risk factors that can be used for internal modelling purposes. The simplified standardised approach is similar to the current Basel II.5 standardised approach, with the risk weights of individual risk classes recalibrated.

The GHOS also published an explanatory note<sup>4</sup> to assist the industry and supervisors in implementing the new framework. It describes and explains the principal changes compared with the current requirements, and gives practical examples for using the new standardised approach, which is based on the first derivatives of the portfolio value with respect to different risk factors.

The new framework will be transposed into European law in the course of revising the European Capital Requirements Regulation (CRR). Some detailed provisions will be implemented by the European Banking Authority (EBA) with mandates for regulatory technical standards (RTS).

### 1.3 Developments at European level

#### 1.3.1 Reform of the Capital Requirements Regulation and the Capital Requirements Directive

At the beginning of December 2018, European finance ministers agreed on wide-ranging reforms to strengthen the European banking sector. The European Commission had submitted a package of reform proposals for the revision of the Capital Requirements Regulation (CRR) and the Capital Requirements Directive IV (CRD IV) at the end of 2016. The trilogue of European Commission, European Council and European Parliament started in July 2018 and gathered momentum from September 2018. The European Council and European Parliament are expected to make a decision on the package in the first months of 2019. The revisions to the CRR will then apply directly in most cases two years after they come into force. However, there will be exceptions for individual provisions with regard to both earlier and later direct application. The period for transposing the amended CRD into national law is likely to be 18 months after the revised version comes into force for the majority of the articles.

##### **Intensive trilogue negotiations**

The trilogue negotiations crystallised a number of issues on which the Economic and Financial Affairs Council and the European Parliament held different opinions.

They included the net stable funding ratio (NSFR)<sup>5</sup>, the leverage ratio and the measurement of credit risk, among others. The question of own funds also generated a variety of contentious points. These related in particular to the long-term impairment of capitalised software, distributable items, the treatment of own funds linked to a profit and loss transfer agreement, and also the level of the minimum requirement for own funds and eligible liabilities (MREL). A number of other topics were also disputed, such as the treatment of intermediate parent companies and the question of the extent to which infrastructure projects or assets dedicated to environmental or social objectives should be supported by specific capital requirements (“green supporting” or “brown penalising” factor).

#### 1.3.2 Proportionality

An important question for the revision of the CRR and CRD IV was where and to what extent it is possible to ensure greater proportionality in the supervisory legal framework. The supervisory regulations should be sufficiently flexible to take into account the size and complexity of institutions to a certain degree. For example, are the supervisory guidelines and requirements that are appropriate for the supervision of a large international bank equally suitable for supervising a small regional institution? For the purposes of the revision of the CRR and CRD IV, therefore, it was firstly a matter of identifying general issues and individual standards for which simplifications based on the size of the institution are appropriate, and then deciding how they should be structured. Secondly, it was necessary to define the institutions to which the new simplifications are intended to apply, i.e. at what point a bank is “small” or “large”.

##### **Simplifications for small banks**

In various areas of the CRR and CRD IV, it was possible to develop approaches for a proportionate gradation of the supervisory requirements. Relevant simplifications for small banks apply above all to disclosure and reporting requirements and to liquidity management. For example, there will be a differentiated system especially for disclosures to determine which requirements will specifically apply only to large institutions and which requirements small, non-complex institutions must also comply with. But small, non-complex institutions will also be allowed simplifications, of a significant nature in some cases, in other areas of supervisory law, such as the calculation of the NSFR

4 [https://www.bis.org/bcbs/publ/d457\\_note.pdf](https://www.bis.org/bcbs/publ/d457_note.pdf).

5 See 2017 Annual Report, page 71.

and the remuneration rules. It is also particularly noteworthy that the CRR envisages a mandate for the EBA on the issue of proportionality. The EBA is tasked with preparing a report containing proposals on how to achieve future cost savings for institutions of at least 10% and ideally 20% by means of simplifications in the supervisory requirements affecting reporting and disclosure.

#### **Definition of “small, non-complex institutions”**

In addition, the CRR will in future define the concepts “small, non-complex institutions” and “large institutions” more precisely in Article 4. The new definition of small, non-complex institutions stipulates an absolute threshold according to which average total assets over the past four years may not exceed €5 billion. The EU member states concerned may reduce this threshold to a figure for total assets of €200 million if necessary. This will enable smaller member states to adjust the threshold to reflect the particular circumstances of their banking markets. The intention is to avoid a situation in which too large a portion of the national banking market is only subject to simplified rules, since otherwise this could endanger national financial stability.

In addition to this key threshold, the definition of small and non-complex institutions also includes a number of qualitative criteria: For example, the institution must be exempt from the requirements for recovery and resolution planning<sup>6</sup> or have the option of complying with simplified requirements. Furthermore, the institution’s trading book business must be classified as “small” within the meaning of the CRR. The derivatives positions held by the institution must not exceed specified thresholds in relation to total assets. The institution’s assets and liabilities must be mainly limited to activities within the European internal market. It may also not employ internal models for the purpose of complying with the supervisory requirements.

Moreover, the competent supervisory authority will be permitted to decline to classify individual institutions as “small” and “non-complex” on the basis of specific criteria. This will be most likely to occur if a bank cannot be classified as “small” or “less complex” from an objective point of view due to its specific risk profile, its business model or its interconnectedness within the financial market although the institution actually satisfies the criteria. Conversely, institutions covered by the definition may also decide voluntarily against classification as “small” and “non-complex” – they will

then continue to be subject to the requirements of the CRR and CRD IV in full.

#### **Definition of “large Institutions”**

An institution will be considered to be a “large institution” within the meaning of the CRR in future, if:

- it is classified as a global systemically important institution (G-SII) or
- as another systemically important institution (O-SII) within the meaning of CRD IV;
- it is one of the three largest institutions – measured by total assets – in its home country or
- its total assets on an individual or a consolidated basis amount to €30 billion or more.

On the basis of the definitions of “small”, “non-complex” and “large institutions”, there now exists a general framework which will permit simplifications and/or differentiations in applying the supervisory regulations in future in accordance with the principle of proportionality. This framework goes beyond the specific individual measures in the applicable version of the CRR and CRD IV.

### **1.3.3 EU harmonisation of covered bonds**

The European Union’s legislative project for the harmonisation of national regulations on covered bonds made significant progress in 2018. It comprises the adoption for the first time of a directive setting out the minimum requirements for structuring covered bonds – Covered Bond Directive (CBD) – together with amendments to the preferential treatment for risk weighting purposes under Article 129 of the CRR. The Council of the European Union, European Parliament and EU Commission completed their trilogue in the first quarter of 2019 so that these regulations can still be adopted in the current legislative period, which runs until the EU Parliamentary elections in May 2019.

#### **Minimum standard for covered bonds**

The CBD Directive will simply establish central principles for national covered bond regulations and in so doing set a minimum standard. It can therefore be assumed that the European proposals will largely correspond to the high standard of quality set by the German *Pfandbrief* legislation. From a German point of view, the initial effects of harmonisation should therefore be limited, since the principles make great allowance for the particular national characteristics of established regimes. The German *Pfandbrief* will also benefit from this. Overall, therefore, the regulatory framework primarily creates a justification under European law for the

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<sup>6</sup> Directive (EU) 2014/59, OJ EU 173/190.

preferential treatment and special rules already applying to covered bonds, including the German *Pfandbrief*, under EU financial market regulation.

The matters requiring most discussion in the trilogue were the rules on assets eligible as cover and the extent to which loans to banks rated credit quality step 3 are permitted for preferential risk weighting treatment under the CRR. Since framework provisions for covered bonds are being issued under EU law for the first time, a relatively lengthy implementation period can be expected. Even though the aim is simply to achieve a minimum level of harmonisation taking into account national specificities, it will be necessary to amend German law relating to covered bonds, including the *Pfandbrief* legislation.

### 1.3.4 EBA Guidelines on outsourcing arrangements

The EBA in collaboration with BaFin has revised the guidelines issued by the Committee of European Banking Supervisors (CEBS) in 2006, and the new version was published in February 2019.<sup>7</sup> The revision exercise had become necessary in particular in view of the continuing process of digitalisation and new Fintech business models which rely on outsourcing to a high degree. An increasing trend was also observed on the part of traditional credit institutions towards outsourcing functions or activities in order to save costs or enhance efficiency. The EBA's recommendations on outsourcing to cloud service providers<sup>8</sup>, adopted at the end of 2017, have been integrated into the new guidelines and will cease to be applicable once the guidelines come into force (as a result of implementation at national level). The same applies to the old CEBS guidelines.

The new guidelines are intended to strengthen the powers and areas of responsibility of the credit institutions' internal audit functions in relation to the service provider and similarly the areas of responsibility of the supervisory authorities as well: Both are granted unrestricted access and auditing rights at the service provider for their purposes. In addition, all institutions must maintain an outsourcing register to enable the institution to identify concentration risks. The register must also be made available to the supervisory authority on request, which will thus be able to evaluate concentration risks in the financial sector as a whole over and above those affecting individual institutions.

<sup>7</sup> EBA/GL/2019/02.

<sup>8</sup> See chapter II 6.3.

## 1.4 Regulations

### 1.4.1 Remuneration Regulation for Institutions

On 16 February 2018, BaFin published its updated interpretative guidance<sup>9</sup> on the amended German Remuneration Regulation for Institutions (*Institutsvergütungsverordnung*). The interpretative guidance relates to the version of the Remuneration Regulation that came into force on 4 August 2017 and replaces the previous version dated 1 January 2014.

The revision of the Remuneration Regulation is intended to implement the essential guidelines<sup>10</sup> for sound remuneration policies issued by the EBA. The existing structure of the regulations on remuneration systems remained in place. This relates to proportionality for both institutions and employees, i.e. the classification of the institutions as significant or non-significant together with the division of employees into risk takers and non-risk takers and the associated requirements.

The main new features in the amended Remuneration Regulation consist of a clearer contouring of the types of remuneration and greater differentiation in the treatment of the different forms of variable remuneration such as severance payments and retention bonuses. Other changes relate to the specification of the ex post risk adjustment together with new clawback clauses which allow variable remuneration components already paid out to be reclaimed. Also new is the obligation to use instruments eligible for bail-in as well when paying variable remuneration components. The amended Remuneration Regulation also specifies in detail the obligation to establish and implement a group-wide remuneration strategy and to identify group risk takers.

### 1.4.2 Liquidity Regulation

BaFin has revised the German Liquidity Regulation (*Liquiditätsverordnung*) in consultation with the Deutsche Bundesbank. The principal new feature is the reduction in its scope. The Amending Regulation<sup>11</sup> entered into force on 1 January 2018.

<sup>9</sup> [www.bafin.de/dok/7864044](http://www.bafin.de/dok/7864044).

<sup>10</sup> Guidelines on sound remuneration policies under Articles 74(3) and 75(2) of Directive 2013/36/EU and disclosures under Article 450 of Regulation (EU) No 575/2013.

<sup>11</sup> Federal Law Gazette I 2017, page 4033.

As a consequence, the provisions of the Liquidity Regulation need only be observed by institutions which do not have to apply the liquidity requirements of Articles 411 to 428 of the CRR. CRR investment firms<sup>12</sup> therefore fall within the scope of the Liquidity Regulation. Nevertheless, firms of this type can obtain exemption subject to certain conditions: This is the case if they are part of a group which has to comply with the liquidity coverage ratio (LCR) at group level. This ensures that liquidity risks are managed and limited at group level.

The background to the amendments is that under Article 412 (5) of the CRR, EU member states may maintain national provisions in the area of liquidity requirements only until binding minimum standards for liquidity coverage requirements have been fully introduced in accordance with Article 460 of the CRR. This has been the case since 1 January 2018. Since that date, the member states have been required to comply with the liquidity coverage ratio at 100%.

On behalf of the European Commission, the EBA had previously examined the impact of a phased increase in the LCR to 100% by 2018. The purpose was to assess whether the introduction should be delayed by one year. In its report<sup>13</sup>, the EBA finally concluded that this was not necessary.

### 1.4.3 Country Risk Regulation and amendment of the Regulation Governing Large Exposures and Loans of €1 Million or More

In consultation with the Deutsche Bundesbank, BaFin repealed the Country Risk Regulation (*Länderrisikoverordnung*) as at 1 January 2018, since the relevant information it contained for bank supervisory purposes has now been incorporated into the reporting system for loans of €1m or more. BaFin also updated the Regulation Governing Large Exposures and Loans of €1 Million or More (*Großkredit- und Millionenkreditverordnung – GroMiKV*) by means of an amending regulation.

As a result of the amendment of section 2 (3) of the GroMiKV which came into effect on 1 January 2018, BaFin can, in particular cases, also respond to business

models of groups of institutions with back-to-back solutions at the request of the institution and, subject to certain conditions, can exempt risk positions with respect to group entities from the calculation of the utilisation of the upper limit for large exposures. Groups of institutions with central risk management are now allowed the same discretion regarding risk positions relating to large exposures with respect to other group entities as groups with central liquidity management. In addition, section 2 (5) of the GroMiKV has expanded the scope of the exemption for particular risk positions within networks. Previously, positions that only involved creditors' rights but no membership rights and qualified as Tier 2 capital could not be counted towards the large exposure limit using a reduced rate.

The reporting system for loans of €1m or more was also updated as at 1 January 2019. It is now restricted solely to bank supervisory objectives. The amended Regulation therefore dispenses with new reporting forms with wide-ranging reporting requirements that would originally have come into effect on 1 January 2019. Instead, the reporting forms currently in use have been retained and are merely being expanded.

### 1.4.4 Financial and Internal Capital Adequacy Information Regulation

In July 2018, BaFin issued the Second Regulation Amending the Financial and Internal Capital Adequacy Information Regulation (*Zweite Verordnung zur Änderung der Finanz- und Risikotragfähigkeitsinformationenverordnung*)<sup>14</sup> in consultation with the Deutsche Bundesbank. It permits a number of simplifications for institutions required to report financial information to BaFin.

The institutions have been able to use the extended periods for submitting information provided for by the Amending Regulation from that date. Certain reporting forms are also no longer required and do not have to be submitted. There was a transitional period for the updated reporting forms until 31 December 2018.

## 1.5 BaFin circulars and guidance notices

### 1.5.1 Circular on interest rate risk

In June 2018, BaFin published the revised Circular 9/2018 (BA) on interest rate risk in the banking book. In conjunction with the new Minimum Requirements

<sup>12</sup> See section 2 (9d) of the German Banking Act (*Kreditwesengesetz*).

<sup>13</sup> The EBA Report on Liquidity Measures under Article 509(1) and the Review of the Phase-in of the Liquidity Coverage Requirement under Article 461(1) of the CRR, EBA/Op/2016/22.

<sup>14</sup> Federal Law Gazette I 2018, page 1086.

for Risk Management (*Mindestanforderungen an das Risikomanagement*) published in 2017, the Circular implements the EBA guidelines on the management of interest rate risk arising from non-trading activities<sup>15</sup> in German supervisory law, thus contributing to the gradual harmonisation of the supervisory treatment of interest rate risks in the banking book in Europe.

As a risk of the traditional banking business, interest rate risk in the banking book is one of the most significant risks for German credit institutions. The persistent low interest rate environment does not just weigh on banks' net interest income; it also increases the incentive to intensify their maturity transformation activities. This in turn results in higher interest rate risks for the institutions.

### New developments

As before, the new Circular restricts itself to providing guidance on how to calculate the supervisory interest rate shock under section 25a (2) of the German Banking Act (*Kreditwesengesetz*). The main new developments are the removal of the alternative procedure and the detailed definition of various terms. The institutions are required to determine the impact of a sudden and unexpected change in the yield curve of  $\pm 200$  basis points on the economic value of their banking business (interest book present value) on the basis of their internal methods. If an institution's regulatory own funds fall by more than 20% in one of the two scenarios (interest rate increase or reduction), the institution is considered to have a heightened interest rate risk.

BaFin will continue to support the institutions' freedom to choose the method of calculating and managing interest rate risk. The provisions of the new Circular on the calculation of the supervisory interest rate shock simply provide the institutions with guidelines for the banks' internal methods, which are intended to contribute to a comparable risk measurement of German credit institutions. This is especially important for the capital charge for interest rate risks in the banking book in the context of the Pillar II capital requirement, in order to ensure equal treatment of the institutions.

## 1.5.2 Minimum requirements for complaints management

In May 2018, BaFin published Circular 06/2018 on the minimum requirements for complaints management.<sup>16</sup>

<sup>15</sup> EBA/GL/2015/08.

<sup>16</sup> [www.bafin.de/dok/10785998](http://www.bafin.de/dok/10785998).

It describes the minimum requirements for complaints management applying to CRR credit institutions, asset management companies, payment institutions and e-money institutions. It is intended to ensure a consistent approach to complaints from customers and investors.

The Circular sets out the detailed requirements for the proper handling of complaints by the undertakings supervised. The undertakings are required to establish a complaints management function and to document all complaints, their processing, measures taken and final decisions in an internal complaints register, among other things.

The Circular also implements the guidelines for complaints-handling for the securities and banking sectors issued by the Joint Committee of the European Supervisory Authorities<sup>17</sup>. Until further notice BaFin will not, however, issue the general administrative act submitted for consultation together with the Circular in summer 2017, which was intended to introduce a reporting obligation for complaints for CRR credit institutions<sup>18</sup>.

### Investment firms

Corresponding details for complaints management in investment firms can be found in BaFin Circular 05/2018<sup>19</sup> published in April, which sets out the minimum requirements for the compliance function and additional requirements governing rules of conduct, organisation and transparency for investment firms (*Mindestanforderungen an die Compliance-Funktion und die weiteren Verhaltens-, Organisations- und Transparenzpflichten für Wertpapierdienstleistungsunternehmen*).

## 1.6 Internal capital adequacy guidelines

BaFin and the Deutsche Bundesbank jointly revised the guidelines for the supervisory assessment of banks' internal capital adequacy approaches<sup>20</sup> and published them in May 2018 (see info box on page 72). The fundamental restructuring of the guidelines established a new basis for the criteria they employ to assess banks' internal capital adequacy concepts and the integration of the relevant processes into the overall management

<sup>17</sup> Final Report on guidelines for complaints-handling for the securities (ESMA) and banking (EBA) sectors, Doc.-No. JC 2014 43.

<sup>18</sup> See BaFinJournal July 2017, page 33 (only available in German).

<sup>19</sup> [www.bafin.de/dok/10744966](http://www.bafin.de/dok/10744966).

<sup>20</sup> [www.bafin.de/dok/10923076](http://www.bafin.de/dok/10923076).

of the bank (Internal Capital Adequacy Assessment Process – ICAAP). This represented a comprehensive response to recent developments within the Single Supervisory Mechanism (SSM).

The guidelines now include a normative and an economic perspective, capital planning covering at least three years and appropriate stress tests as part of the ICAAP. Prior to the publication of the new guidelines, BaFin had given market participants the opportunity to comment on the draft.

#### Definition

### Internal capital adequacy guidelines

The guidelines on the supervisory assessment of banks' internal capital adequacy concepts set out in detail BaFin's expectations and assessment standards for individual elements of the banks' internal procedures for ensuring capital adequacy. These procedures are of great importance for the management of the banks. Their design and structure are essentially governed by the Banking Act and the Minimum Requirements for Risk Management (*Mindestanforderungen an das Risikomanagement der Banken*).

#### Conference

On 29 May 2018, a conference on the new guidelines was held in Bonn, where BaFin together with the Deutsche Bundesbank provided extensive information on the specific contents of the guidelines and the background considerations to the parties to whom they are addressed. The European Central Bank's corresponding ICAAP guide<sup>21</sup> and possible implementation steps in banking practice were also discussed. Representatives of the institutions under supervision and their associations were able to obtain information about the new developments in situ at the conference and put their questions in a direct exchange with BaFin.

<sup>21</sup> ECB Guide to the internal capital adequacy assessment process (ICAAP), see [https://www.bankingsupervision.europa.eu/legalframework/publiccons/pdf/icaap\\_ilaap/ssm.icaap\\_guide\\_201803.en.pdf](https://www.bankingsupervision.europa.eu/legalframework/publiccons/pdf/icaap_ilaap/ssm.icaap_guide_201803.en.pdf).

## 2 Supervision in practice

### 2.1 German institutions directly supervised by the SSM<sup>22</sup>

#### 2.1.1 Supervision of significant institutions

As in the previous year, a total of 19 German groups of institutions and several foreign institutions with a strong presence in Germany (including German subsidiaries of foreign groups of institutions) were directly supervised by the European Central Bank (ECB) under the Single Supervisory Mechanism (SSM) (see Table 40 "German institutions supervised by the ECB under the SSM", Appendix on page 173).

With the launch of the SSM in November 2014, the ECB had taken over the direct supervision of those banking groups classified as significant. A joint supervisory team (JST) has been responsible for each of these significant institutions (SIs) since then.

#### Around 100 BaFin employees in joint supervisory teams

In addition to employees of the ECB, the teams also include staff from the national supervisory authorities and therefore also from BaFin and the Bundesbank. The number of members in each JST and its composition vary depending on the size and complexity of the banking group. In 2018, around 100 BaFin employees collaborated in the JSTs. They contributed a German supervisory perspective to the teams, in addition to their experience and expertise. Each of the JSTs is headed up by a JST coordinator from the ECB. For German SIs, the core JST consists of the JST coordinator together with one sub-coordinator from each of BaFin and the Bundesbank.

BaFin President Felix Hufeld is a voting member of the Supervisory Board, the primary decision-making body of the SSM.

#### 2.1.2 Work in the joint supervisory teams

The BaFin employees in the JSTs participated among other things in the supervisory review and evaluation process (SREP), the centrepiece of micro-prudential banking supervision from which the

<sup>22</sup> Further information on supervision in the SSM can be found in the ECB's annual report: <https://www.ecb.europa.eu/pub/annual/html/index.en.html>.



specific capital requirements for each institution are derived.<sup>23</sup> In addition, they were involved in more than 1,000 meetings and collaborated in over 80 thematic reviews and deep dives in all risk categories. BaFin's employees also contributed their expertise acquired over many years to ordering and following up on supervisory inspections and again assisted with the EBA stress test in 2018.

### Review of the profitability and business models of the significant institutions

The JSTs conducted a thematic review of the profitability and business models of the SIs in 2018. They examined the viability and sustainability of the banks' business plans and focused on their strategic controllability, i.e. the question of whether the banks can achieve their long-term objectives.

The review had started in 2016 with the development of the methodology and the instruments. In the following year, the JSTs performed the individual analyses and assessments interacting directly with the institutions. This was followed by a horizontal benchmark comparison for quality control purposes. In 2018, the JSTs first of all presented the preliminary findings to the banks in supervisory consultations, and informed them subsequently of the final findings and recommendations – together with timetables for their implementation. The results of the review were also included in the 2018 SREP. The JSTs will also follow up the implementation of their recommendations in 2019.

### Results of the review

According to the review, the principal challenges facing the banks are to analyse their earnings drivers in detail using sensitivity and scenario analyses, to allocate their costs in full to business or distribution activities and to establish their margins for credit risks (including minimum pricing for loans) on the basis of a consistently applied policy. The institutions also need to integrate their risk management functions more closely into their business planning, to critically examine the assumptions underlying the business plan, then to link these assumptions with their risk appetite and the ICAAP and also to involve significant subsidiaries in the planning process. The ECB published a report on the combined findings of the review on 18 September 2018.<sup>24</sup>

<sup>23</sup> For details of the SREP for less significant institutions directly supervised by BaFin, see 2.2.2.

<sup>24</sup> [https://www.bankingsupervision.europa.eu/press/pr/date/2018/html/ssm.pr180918/ssm.pr180918\\_FAQ.en.html](https://www.bankingsupervision.europa.eu/press/pr/date/2018/html/ssm.pr180918/ssm.pr180918_FAQ.en.html).

## 2.2 Institutions under German supervision

### 2.2.1 Less significant and other institutions supervised by BaFin

BaFin's Banking Supervision Sector was responsible for supervising 1,521 credit institutions subject to special audits at the end of 2018 (see Table 14 "Number of institutions by group of institutions").<sup>25</sup> 59 of them were classified as significant institutions and were therefore directly supervised by the ECB (see Table 40 "German institutions supervised by the ECB under the SSM", Appendix on page 173).<sup>26</sup> Responsibility for most of the institutions, the 1,407 less significant institutions (LSIs), rested with BaFin as the national competent authority (NCA) in the context of the SSM, and therefore only indirectly with the ECB.

**Table 14: Number of institutions by group of institutions**

As at 31 December 2018

	2018	2017	2016
Commercial banks*	185	170	171
(of which SIs)	33	37	37
Institutions belonging to the savings bank sector	392	398	412
(of which SIs)	9	10	11
Institutions belonging to the cooperative sector	879	919	976
(of which SIs)	3	3	3
Other institutions	65	66	69
(of which SIs)	14	13	15
<b>Total</b>	<b>1,521</b>	<b>1,553</b>	<b>1,628</b>

\* The group of commercial banks was expanded in 2018 to include 20 credit institutions classified as branches under section 53 of the Banking Act.

<sup>25</sup> On the institutions supervised by the Securities Supervision/Asset Management Sector, see 2.4. On the definition of "credit institution" and the number of authorised institutions in Germany, see the Appendix, page 172.

<sup>26</sup> The table includes all 59 individual institutions domiciled in Germany that are supervised in the SSM. See the Appendix, page 173.

55<sup>27</sup> of the 1,521 institutions were not subject to supervision under the SSM; German banking supervision is solely responsible for these institutions. As before, the number of institutions under supervision is declining.

### Division into groups

In Germany, the banks are divided into the following four groups of institutions: commercial banks, institutions belonging to the savings bank sector, institutions belonging to the cooperative sector and other institutions. The group of commercial banks includes the major German banks, subsidiaries of foreign banks and the private banks. The group of other institutions includes, among others, *Bausparkassen*, guarantee banks and special-purpose credit institutions.

From 2018, Banking Supervision has also been responsible for 492 institutions classified as financial services institutions (excluding stock exchange brokers) which were previously supervised by Prevention of Money Laundering. They also belong to the "Other institutions" group.

## 2.2.2 SREP in Germany

In the context of Pillar 2 at national level, BaFin and the Deutsche Bundesbank, the national competent authorities, conduct a wide-ranging examination and assessment, the Supervisory Review and Evaluation Process (SREP), of the risks to which the individual less significant institutions (LSIs) subject to direct national supervision are exposed. They also assess in a regular cycle whether these institutions have sufficient own funds to cover existing and foreseeable risks – to the extent that they can be capitalised – (SREP capital quantification), and determine where necessary an institution-specific capital requirement going beyond the Pillar 1 provisions to provide capital backing for the Pillar 2 risks (Pillar 2 requirement – P2R).

### Supervisory authorities introduce fixed cycle for institutions

In 2016 and 2017, BaFin and the Deutsche Bundesbank implemented the SREP in full for the first time and also performed the SREP capital quantification for each LSI as a newly introduced component of the process. For this purpose, they first of all divided the institutions into two tranches according to proportionality and risk criteria, so

that an SREP capital requirement was calculated for each LSI at the latest in 2017. In order to transfer the SREP capital quantification into a standard process from 2018 following this successful start, BaFin and the Deutsche Bundesbank specified a fixed individual cycle for each LSI which is described below.<sup>28</sup> The focus here is on the SREP capital quantification which, in contrast to the overall evaluation of the institution in the context of the SREP, does not have to take place annually.

### EBA capital quantification requirements

Under the EBA's SREP Guidelines, the national supervisory authorities are to perform the SREP capital quantification on a regular basis – every twelve months to every three years. If the supervisory authority obtains materially new findings, however, it can also depart from the scheduled regular cycle.

The EBA's SREP Guidelines set out the following categories:

#### Category 1:

- global systemically important institutions (G-SIIs)
- other systemically important institutions (O-SIIs)
- any other institutions determined by the competent authorities, based on an assessment of the institution's size and internal organisation and the nature, scope and complexity of its activities

#### Category 2:

- all medium to large institutions other than those included in Category 1 that operate domestically or with sizeable cross-border activities, operating in several business lines – including non-banking activities – and offering credit and financial products to retail and corporate customers
- non-systemically important specialised institutions with significant market shares in their lines of business, payment systems or financial exchanges.

#### Category 3:

- small to medium institutions that do not qualify for Category 1 or 2, operating domestically or with non-significant cross-border operations, and operating in a limited number of business lines, offering predominantly credit products to retail and corporate customers with a limited offering of financial products
- specialised institutions with less significant market shares in their lines of business, payment systems or financial exchanges.

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27 These consist, for example, of securities trading banks, branches in accordance with section 53 of the Banking Act and other credit institutions. Responsibility for the supervision of credit institutions by the ECB is derived from the SSM Regulation.

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28 See BaFinJournal July 2018, page 11 ff.

**Table 15: Cycle by EBA category**

Category	Evaluation of all SREP elements including capital quantification*	Summary of the overall evaluation
1	Annually	Annually
2	Every two years	Annually
3 <sup>29</sup>	Every three years	Annually
4	Every three years	Annually

\* Minimum frequency

#### Category 4:

- all other small non-complex domestic institutions that do not fall into Categories 1 to 3 (e.g. Institutions with a limited scope of activities and non-significant market shares in their lines of business).

The categorisation determines the minimum cycle according to which the national competent authority must carry out the SREP capital quantification, in addition to the overall evaluation of the institution which in Germany is based on the risk profile (see Table 15 "Cycle by EBA category").

#### Individual cycle of SREP capital quantification cycle for German institutions

BaFin and the Deutsche Bundesbank categorised the LSIs in accordance with these requirements, which the ECB also observes for the purposes of the SREP for the SIs. The majority of the German institutions currently fall into categories three and four. They are therefore subject to a three-year cycle for the SREP capital quantification. The key factors for the categorisation based on the principle of proportionality were firstly the significance of the particular institution for the financial system, mainly on the basis of its size and complexity ("potential impact of a solvency or liquidity crisis of the institution on the stability of the financial sector"), and secondly its risk position ("quality of the institution").

The allocation of an institution to a category determines the fixed cycle for its SREP capital quantification. The capital quantification is brought forward only if the risk position of an institution deteriorates drastically or if its situation is materially changed, for example in a merger.

#### Target own funds ratio

The details above relate solely to the determination of the capital requirement for backing the Pillar 2 risks (P2R). They do not determine the cycle for the target own funds ratio, which represents the German equivalent of the Pillar 2 guidance (P2G) and is therefore another component of the Pillar 2 requirements. To date, this has been a two-year cycle, since the target own funds ratio is based on the results of the national stress test which is carried out every two years. The next stress test will take place in 2019, so that all LSIs will be informed of a new target own funds ratio in 2019.

While the institutions may publish their individual SREP capital requirement in percent, the target own funds ratio is an indicator used solely for internal supervisory purposes. The target own funds ratio expresses the amount of capital an institution should maintain from a supervisory point of view, so that it can comply with the SREP overall capital requirement at all times over the long term and after taking into account potential losses in stress phases.

#### 2.2.3 Risk classification

The EBA SREP Guidelines require BaFin and the Deutsche Bundesbank to assess the risk profiles of all LSIs, the less significant institutions, on an annual basis (see Table 16 "Risk classification results of LSIs in 2018" on page 76). BaFin uses the risk profile to classify each institution into risk classes from 1 to 4 according to the categories "quality of the institution" and "potential impact of a solvency or liquidity crisis of the institution on the stability of the financial sector".

It derives the necessary supervisory measures from this overall assessment and determines the intensity of the supervision on the basis of the principle of proportionality.

<sup>29</sup> The cycle for categories 3 and 4 is identical; but categorisation has other supervisory consequences in addition to determining the cycle.

**Table 16: Risk classification results of LSIs in 2018**

As at 31 December 2018

Institutions in %		Quality				
Risk matrix	1	2	3	4	Total	
Impact	High	0.1	0.4	0.1	0	0.6
	Medium	4.1	8.8	1.8	0.1	14.8
	Medium-low	13.7	36.3	5.2	0.3	55.5
	Low	4.8	17.2	6.3	0.8	29.1
<b>Total</b>	<b>22.7</b>	<b>62.7</b>	<b>13.4</b>	<b>1.2</b>	<b>100.0</b>	

\* This table presents the LSIs under the supervision of the Banking Supervision Sector.

There were only marginal changes in the allocation of the institutions to the individual risk classes in 2018 compared with the previous year.

## 2.2.4 Special audits

BaFin ordered 153 special audits pursuant to section 44 (1) sentence 2 of the Banking Act for less significant institutions subject to supervision by the Banking Supervision Sector (see Table 17 "Breakdown of special audits of LSIs by areas of emphasis"). 10.9% of the LSIs supervised were therefore required to undergo a special audit. As in the previous year, the audits mainly related to section 25a (1) of the Banking Act. They are used to monitor the appropriateness of an institution's risk management system. The MaRisk set out the minimum requirements in detail. Among other things, they include provisions for the design of an institution's internal control system, its organisational and operational structure and, in particular, its risk management processes.

### Increased information requirement

BaFin always orders special audits pursuant to section 44 (1) sentence 2 of the Banking Act if it identifies a greater need for information than is covered by the regular sources of information, such as the reporting system, the direct exchange of information with the institutions and the audit reports on the annual financial statements. BaFin may order an audit pursuant to section 44 of the Banking Act either for a specific reason or if the previous special audit was too long ago. The special audits also include cover audits which must normally be carried out every two years in accordance with the statutory provisions in the *Pfandbrief Act*. Banks may also request special audits themselves, if they intend to use internal models and BaFin's approval

is required. For most special audits, BaFin instructs the Deutsche Bundesbank which then also carries them out. In some cases, external auditors also undertake the special audits.

**Table 17: Breakdown of special audits of LSIs by areas of emphasis\***

As at 31 December 2018

	2018	2017
Impairment-related special audits	9	15
Section 25a (1) of the Banking Act (MaRisk)	130	166
Cover	7	13
Market risk models	0	0
IRBA (credit risk measurement)	7	5
AMA (operational risk measurement)	0	0
Liquidity risk measurement	0	0
<b>Total</b>	<b>153</b>	<b>199</b>

\* This table relates to LSIs under the supervision of the Banking Supervision Sector. IRBA stands for internal ratings-based approach, AMA stands for advanced measurement approach, and OpRisk stands for operational risk.

### Highest audit ratio for other institutions

The majority of the special audits in 2018 related to the cooperative sector, which also accounts for the largest number of institutions. However, the other institutions showed the highest audit ratio (see Table 18 “Breakdown of special audits of LSIs in 2018 by groups of institutions”).

Table 19 (page 78) shows the breakdown of special audits of LSIs initiated by BaFin in 2018 by risk class. The special audits are risk-based with the result that the percentage of institutions audited tends to rise for those with a higher impact or lower quality. BaFin also ordered seven special audits which had been requested.

**Table 18: Breakdown of special audits of LSIs in 2018 by groups of institutions**

As at 31 December 2018

	Commercial banks	Savings bank sector	Cooperative sector	Other institutions
Impairment-related special audits	1	0	8	0
Section 25a (1) of the Banking Act (MaRisk)	19	34	69	8
Cover	0	6	0	1
Market risk models	0	0	0	0
IRBA (credit risk measurement)	3	2	0	2
AMA (operational risk measurement)	0	0	0	0
Liquidity risk measurement	0	0	0	0
<b>Total</b>	<b>23</b>	<b>42</b>	<b>77</b>	<b>11</b>
<b>Audit ratio in %*</b>	<b>18.9</b>	<b>11.0</b>	<b>8.8</b>	<b>37.9</b>

\* Number of audits as a proportion of the number of institutions in each group of institutions. This relates to LSIs supervised by BaFin’s Banking Supervision Sector.

#### Definition

### Special audits

With respect to banking supervisory special audits, BaFin distinguishes between three types: requested audits, ad-hoc audits and scheduled audits. In the first case, BaFin only conducts the audit at an institution’s request; in the second case, the audit is based solely on Banking Supervision’s need to adequately clarify an issue. The third case comprises audits performed by BaFin such as those in accordance with a statutory audit schedule. This applies, for example, to cover audits in the *Pfandbrief* segment, which must be

performed at regular two-year intervals under the German *Pfandbrief* Act (*Pfandbriefgesetz*).

Requested audits consist in particular of audits for the approval of the institutions’ internal risk measurement procedures. Ad-hoc audits are conducted for a specific reason, such as to follow up comments in the auditor’s report. These audits enable BaFin to obtain its own in-depth insight into an institution’s risk situation.

**Table 19: Breakdown of special audits of LSIs initiated by BaFin in 2018 by risk class**

As at 31 December 2018

Special audits initiated by BaFin		Quality of the institution				Total	Institutions* in %
		1	2	3	4		
Risk matrix	Impact						
	High	0	1	1	0	2	25.0
	Medium	7	13	10	0	30	14.5
	Medium-low	19	54	11	1	85	10.9
	Low	1	12	7	2	22	5.4
	<b>Total</b>	<b>27</b>	<b>80</b>	<b>29</b>	<b>3</b>	<b>139</b>	<b>9.9</b>
	<b>Institutions in %*</b>	<b>8.5</b>	<b>9.1</b>	<b>15.4</b>	<b>17.6</b>	<b>9.9</b>	

\* Percentage of the total number of institutions in the respective quality/impact category accounted for by the audits.

## 2.2.5 Objections, measures and sanctions

The Banking Supervision Sector recorded a total of 684 objections, measures and sanctions in 2018 (see Table 20 "Supervisory law objections and measures under the Banking Act in 2018" on page 79). The contrast with the previous year's 974 objections and measures is largely attributable to the SREP notices, since BaFin introduced the SREP cycle in 2017. Compared with 2016 (415 objections and measures), the number has therefore increased significantly in recent years.

### Discussions and letters as a supervisory instrument

Banking Supervision contacts the institutions concerned at the first indications of deficiencies. BaFin does not initiate formal measures immediately in the case of lesser deficiencies. Instead, it firstly uses regular discussions with representatives of the banks and letters as an instrument of preventive supervision. This enables it to inform the institutions, for example, of its assessment of the findings for the audit of the annual financial statements or its evaluation of the results of a special audit. The banks therefore quickly become aware of minor deficiencies and are able to rectify them before they develop into serious deficiencies and potentially trigger formal measures.

These preventive supervisory measures were successful in most cases: BaFin had to take formal measures against an institution's managers or members of its supervisory or administrative boards only in very isolated cases in 2018, as Table 20 (page 79) shows.

## 2.2.6 Situation of the institutions

### 2.2.6.1 Situation of the private, regional and specialist banks

The private, regional and specialist banks group of institutions features a wide range and variety of business models. A clear specialisation in particular financial services again provided some of the institutions with more than adequate margins in 2018, especially if they enjoyed competitive advantages as a result. This is increasingly the case for institutions able to benefit from new technologies or cooperative arrangements with fintech companies.

#### Institutions under pressure

Other institutions within this group, on the other hand, are coming under ever greater pressure to develop new areas of business. The reasons are the persistent low interest rate environment and the fact that their business models are not sustainable. During the year under review, a number of institutions – many of them with strong regional ties – expanded their range of services beyond traditional banking activities in search of sources of income that are not dependent on interest rates. This led them to engage, for example, in the cross-border purchasing of receivables or to specialise in individual loan portfolios (supply chain finance, bridge financing of transfer payments for football clubs, etc.). The associated concentration and cluster risks are creating additional corporate governance and risk management requirements for these generally smaller institutions.

**Table 20: Supervisory law objections and measures under the Banking Act in 2018\***

As at 31 December 2018

Type of measure	Group of institutions				Total
	Commercial banks	Savings bank sector	Cooperative sector	Other institutions	
Substantial objections/letters	11	8	17	4	40
Measures against managers	Dismissal requests***				
	1	2	0	0	3
Measures against members of supervisory/administrative boards	Dismissal requests***				
	0	0	0	0	0
	Cautions				
	0	0	0	0	0
Measures related to own funds/liquidity, exceeding the large exposure limit (sections 10, 13 and 45 of the Banking Act)	66	161	381	25	633
Measures in accordance with section 25a of the Banking Act	4	1	0	0	5
Measures in accordance with sections 45, 45b and 46 of the Banking Act**	3	0	0	0	3
<b>Total</b>	<b>85</b>	<b>172</b>	<b>398</b>	<b>29</b>	<b>684</b>

\* These figures relate to less significant institutions (LSIs) only.

\*\* Measures to improve own funds and liquidity (section 45 of the Banking Act), in the case of organisational deficiencies (section 45b of the Banking Act) and in the case of specific danger (section 46 of the Banking Act).

\*\*\* These figures comprise formal and informal measures and dismissal requests from third parties.

**Outsourcing and cooperation arrangements**

Some institutions are aiming to improve their results of operations by making greater use of innovative platforms. This enables particularly small institutions to reduce costs or to establish a wider market presence. However, the breakup of traditional operating procedures due to outsourcing and cooperation arrangements means that the business processes

become more complex, which requires more detailed preparation and monitoring. The institutions therefore need above all to identify business risks and to define the areas of responsibility of the outsourcing or cooperation partners, also in order to protect customers. They must further ensure that outsourcing or corporation partners do not take over activities requiring authorisation without the relevant authorisation having been granted.

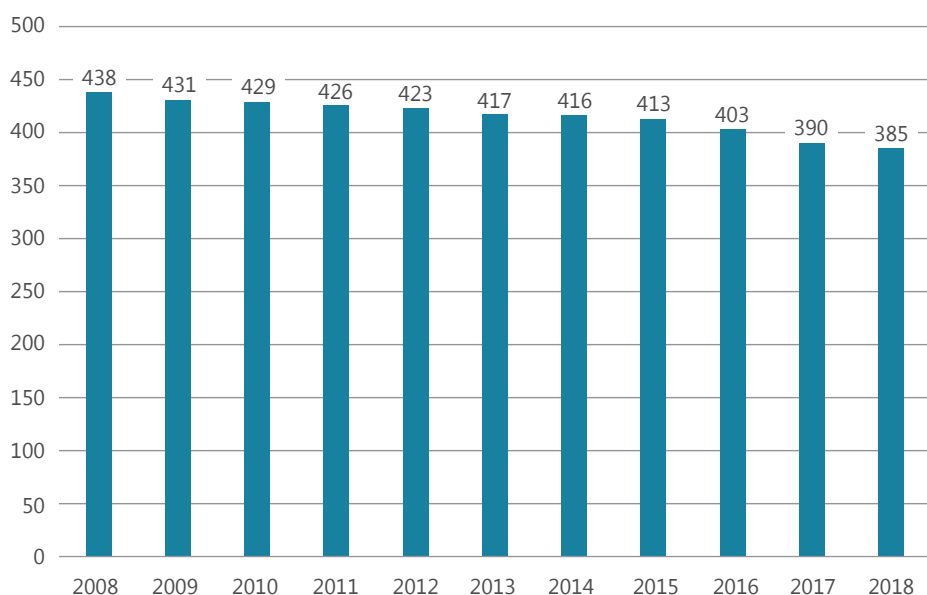
## Definition

**Cum/ex and cum/cum transactions**

Cum/ex transactions used short sales around the dividend record date to create a situation in which, from a legal perspective, a share appeared to have more than one owner for a short period of time. The principal objective of transactions constructed in this way was to enable investment income tax to be reimbursed or credited multiple times, even though the tax had only been paid once. Following a change in the law in 2012, transactions of this kind are no longer possible in Germany.

Cum/cum transactions involved the transfer of domestic shares immediately prior to the dividend record date to a tax resident entitled to a tax credit for investment income tax for the purpose of avoiding the tax being definitively charged (in particular in the case of tax non-residents). If there is no reasonable economic justification for the transaction and overall the case has the features of a tax-motivated structure (tax arbitrage), it can be assumed that the structure is abusive.

**Figure 1: Number of savings banks\***



\* This statistic does not include seven *Landesbanks* and DekaBank.

### **Cum/ex and cum/cum transactions**

A number of institutions in this group were again affected in 2018 by the review of cum/ex and cum/cum transactions (see info box on page 79) by the tax prosecution authorities, following the Federal Ministry of Finance's letter dated 17 July 2017, which has not yet been completed. One institution that was itself suspected of tax evasion was forced to close in 2018 and is undergoing insolvency proceedings at the time of going to press<sup>30</sup>.

### **2.2.6.2 Situation of the savings banks**

The German savings banks again achieved a satisfactory overall result during the past financial year. They achieved significant increases in new lending to corporate and self-employed clients. Private residential building and the consumer credit business also recorded further growth with the result that the loan portfolios reached new record figures. However, net interest income declined year-on-year despite the strength of the lending business due to the persisting low interest rate environment. In contrast, the savings banks achieved an increase in income from commissions, whose share of the operating result has been steadily climbing for years.

Impairment charges required in the lending and securities business rose only marginally and continued

at a very low level as before. The operating result after valuation fell as expected due to lower interest income. Nevertheless, the savings banks were once again able to strengthen their reserves and maintain a stable net profit for 2018 compared with the prior year. All of the savings banks complied with the statutorily prescribed capital requirements; the average total capital ratio was again well above the minimum value required by the supervisory authorities.

Many savings banks adjusted their terms and conditions and increased fees to counteract the decline in net interest income. Negative or penalty interest, i.e. fees charged for holding deposits, remained the exception in retail banking, however. The savings banks generally charged deposit fees for corporate clients and local authorities only for larger deposits.

### **Branch closures**

In view of the high cost of their dense branch networks, the savings banks continued to reduce the number of their branch offices during the financial year. According to the German Savings Banks Association (*Deutscher Sparkassen- und Giroverband – DSGV*), however, the affiliated institutions will maintain a nationwide presence in accordance with their public obligation to provide all sections of the population with banking services – even if customer visits to the branches are becoming less and less frequent due to the ongoing digitalisation of the banking business. The development from 2008 to 2018 can be seen from Figure 1 "Number of savings banks".

<sup>30</sup> See 2016 Annual Report, page 24.



## Digitalisation

In order to meet the challenges of digitalisation, the Savings Banks Finance Group pushed further ahead with the implementation of its digital strategy in 2018, including the “Kwitt” smartphone application. For example, the savings banks were the first group of institutions to create across-the-board access to real-time transfers and to mobile payment using a smartphone. The introduction of multi-bank capability now also allows savings bank customers to manage their accounts with other credit institutions using online banking. The cooperative banks joined the savings banks’ system for mobile-to-mobile transfers in 2018. As a result, around 80% of bank customers in Germany can now use “Kwitt” on their smartphones.<sup>31</sup>

### 2.2.6.3 Situation of the *Bausparkassen*

The persisting low interest rate environment was once again the main factor affecting the situation of the *Bausparkassen* in 2018. The institutions therefore continued their attempts to reduce the impact on their earnings of older *Bauspar* contracts paying interest that is no longer in line with market rates. They achieved this, for example, by terminating over-saved contracts that have been eligible for allocation for more than 10 years. A building savings contract is over-saved if payments by the customer have already reached the agreed target contract sum and a *Bauspar* loan can therefore no longer be paid out.

High-interest *Bauspar* deposits nevertheless affected the institutions’ results of operations as in the past: *Bauspar* customers continued to save into the older contracts still available, but in view of the low interest rate environment were not interested in taking out a *Bauspar* loan on the basis of those contracts at above-market rates. The proportion of *Bauspar* loans disbursed in 2018 was therefore once again very low. In contrast, the number of building loans granted increased, in particular pre-financing and bridging finance loans.

#### Further relief measures

At the same time, the *Bausparkassen* continued working to reduce their personnel and non-personnel costs and to improve their (IT) processes. They were also developing new generations of *Bauspar* contract models with lower rates of interest for both the *Bauspar* deposits and the loans. These measures are intended firstly to improve earnings over the medium and long

term, and secondly to generate a perceptible increase in the proportion of new *Bauspar* loans in the future.

### 2.2.6.4 Situation of the cooperative banks

The cooperative banks’ performance was satisfactory in the 2018 financial year despite the continuing difficult market environment. The net profit for the year after taxes was maintained at a stable level compared with the prior year. The renewed moderate decline in earnings is attributable – as for other groups of institutions – to the persisting low interest rate environment. Net interest income declined once again compared with the previous year and is now noticeably below the long-term average. The continuing successful efforts by the primary institutions to manage costs only partially compensated for the lower net interest income. However, the cooperative banks benefited from the fact that the interest expense has fallen further and has now reached an all-time low. Measurement gains and losses were virtually unchanged from the prior year. The measurement losses remained below average in relation to the long-term comparative figure (since 2002). However, adequate risk provisioning in the form of reserves continues to be possible at an appropriate level.

#### Mergers

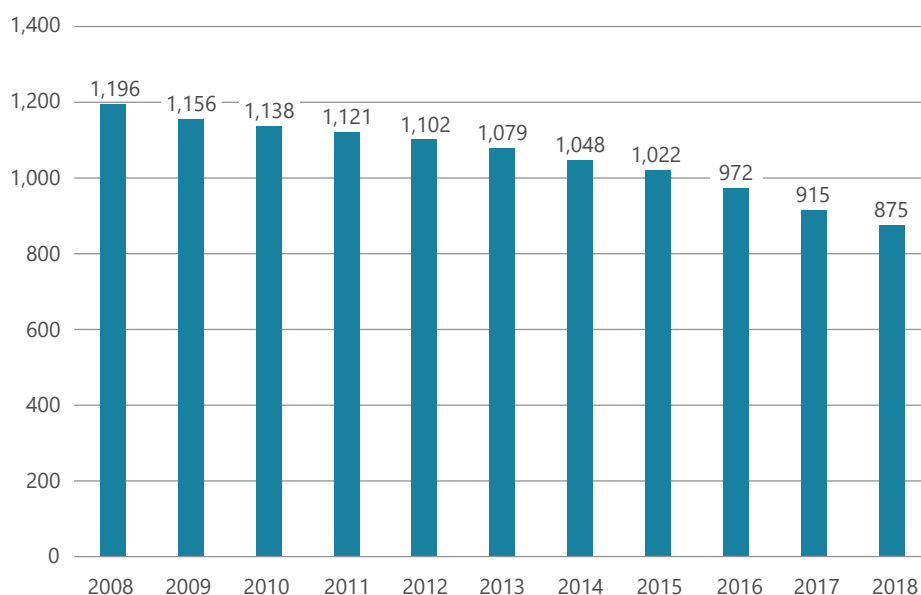
As in previous years, a large number of mergers of primary cooperative institutions took place in 2018. The number of cooperative societies therefore declined by 4.3% from 915 (prior year) to 875 institutions in 2018. This therefore represents a continuation of the trend in the Cooperative Financial Network, as shown by Figure 2 “Number of primary cooperative institutions” on page 82. There had already been mergers between the leading cooperative institutions DZ Bank and WGZ Bank (2016) and the two largest computer centres in the cooperative sector, Fiducia IT and GAD (2015). Subsequently, the two auditing associations Rhineland-Palatinate cooperative association (*Rheinisch-Westfälischer Genossenschaftsverband*) and the Cooperative Association (*Genossenschaftsverband*) combined to form the largest cooperative auditing association in Germany (2017).

#### Digitalisation and negative interest

The Cooperative Financial Network is pushing ahead with its new digitalisation initiative in response to the challenges of the digital transformation. The expansion of digital banking is intended to support the primary institutions on the ground: The aim of the initiative is to interlink branches, service centres and online banking in such a way that in future customers will be able to

<sup>31</sup> On this subject, see also Schmalzl, The status of digitalisation at savings banks, in: BaFinPerspectives, edition 1/2019, page 68 ff.

**Figure 2: Number of primary cooperative institutions**



conduct their banking business at any time on a flexible basis and, wherever possible, in real time. For example, the cooperative banks have already joined the “Kwitt” cashless payment system of the Savings Banks Finance Group in 2018, as mentioned above.

In 2018, BaFin audited the IT system of one service provider in the cooperative sector. The Supervisory Authority will continue to keep a close eye on this issue in 2019, given its great significance for the network.<sup>32</sup>

Negative interest for retail customers continues to be a topic of discussion in the cooperative sector. At the present time, this is normally only charged for very large deposits. The institutions are making greater efforts to use commission income to compensate for the decline in interest income. Free current accounts are now rarely available in the cooperative sector.

#### 2.2.6.5 Situation of the foreign banks

Foreign banks played a major role in the German financial market in 2018 as in previous years. The foreign banks located in Germany are concentrated on the deposit business and also mainly on the lending business, private banking, investment banking, custodian bank operations as well as export finance and payment services. The activities of Iranian banks continue to be legally permitted on the basis of the continuing sanctions exemptions granted by the EU,

despite the reimposition of US sanctions in full on 5 November 2018. BaFin authorised the branch of an Iranian bank in 2018; a further authorisation procedure has not yet been concluded.

Most of the foreign banking entities domiciled in Germany continued to qualify as less significant institutions in the year under review. However, the structure of the foreign banking segment is expected to change in connection with Brexit.<sup>33</sup>

#### Consequences of Brexit

A number of foreign banks are relocating parts of their business operations from the United Kingdom to Germany in view of the proposed exit of the UK from the European Union<sup>34</sup>. This is expected to increase the volume of business of the institutions already located here. Some banks are planning such a large expansion of their business in Germany that they will already exceed the thresholds for significant institutions within the meaning of the SSM Regulation shortly after Brexit. BaFin is currently processing numerous authorisation, qualifying holding and EU passporting procedures together with the ECB. In 2018, 14 authorisation procedures were already concluded for foreign banks relating to CRR credit institutions, branches, branch offices and securities trading banks. The importance of foreign banks for the German financial marketplace can be expected to increase along with changes in the

<sup>32</sup> On IT supervision, see also chapter II 6.4.

<sup>33</sup> On this topic, see the following section “Consequences of Brexit”.

<sup>34</sup> For details of Brexit, see also chapters I and II 1.

demands on supervisors. BaFin has already responded to the challenge and implemented organisational adjustments.

### 2.2.6.6 Situation of the finance leasing and factoring institutions

The number of (pure) finance leasing institutions subject to ongoing supervision by BaFin fell to 311 in 2018 (previous year: 322 institutions), while the number of (pure) factoring institutions declined to 158 (previous year: 163 institutions). In addition, 28 institutions provided both finance leasing and factoring services; these services were offered by 28 banks in the previous year.

#### Authorisations

BaFin approved 17 new applications for authorisation pursuant to section 32 of the Banking Act. A total of 24 authorisations terminated in 2018, mainly as a result of waivers, in some cases also due to mergers.

BaFin initiated 186 qualifying holding procedures. In these procedures, BaFin investigates the integrity and the objectives of the potential purchaser of a qualifying holding, among other things. It must also check the existence and origin of the funds used to make the purchase. BaFin received a total of 109 notifications of the intention to appoint new members of management or commercial attorneys-in-fact; it was also notified that the appointments of 62 members of supervisory or advisory boards had been completed. In each of these cases, the Supervisory Authority reviews whether the persons in question are reliable and suitable for these responsibilities.

#### Measures and sanctions<sup>35</sup>

During the year under review, BaFin sent letters dealing with serious matters to three finance leasing and factoring institutions and initiated five administrative fine proceedings. In two cases, institutions waived their authorisation to provide financial services during the course of administrative proceedings. Furthermore, in one case BaFin filed a criminal complaint against a former manager of an institution. In BaFin's opinion, there are initial grounds for suspecting a breach of section 15 (1) sentence 1 of the German Insolvency Code (delay in filing for insolvency).<sup>36</sup>

<sup>35</sup> The measures and sanctions described here relate only to institutions engaged in finance leasing and factoring. They are not included in the tables presented earlier.

<sup>36</sup> For a comprehensive overview of measures and sanctions across the different sectors, see chapter II 4.

### 2.2.6.7 Situation of the payment institutions and e-money institutions

In 2018, BaFin granted authorisation in accordance with the new German Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz – ZAG*) to 36 payment institutions and 6 e-money institutions that had already been subject to ongoing supervision by BaFin as at 12 January 2018. The new law largely entered into force on 13 January 2018. These institutions were permitted to continue providing payment services without having authorisation under the requirements of the amended ZAG until 13 July 2018 at the latest. After that date, the transitional provisions no longer applied.

The new version of the ZAG had other implications for the existing institutions under the ZAG and the ongoing supervision of these undertakings, in addition to the transitional provisions. The new law intensifies the focus on the technical and IT aspects of payment services.

The amended ZAG and the payment services which now require authorisation – namely payment initiation services and account information services – also generated further enquiries from innovative companies and general enquiries on the national implementation of PSD2 (see info box "Payment initiation service" and "Account information service" on page 84).

For example, companies that were already providing these new payment services at 13 January 2018 and wanted to continue doing so beyond that date, had to apply for corresponding authorisation or registration by 13 April 2018 to be able to take advantage of the transitional provisions in the ZAG.

In 2018, BaFin received a total of 44 new applications for authorisation to provide payment services or to engage in e-money business, or for registration as an account information service provider. 14 of those applications related to authorisation to provide the new payment services, i.e. the payment initiation service and the account information service. 16 applications were submitted for registration as account information service providers.

Three payment institutions were granted new authorisations in 2018. They included one provider of the new payment services, i.e. the payment initiation service and the account information service. BaFin issued one further new authorisation for an e-money institution.

## Definition

### Payment initiation service

In a payment initiation service, a payment order is initiated for the user at their credit institution in order to trigger “the transfer of money from one payment account to another payment account”<sup>37</sup>. The service provider has access to the payer’s payment accounts for this purpose, using the payer’s personal account access information. According to the definition in section 1 (33) of the ZAG, a payment initiation service is a service which initiates a payment order at the request of the user with respect to a payment account held at another payment service provider.

### Account information service

An account information service is an online service providing consolidated information about one or more of the customer’s payment accounts held with one or more other payment service providers. The account information service provider also has access to the customer’s payment accounts. The service provides the user with an overall view of their payment accounts and, for example, of past transactions. Section 1 (34) of the ZAG covers services irrespective of the party to whom the information is addressed. A link to a specific payment transaction is not necessary.

In total, 7 e-money institutions and 39 payment institutions were subject to ongoing supervision by BaFin in 2018.

<sup>37</sup> Bundestag printed paper 18/11495, page 107.

## 2.2.6.8 Pfandbrief business

The German *Pfandbrief* again performed relatively well in 2018, despite the difficult market environment and the continuing low level of interest rates. Total sales of *Pfandbriefe* increased slightly with the result that *Pfandbriefe* with a total volume of €50.4 billion were sold in 2018 (see Table 21 “Gross *Pfandbrief* sales”). In 2017, the volume had amounted to €48.8 billion.

Measured by the issue volume of €43.2 billion, sales of mortgage *Pfandbriefe*, including ship and aircraft *Pfandbriefe* although these are niche products, were more than six times higher than those of public-sector *Pfandbriefe*. Issues of the latter amounted to only €7.2 billion in 2018. In 2017, the figure was €11.9 billion.

### Total volume of outstanding *Pfandbriefe*

The total volume of outstanding *Pfandbriefe* in 2018 amounted to €364.6 billion (see Table 22 on page 85). The outstanding volume of mortgage *Pfandbriefe* (including ship and aircraft *Pfandbriefe*) rose to €230.5 billion in 2018, while the volume of public-sector *Pfandbriefe* outstanding declined further to €134.1 billion.

### Lower ECB investments

The upward trend in mortgage *Pfandbriefe*, which are benefiting as before from a high level of sales in the real estate market, is likely to continue. In contrast, the performance of the public-sector *Pfandbriefe*, which are mainly still used for funding traditional local government financing requirements and state-backed export finance, continues to decline.

The ECB – as the largest investor in the covered bond market in recent years – gradually reduced its monthly purchase volumes during 2018. From 2019, the ECB will only reinvest the cash reflows from the various bond purchase programmes. At the same time, the ECB is endeavouring initially to maintain the level at the end of

**Table 21: Gross *Pfandbrief* sales**

Year	Mortgage <i>Pfandbriefe</i> (€ billion)	Public-sector <i>Pfandbriefe</i> (€ billion)	Total sales (€ billion)
2014	30.6	15.3	45.9
2015	42.6	15.5	58.1
2016	35.1	10.4	45.5
2017	36.8	11.9	48.8
2018	43.2	7.2	50.4

**Table 22: Total volume of outstanding Pfandbriefe**

Year	Mortgage Pfandbriefe (€ billion)*	Public-sector Pfandbriefe (€ billion)	Total outstanding (€ billion)
2014	195.8	206.5	402.3
2015	203.9	180.5	384.4
2016	203.7	155.2	358.9
2017	214.0	148.2	362.2
2018	230.5	134.1	364.6

\* Including ship and aircraft Pfandbriefe.

2018. Over the next 10 years, the ECB will increasingly withdraw from the covered bond market, meaning that marketing to traditional investors will again grow in importance for issuers in the longer term. The sector has so far been increasingly successful in attracting the attention of new groups of investors with the issues of sustainability and energy efficiency in the form of the "green Pfandbrief"<sup>38</sup>.

### 2.3 Financial services institutions

At the end of 2018, BaFin's Securities Supervision/Asset Management Sector had 722 financial services institutions under its supervision (previous year: 722). It was also responsible for supervising 110 German branches of foreign undertakings; the figure for the prior year was 106 branches.

47 undertakings applied for authorisation to provide financial services in 2018 (previous year: 45). Eight financial services institutions applied to extend their authorisation to cover the provision of additional financial services. In 2017, 12 institutions had made such a request.

The number of tied agents at the end of 2018 amounted to 23,300 agents and therefore fell significantly (previous year: 34,900 agents). The sharp decline in the number of tied agents is mainly attributable to the fact that a larger liability umbrella has resulted in changes to the distribution structure. The number of liable undertakings amounted to 183 (prior year: 179 undertakings).

#### Brexit

Approximately one-third of the applications for authorisation came from undertakings wanting to commence operations as financial services institutions

in Germany in connection with Brexit.<sup>39</sup> They mainly comprise subsidiaries of foreign undertakings which have already been established and have their registered office in Frankfurt am Main. Many of the applicants belong to larger groups, with the result that a large part of the application processing relates to the qualifying holding procedure. As with the securities trading banks, issues such as process and structural organisation as well as outsourcing management also play a major role in these applications. Moreover, it is also often a question of the staffing requirements, in particular the amount of time for which the members of the management body are present and available on site.

#### Purchase and sale of qualifying holdings

BaFin received a higher number of notifications in 2018 compared with earlier years relating to the acquisition or sale of a qualifying holding in a financial services institution. The owners of institutions may be replaced or change for a wide variety of reasons: Institutions may be merged, a new owner may result from a succession arrangement or, for institutions forming part of a group, there may be changes to the group structure.

In the course of 2018, BaFin participated in 28 audits at financial services institutions and conducted a total of 82 supervisory interviews with the latter. For comparison: BaFin participated in 39 audits and conducted 97 supervisory interviews in 2017. 26 authorisations held by financial services institutions ended in 2018, in most cases because they were returned. In the prior year, 29 authorisations ended.

### 2.4 Securities trading banks

The Securities Supervision/Asset Management Sector is also responsible for supervising the solvency and conduct of securities trading banks, as the business

<sup>38</sup> <https://www.green-pfandbrief.com/home>.

<sup>39</sup> On Brexit see chapter I and chapter II 1.

models of these institutions differ from those of the credit institutions.

Securities trading banks are primarily engaged in securities trading and are classified as investment firms. Their spectrum of services ranges from various forms of own account trading, such as market-making on the stock exchanges, to assisting with issuers' capital raising activities. The product range comprises many types of financial instruments. In addition to equities and bonds, they also include cleared and uncleared derivatives, for example credit default swaps (CDSs), energy derivatives and contracts for difference (CFDs).

### **Fierce competition**

The securities trading banks operating in Germany were once again faced with fierce competition between each other and with other credit institutions with securities trading activities with respect to business with institutional customers. In addition, the modalities of CFD trading with retail investors have changed in the wake of the restrictions imposed on sales of CFDs by the European Securities and Markets Authority (ESMA)<sup>40</sup>. BaFin therefore asked a number of securities trading banks to review their financial projections and to diversify their business models.

With the implementation of the Markets in Financial Instruments Directive II (MiFID II), new requirements have applied to securities trading banks since the start of

2018, for example relating to systematic internalisation, cost transparency and product governance.

In the case of one institution, BaFin arranged a hearing on the proposed revocation of its authorisation because the risk-bearing capacity of its business model was inadequate. The institution then returned its authorisation.

### **Brexit**

The supervision of securities trading banks also continued to be dominated by Brexit in 2018. During the year under review, BaFin processed a total of 12 authorisation procedures for securities trading banks which have conducted their European business in the past primarily from London. The planned relocation of business activities is an enormous challenge for the banks themselves, as it is for the supervisory authorities. The authorisation procedures are highly complex and require an intensive exchange of information on topics such as risk management, process and structural organisation and outsourcing.

At the same time, BaFin participated in ESMA's Supervisory Coordination Network (SCN). In this network, the European supervisory authorities involved in authorisation procedures in connection with Brexit exchange information. This is intended to ensure supervisory convergence. The work of the SCN makes an important contribution to the development of uniform standards for the authorisation of securities trading banks which wish to relocate their broker-dealer activities to one of the remaining 27 EU countries in the wake of Brexit.

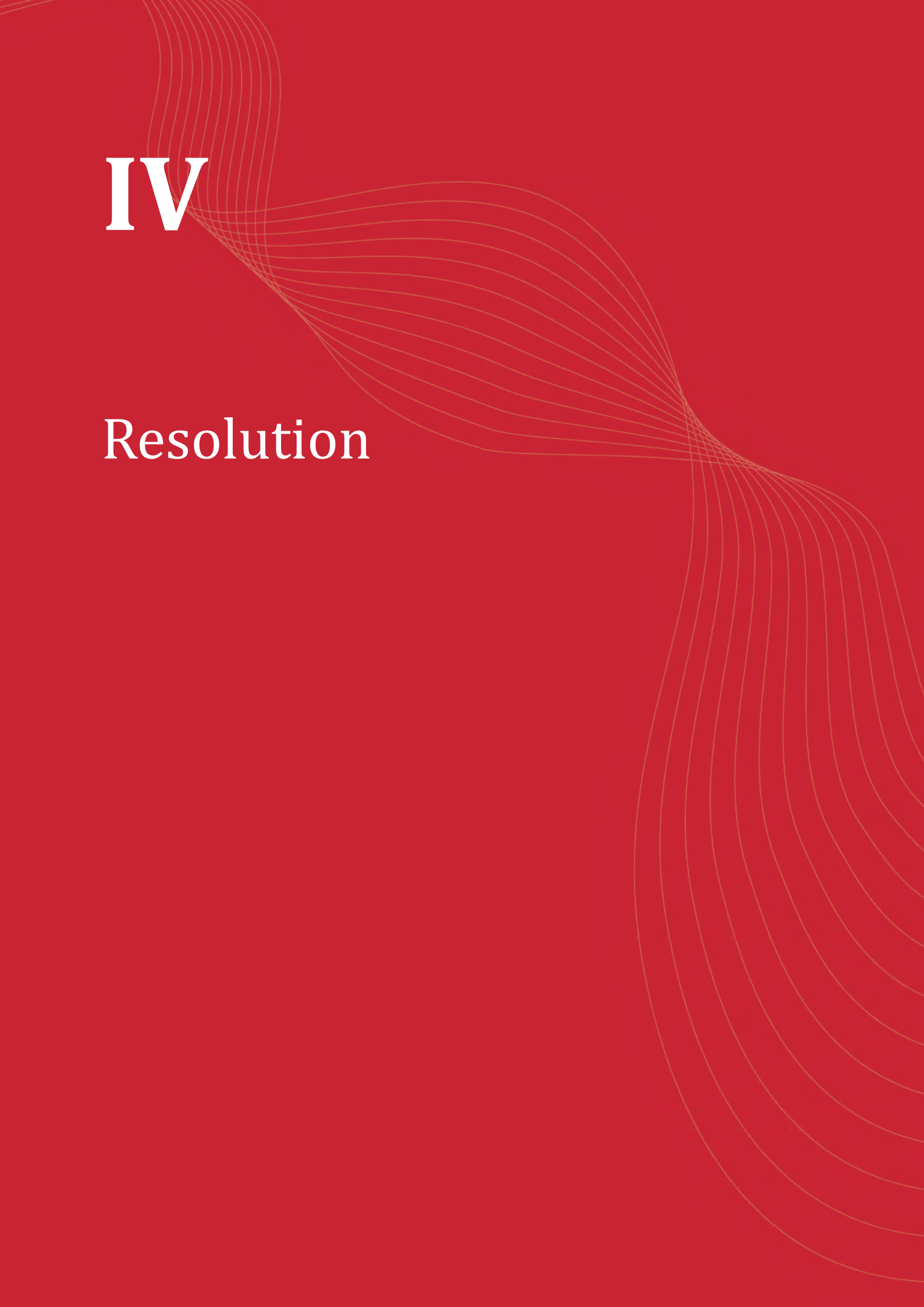
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<sup>40</sup> See ESMA press release dated 27 March 2018 and BaFinJournal April 2018, page 7 (only available in German).



# IV

## Resolution







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# 1 Bases of resolution

## 1.1 Recovery and Resolution Act and SRM Regulation

**T**he global financial crisis of 2007/2008 showed that neither current insolvency laws nor the existing regulations governing recoveries provided an adequate range of instruments for taking action to deal appropriately with a systemically important institution that is failing or likely to fail. It also became clear that there was a mismatch between liability and risk if in the end the taxpayer was liable for rescuing banks.

### Resolution regime established

On behalf of the Heads of State and Government of the G20, the Financial Stability Board (FSB) then developed its key attributes of effective resolution regimes for credit institutions and investment firms. Based on this, a standard framework governing the recovery and resolution of institutions for all EU member states was established at European level in the form of Directive 2014/59/EU for the recovery and resolution of credit institutions and investment firms (Bank Recovery and Resolution Directive – BRRD), which came into force on 2 July 2014.

The Directive was implemented in Germany with the entry into force of the German Recovery and Resolution

Act (*Sanierungs- und Abwicklungsgesetz – SAG*)<sup>1</sup> on 1 January 2015. However, some of the principal provisions of the BRRD had already been introduced into German legislation in 2013 with the German Ringfencing Act (*Abschirmungsgesetz*)<sup>2</sup>. These related mainly to the requirements for recovery planning, resolution planning and the resolvability assessment, and to the power to remove impediments to resolution.

### Key attributes of the resolution regime

The key attributes of the resolution regime now in force include new types of tools for intervention under administrative law and powers enabling an institution to be resolved in an orderly manner in a crisis. These powers include in particular the bail-in of shareholders and creditors<sup>3</sup>, sale of the business, transfer to a bridge institution and transfer to an asset management company. The new regulatory framework also includes detailed provisions for crisis prevention: Firstly, the institutions are required to prepare recovery plans in

<sup>1</sup> German Recovery and Resolution Act of 10 December 2014 (Federal Law Gazette I p. 2091), last amended by Article 3 of the Act of 23 December 2016 (Federal Law Gazette I page 3171).

<sup>2</sup> Federal Law Gazette I 2013, page 3090.

<sup>3</sup> BaFin's brochure dealing with banks or insurers in difficulties informs retail clients when and to what extent they would share in the losses of a bank in the event of a resolution, and to what extent they are protected in those circumstances. The brochure is available at [www.bafin.de/dok/11595794](http://www.bafin.de/dok/11595794).

advance. Secondly, the competent authorities have an obligation to draw up resolution plans which make it possible to react effectively to future difficulties.

### European resolution mechanism

For the eurozone, European legislators considered the exclusive competence of the national authorities for applying the provisions and instruments of the BRRD, which makes the decision process more difficult in cross-border situations, to be inadequate for the aims of the banking union to be realised. As the second pillar of the banking union, therefore, the Single Resolution Mechanism (SRM)<sup>4</sup> was established by means of the SRM Regulation, which came into force on 1 January 2016. This Regulation also contains provisions for the European Single Resolution Board (SRB) and for the Single Resolution Fund (SRF). The SRM comprises the SRB and the national resolution authorities (NRAs) in the eurozone.

### Integration of the national resolution authority into BaFin

BaFin has been the national resolution authority in Germany since 1 January 2018.<sup>5</sup> This function was performed by the Financial Market Stabilisation Agency (FMSA) from 2015 to 2017. Its integration as a separate sector within BaFin ensures that the resolution function will remain operationally independent from the supervisory function.

### Role of SRB and BaFin

The SRB is responsible within the SRM for its efficient and consistent functioning. Together with the competent NRA, the SRB prepares the resolution plans for the significant institutions (SIs), which are supervised by the European Central Bank (ECB) in the context of the Single Supervisory Mechanism (SSM), and for less significant financial institutions and groups of institutions with cross-border activities (cross-border LSIs). It also assesses the extent to which an institution is resolvable. At the same time, the SRB identifies impediments to resolution and appropriate measures for removing them.

This involves the SRB and the respective competent NRAs working together in internal resolution teams (IRTs) formed for each institution or group of institutions being managed. The IRTs also prepare the SRB's decisions and rulings relating to resolution planning and resolution actions, which are then implemented by the respective NRA.

For institutions classified as less significant (LSIs), including financial market infrastructures (FMIs), competence rests solely with the NRA – in Germany therefore with BaFin. The NRA draws up resolution plans for this group of institutions on its own responsibility. Similarly to the work in the internal resolution teams, it assesses whether a less significant institution can be resolved, identifies impediments to an orderly resolution and defines appropriate countermeasures.

The SRB acts as a control body to ensure that the standards and guidelines are applied consistently for these LSIs.

### Cross-border collaboration

In addition to direct (SIs/cross-border LSIs) and indirect (LSIs) collaboration with the SRB, resolution colleges (RCs) or crisis management groups (CMGs) are put together from the NRAs concerned and certain institutions as observers (see Figure 3 "Cross-border collaboration" on page 91). These RCs or CMGs are used by the various resolution authorities responsible for parts of the relevant institution for exchanging information. They are able to coordinate with each other within these bodies in order to improve the resolvability of the institution concerned.

### Single Resolution Fund

The principal purpose of the Single Resolution Fund (SRF) is to provide funds to support a resolution process. The institutions pay an annual contribution into the SRF for this. The SRB calculates the banks' contributions and manages the fund. In Germany, BaFin is responsible for collecting the contributions to the SRF.<sup>6</sup> However, the intention in principle is to avoid relying on these financial resources as far as possible.

## 1.2 European banking package

On 15 February 2019, EU ambassadors approved the agreement reached between the presidency of the Council and the Parliament on a comprehensive package of legislation aimed at reducing risks in the European banking sector. The European Parliament will vote on the package in mid-April 2019.

The banking package amends the Capital Requirements Regulation (CRR) and the Capital Requirements Directive IV (CRD IV)<sup>7</sup> as well as the BRRD and the

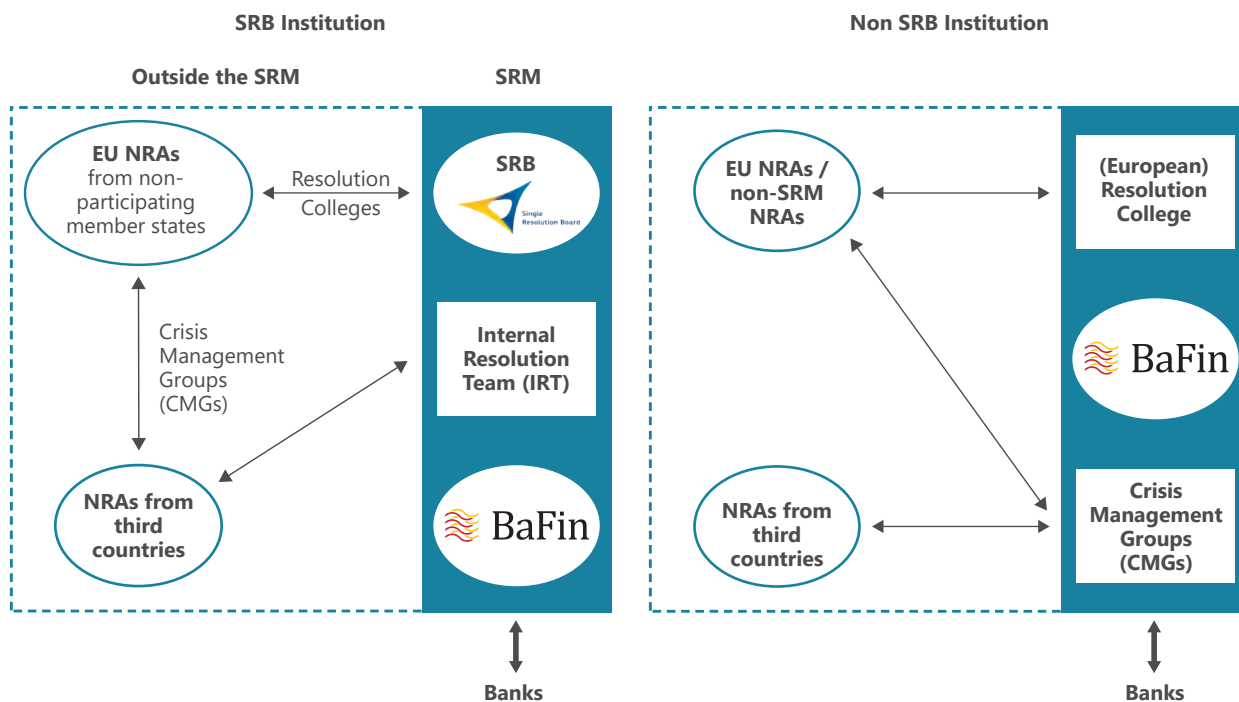
<sup>4</sup> Regulation (EU) No 806/2014.

<sup>5</sup> See 2017 Annual Report, page 164.

<sup>6</sup> See 2.6.

<sup>7</sup> On the proposed amendments to the CRR and CRD IV, see chapter III 1.2.2. and 1.3.1.

**Figure 3: Cross-border collaboration**



SRM Regulation. The following points are worthy of particular mention:

- Implementation of the regulatory framework of November 2015 agreed by the FSB, the Total Loss-absorbing Capacity (TLAC) Term Sheet<sup>8</sup>: The requirements for global systemically important institutions to maintain minimum levels of equity and other instruments that absorb losses in a resolution of the institution will be incorporated into the existing regulations on the Minimum Requirement for Own Funds and Eligible Liabilities (MREL<sup>9</sup>). In particular, the qualitative and quantitative requirements are intended to be harmonised to a large extent. Since the requirements must be met using certain unsecured debt instruments, among other things, a specific seniority has been introduced for these instruments in the insolvency ranking<sup>10</sup>. The intention is to bring the regulations into line with the liability cascade in bank resolutions in accordance with the no creditor worse off (NCWO) principle.<sup>11</sup>

- Introduction of a new moratorium (suspension of payment or delivery obligations), which occurs in advance of the resolution action and which can be used for a maximum duration of two days after the relevant institution is declared to be failing or likely to fail
- Introduction of a provision that an institution which is failing or likely to fail whose resolution is not in the public interest must be wound up in accordance with national laws
- Adoption of a provision already in force in the SAG on contractual recognition of the temporary suspension of termination rights for financial contracts subject to the laws of a third country

### 1.3 SRB guidelines and standards

The SRB issues mandatory guidelines and interpretive guidance to ensure that a consistent approach is adopted within the SRM for resolution planning for SIs as well as for institutions and groups of institutions with cross-border activities. They are developed in close cooperation with the NRAs in working groups and expert networks in which BaFin is actively involved. The guidelines and interpretative guidance are made available to the IRTs who apply them in their daily work.

For LSIs, BaFin produces its own guidelines and interpretive guidance. They are based on the SRB

8 <http://www.fsb.org/2015/11/total-loss-absorbing-capacity-tlac-principles-and-term-sheet/>.

9 See 1.3.

10 See section 46f of the Banking Act.

11 In a resolution, no shareholder, holder of relevant capital instruments or creditor shall incur greater losses than would be the case in an insolvency. See 1.4.

standards to ensure that all participants in resolution planning adopt a coordinated approach here as well.

In 2018, the SRB's work focused mainly on the further development of its guidelines for the minimum requirements for own funds and eligible liabilities (MREL policy).

The first part of the MREL policy of 2018 was published on 20 November 2018 for those institutions for which no binding requirements were stipulated in the 2017 resolution planning cycle. The SRB published the second part of its MREL policy on its web site on 16 January 2019 for more complex institutions, for which collaboration with resolution authorities outside the banking union takes place in resolution colleges.

### **Sufficient funds for loss absorption and recapitalisation**

The MREL requirements are intended to ensure that sufficient funds are available if a financial institution is failing or likely to fail and has to be resolved. This is because it is only then that the bail-in tool can be used credibly and efficiently. The bail-in of creditors represents a central means of improving resolvability. While the 2017 MREL policy provided for the MREL requirement to be set at the consolidated level, the 2018 policy was ultimately revised and expanded to include a number of central points. The priority issues addressed in the 2018 MREL policy include:

- the eligibility of liabilities issued by subsidiaries of a resolution entity
- the determination and setting of general subordination requirements and additional subordination requirements on the basis of the NCWO principle
- the setting of individual MREL requirements for subsidiaries of resolution entities<sup>12</sup>
- consideration of the planned resolution strategies when setting the MREL requirement

## **1.4 BaFin circulars and guidance notices**

### **1.4.1 Contractual recognition of temporary suspension of termination rights**

BaFin regularly publishes circulars and guidance notices on supervisory topics and on new regulations. Its aim in doing so is to assist the institutions under supervision in

implementing the relevant requirements and therefore to ensure consistent administrative practice.

On 21 December 2018, BaFin published a guidance notice with guidelines and explanations on the obligations deriving from the statutory provisions for contractual recognition of the temporary suspension of termination rights in accordance with section 60a of the SAG.<sup>13</sup>

So that, if an institution is in financial difficulties, the necessary time is available to initiate the resolution actions required, the resolution authority has the power to temporarily suspend termination rights and other contractual rights of counterparties subject to certain conditions. However, with financial contracts subject to the laws of a third country or to which a third-country place of jurisdiction applies, it could be the case that the suspension is not recognised in the relevant jurisdiction. This would then create a risk that the lack of enforceability could have a material effect on the resolvability of an institution.<sup>14</sup>

If implementation is not possible for the institutions and undertakings bound by section 60a of the SAG in certain cases, i.e. for certain financial contracts or with respect to certain counterparties, for legal or other reasons, the institutions and undertakings concerned are required to provide BaFin with more detailed information for the purpose of investigating the matter. This information consists, among other things, of the types of financial contracts in question, the number of contracts, the total nominal amount and market value of all contracts for each type of financial contract and details of why the statutory requirements were not implemented in the particular case.

### **1.4.2 Treatment of certain liabilities of CRR institutions under insolvency law**

The new provisions for the treatment of certain CRR credit institutions under insolvency law are the subject of a guidance notice issued for consultation by BaFin in February 2019. It deals with the amendment of section 46f of the German Banking Act (*Kreditwesengesetz*). The purpose of the amendment is to transpose a change in Directive 2014/59/EU made by Directive (EU) 2017/2399 of the European Parliament and of the Council of 12 December 2017 into German law.<sup>15</sup> This relates to Article 108 of Directive 2014/59/EU which

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<sup>12</sup> Institutions within a group for which the use of resolution tools is envisaged under the resolution strategy.

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<sup>13</sup> [www.bafin.de/dok/11861878](http://www.bafin.de/dok/11861878).

<sup>14</sup> See explanatory memorandum Bundestag printed paper 18/5009, page 65.

<sup>15</sup> Federal Law Gazette I 2018, page 1102.

regulates the ranking under insolvency law of certain claims resulting from unsecured debt instruments in the event of the insolvency of CRR credit institutions, whose position in the insolvency hierarchy<sup>16</sup> has now been redefined.

The amendment to the Directive in turn implements the Total Loss-absorbing Capacity (TLAC) Term Sheet published by the FSB on 9 November 2015. This was issued by the FSB in order to ensure that sufficient capacity is available for loss absorption and recapitalisation, in particular in the case of global systemically important banks, in order to maintain critical functions if the institution is failing or likely to fail. The minimum requirements for the loss-absorption and recapitalisation capacity must be satisfied with subordinated liabilities, because creditors may not be left worse off than in insolvency proceedings. The subordination is achieved by allowing a special ranking within the liability cascade to be allocated to certain unsecured debt instruments.<sup>17</sup>

In the same manner as the provisions of section 46f (5) to (7) of the Banking Act in force until 20 July 2018, the new provisions apply a lower ranking only within the class of liabilities of CRR institutions that represent insolvency claims for the creditors concerned pursuant to section 38 of the German Insolvency Code (*Insolvenzordnung*).<sup>18</sup> The previously applicable ranking of liabilities that represent subordinated insolvency claims for the respective creditors within the meaning of section 39 of the Insolvency Code remains unaffected by the amendment.

The provisions do not just affect the manner of determining the order of satisfaction in insolvency proceedings. They also come into play if a CRR institution has to be resolved, whether in accordance with the requirements of the SAG or of the SRM Regulation. If the preconditions for the resolution of an institution pursuant to Article 18 of the SRM Regulation or section 62 of the SAG are met, the resolution authority may employ the bail-in tool<sup>19</sup>, among other options. In the event of a bail-in of creditors pursuant to Article 27 of the SRM Regulation, eligible liabilities<sup>20</sup> may be written down in accordance with the amount

of the losses determined in a valuation, and converted into equity of the institution for the purposes of recapitalisation. If the resolution authority employs the bail-in tool, it must observe the liability cascade pursuant to section 97 (1) of the SAG (Article 17 of the SRM Regulation). This requires eligible liabilities to be used for the purposes of a bail-in only after the shares and other instruments classified as Common Equity Tier 1 capital, Additional Tier 1 capital and Tier 2 capital.

### 1.4.3 Draft Circular on minimum requirements for implementing a bail-in

At the start of 2019, BaFin submitted the draft of its Circular on the minimum requirements for implementing a bail-in (MaBail-in) for consultation.<sup>21</sup> The draft contains requirements for a bail-in in the case of less significant institutions (LSIs)<sup>22</sup>. The MaBail-in cover the information necessary for a precise, reliable and speedy calculation and implementation of the bail-in. They also set out the requirements for the technical and organisational resources. The nature of the information provided must be such that it can deliver an up-to-date, precise and complete picture of the institution's liabilities in a resolution. It includes specific disclosures relating to the liabilities and other information that is important for the correct calculation of own funds and for accounting purposes.

The requirements of the MaBail-in for the institutions' technical and organisational resources firstly ensure that they are able to deliver the information required on time. They also serve two further purposes: the preparation of internal impact analyses by the banks to support their own calculations and the implementation of the bail-in in practice. In order to avoid delays in implementation, this information must be able to be delivered promptly and must show a high level of standardisation. Technical and organisational resources are also necessary on the part of the banks to ensure that the bail-in is implemented in a speedy and reliable manner.

### 1.4.4 Draft Circular on reporting information for resolution planning

At the beginning of 2019, BaFin submitted a draft of its Circular on reporting information for resolution planning for consultation. In the draft, BaFin explains

<sup>16</sup> See OJ EU L 345 dated 27 December 2017, page 96.

<sup>17</sup> See Bundestag printed paper 19/2435, page 54.

<sup>18</sup> Federal Law Gazette I 2018, page 1102.

<sup>19</sup> See Article 27 of Regulation (EU) No 806/2014, OJ EU L 225/52 and section 90 of the SAG.

<sup>20</sup> See Article 27(3) of Regulation (EU) No 806/2014, OJ EU L 225/52 and section 91 (1) of the SAG.

<sup>21</sup> The MaBail-in had not yet been published at the time of going to press (31 March 2019). Publication is planned for April 2019.

<sup>22</sup> See 2.4.

the administrative practice it intends to implement in dealing with Implementing Regulation (EU) 2018/1624<sup>23</sup>. The regulation lays down the implementing technical standards that must be observed with regard to procedures. It also lists the (minimum) set of templates for the provision of information required for the purpose of drawing up resolution plans. The Circular is addressed only to undertakings or groups of undertakings falling within BaFin's competence as the national resolution authority, but not to undertakings or groups for which the SRB is responsible.

The draft envisages that BaFin will inform the undertakings and groups concerned in good time prior to the reference date which templates they must submit in all cases. In addition, BaFin reserves the right to require further information not already requested in the templates.

## 2 Practice of the national resolution authority

### 2.1 Resolution planning

Compared with other member states of the European Union (EU), the banking industry in Germany is unusually diverse: From BaFin's point of view as the NRA, at the end of 2018 it comprises a total of 1,436 credit institutions<sup>24</sup> (excluding CRR investment firms) for which a resolution plan must be prepared. 39<sup>25</sup> of those institutions fell directly within the remit of the SRB, since they were either supervised directly by the ECB or had cross-border operations in the eurozone. If one of these institutions needed to be resolved, the SRB would be responsible for the relevant decisions in collaboration with BaFin. Implementing those decisions would in turn be BaFin's responsibility. As far as the remaining 1,397 institutions domiciled in Germany are concerned, resolution planning and the application of resolution actions fall within the primary area of competence of BaFin as the national resolution authority. This group of institutions includes the less significant institutions

(LSIs) which do not have cross-border activities, as well as financial market infrastructures with banking authorisation that are classified as systemically important because of their function. The group also includes significant subsidiaries of third-country undertakings. BaFin prepares resolution plans for these institutions, the scope of which is based on the institutions' systemic importance and other qualitative criteria.

The objective of resolution planning is to achieve and safeguard the resolvability of the institution in question. The national resolution authority pursues this aim both for SIs – in collaboration with the SRB – and also on its own responsibility for LSIs. In addition to preparing and updating the resolution plans, BaFin attaches special importance to the further development of resolution planning. This relates in particular to operationalising resolution tools and improving the institutions' and authorities' preparedness for a crisis, but also to strengthening international collaboration and optimising operating processes.

#### **Specialist conference on bank resolution**

BaFin hosted a specialist conference on the topic of bank resolution for the first time on 30 October 2018. The event was mainly aimed at representatives of institutions for which BaFin has primary responsibility. Chief Executive Director Dr Thorsten Pötzsch welcomed 180 representatives of credit institutions, industry associations and other institutions in the finance sector at BaFin's Frankfurt am Main location.<sup>26</sup> The conference was also intended to raise the participants' awareness of the need to give greater prominence to resolvability in the institutions' strategic deliberations. The panel discussion – which included representatives of industry associations, the SRM and the SSM – and a variety of specialist talks dealt with current topics relating to resolution planning, resolution tools and the question of how obstacles to resolution can be identified and removed.

#### **Nature of the resolution planning process**

Resolution planning is not restricted to preparing and updating a resolution plan. One of its core functions is to assess the resolvability of the institutions (see Figure 4 "From resolution planning to resolvability" on page 95). Resolution planning therefore begins with a strategic analysis of the institution and the task of assessing the public interest in a resolution (public interest assessment – PIA). On the basis of the results, the next

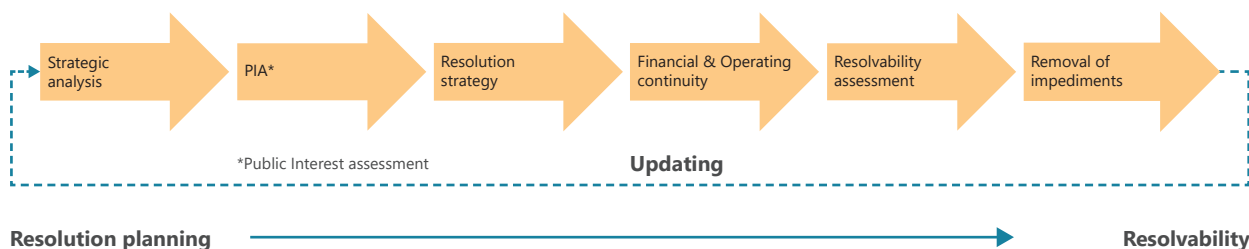
<sup>23</sup> Implementing Regulation (EU) 2018/1624, OJ EU L 277/1.

<sup>24</sup> The total number does not include branches of foreign banks or financial services providers such as housing enterprises with savings schemes, since these institutions do not fall within the area of competence of the NRA.

<sup>25</sup> The list of banks is available on the SRB's website at: <https://srb.europa.eu/en/content/banks-under-srbs-remit>.

<sup>26</sup> The SRB has established a similar exchange with the banking sector in the form of its annual "Industry Dialogue" in Brussels.

**Figure 4: From resolution planning to resolvability**



steps consist of defining individual resolution strategies and associated resolution tools, identifying possible impediments to resolvability and working towards removing them. A complete implementation of the resolution regime comprises:

- setting the institution-specific MREL
- (if necessary) ordering impediments to resolvability to be removed
- (if necessary) ordering resolution actions

The resolution plan represents a snapshot of the resolution planning. It is a standardised document, tailored to reflect the particular features of the institution, which the authorities use in the case of resolution as a template for implementing or adapting resolution strategies. Resolution planning therefore functions as a preventive method of preparing all the parties involved for possible crisis scenarios. It also improves the institutions' ability to withstand a crisis, reduces the costs of a resolution and therefore has a stabilising effect on the system.

**Resolution strategy**

The development of an appropriate individual resolution strategy is at the heart of every resolution planning exercise. In selecting resolution strategies, the resolution authority takes into account the overall objectives of the resolution and chooses the strategy<sup>27</sup> most suited to achieving those objectives. The resolution strategy is therefore based on the findings resulting from the review of the PIA. The consideration of the strategy is based on the following resolution objectives:

- Ensuring the continuity of critical functions
- Avoidance of significant negative effects on financial stability
- Protection of public funds
- Protection of depositors covered by the German Deposit Guarantee Act (*Einlagensicherungsgesetz*)

- Protection of investors covered by the German Investor Compensation Act (*Anlegerentschädigungsgesetz*)
- Protection of customers' money and assets

For the purpose of defining appropriate resolution strategies, financial, legal and operational risks after the reorganisation of the relevant institution also play an important role, in addition to considering whether the strategies can actually be implemented from an operating perspective. Other important individual aspects of resolution planning must also be taken into account, such as the reorganisation plan as a statutory requirement following a creditors' bail-in, communications with the aim of restoring the market's confidence and also liquidity planning and management in the event of a crisis.

**2018 planning cycle**

Every planning cycle is based on guidelines and defined priority areas. These are necessary firstly to ensure that the resolution plans are of high quality and can be operationalised, and secondly to implement resolution planning for institutions that is consistent and competitive. In 2018, the IRTs continued work on harmonising the contents of the resolution plans. The continuous development of the basic SRM principles on various topics has resulted in a significant increase in the quality of the resolution plans. This applies especially to the basic principles on critical functions, on the minimum requirements for own funds and eligible liabilities (MREL), on access to FLMs and on the continuity of business operations in a resolution. In this context, the prioritisation and scope of the resolution planning reflect the systemic importance of the particular institution or, where relevant, other qualitative criteria.

**Institutions for which the SRB has primary responsibility**

For 24 SRB institutions, the SRB and BaFin develop the resolution planning jointly in the respective IRTs. BaFin also collaborated on 15 foreign groups of institutions for

<sup>27</sup> See 2.4.

which the SRB was primarily responsible. A number of foreign institutions are expected to transfer from BaFin's area of responsibility to the remit of the SRB in the course of Brexit.

In the context of the iterative planning cycle, a distinction must be made between institutions with a resolution college and those without one, depending on their presence in member states that are not part of the banking union. The planning cycle for institutions without a resolution college, which began in January 2018, was broadly completed at the end of the year under review. The resolution planning process for institutions with a resolution college got underway in September 2018. The work for these institutions is scheduled to continue into the second half of 2019.

### **Institutions for which BaFin has primary responsibility**

In 2018, BaFin prepared draft resolution plans for a total of 604 less significant institutions that were not cross-border (within the meaning of the SRM Regulation). For 603 of these LSIs, ordinary insolvency proceedings are envisaged as a potential resolution strategy in view of the current risk assessment. BaFin also developed initial preferred resolution strategies for other less significant institutions.

## **2.2 MREL decisions**

The minimum requirement for own funds and eligible liabilities (MREL) represents one of the key resolution planning tools<sup>28</sup> for achieving the resolvability of banks. For SRB institutions, BaFin sets the level of the institution-specific MREL ratio in accordance with the decision of the SRB. The purpose of the MREL ratio is to ensure that institutions maintain sufficient own funds and eligible liabilities to be able to use the bail-in tool for loss absorption and recapitalisation in the event of a resolution. The MREL ratio is determined for the specific institution, based on its capital requirements and depending on the particular resolution strategy.

### **First MREL decisions for SRB banks**

A multi-stage process is necessary for the purpose of determining the MREL. In 2018, BaFin set the first binding MREL targets at consolidated level. The related processes, necessary structures and legal preparations were implemented during the course of the year. Informative MREL ratios were determined for most of the other banking groups directly within the remit of the SRB.

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<sup>28</sup> See 1.3.

BaFin maintains an active dialogue with the relevant institutions and associations. It uses BaFin workshops to work on raising the institutions' awareness that they must take responsibility for building up the MREL and improving their own resolvability.

## **2.3 Impediments to resolution**

Resolution planning also includes identifying potential impediments that could hinder the implementation of individual resolution strategies. BaFin initially asks the institution concerned to put forward suitable measures for the purpose of removing such obstacles. If the institution in question does not ensure that remedial action is taken, however, BaFin has wide-ranging powers to impose measures on the bank.

The identification and analysis of potential impediments to resolvability for significant institutions (SIs) were intensified during the 2018 planning cycle. The internal resolution teams organised workshops with the institutions on resolvability for this purpose. In so doing, the IRTs created an impetus for eliminating potential impediments to resolution. As a result of this process, institutions seized the initiative themselves and improved their resolvability on a continuing basis.

## **2.4 Operationalisation of the resolution tools**

The five resolution tools mentioned above<sup>29</sup> are contained in the SAG and the SRM Regulation. It is important to make a further distinction here. The write-down and conversion of relevant capital instruments and the bail-in of creditors are purely financial resolution tools, referred to collectively as a bail-in. In contrast, the sale of the business, transfer to a bridge institution and transfer to an asset management company represent structural resolution tools.

In view of this, what is the best way to provide support for the decision on a resolution strategy for planning purposes and in a crisis? At the start of 2018, the central question for BaFin was first of all which of these tools to employ, singly or in combination with each other, in order to achieve the resolution objectives as effectively as possible. To answer this, BaFin analysed all the conceivable combinations of the tools and ultimately developed a methodical procedure to back up the choice of an appropriate resolution strategy. The

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<sup>29</sup> See 1.1.



concept was closely based on the corresponding results of the work at SRB level. For the practical work, BaFin developed an IT tool that leads the user through the selection process and can be used for documentation purposes.

Another major topic in 2018 was the methodical development of the separation analysis. This is always necessary in cases where a partial transfer is carried out by means of a structural resolution tool. In 2019, the focus will be on the separation of portfolios. BaFin also continued its work on a procedural model, to establish the details of how the sale of business tool should be implemented in practice.

#### **Playbook for external implementation of a bail-in**

In order to drive forward the operationalisation of the bail-in, in 2018 BaFin prioritised the preparation of the institutions for implementing a bail-in. The guidelines were included in the MaBail-in Circular<sup>30</sup> and in a playbook for external implementation of a bail-in with financial market infrastructure service providers, which was published in March.

BaFin's intention with both sets of guidelines is to enhance the resolvability of the institutions in relation to the bail-in. The most important issues relate to the need for a more precise structure for the bail-in and speedier and more reliable implementation.

The playbook for external implementation of a bail-in is being developed jointly with the Deutsche Börse Group, in particular Clearstream Banking AG (Clearstream) and the Frankfurt Stock Exchange, and also with WM Datenservice. It deals with the process steps necessary for writing down and converting securities and creating new shares. In addition to describing the various participants in the procedure, the playbook sets out in detail the sequence of events for the necessary work steps and in particular the different interactions between the individual parties involved. It also explains how and in what form the institutions must provide the information necessary for an external implementation on the basis of the resolution order, so that the data can be processed in the quickest and most standardised manner possible. BaFin presented an initial version of the document together with its partners in a workshop with associations and institutions at the beginning of March 2019. It is now planned to develop the external implementation of a bail-in in successive stages.

<sup>30</sup> See 1.4.3.

## 2.5 Crisis Preparedness

BaFin did not have to implement any resolution actions as the national resolution authority in 2018. In order to ensure that it is prepared to deal with a crisis, BaFin has established the following preconditions:

1. preconditions for structural organisation ("crisis organisation")
2. preconditions for process organisation ("crisis processes") and
3. technical preconditions ("crisis infrastructure")

If it is foreseeable that an institution is failing or likely to fail for which the application of resolution measures in accordance with the statutory provisions cannot be ruled out, this triggers a higher state of preparedness for a crisis on the part of the NRA. The transition to crisis mode follows, where necessary. This results in a review of the preconditions for a resolution and, if those preconditions are met, resolution actions are then initiated.

As the NRA, BaFin has a well targeted crisis governance system and maintains a network with all relevant national and international authorities, institutions and ministries which must be contacted or involved in a crisis situation. The processes for managing a crisis have been updated in line with the new organisational structure and the system of governance.

BaFin carries out crisis practice exercises at regular intervals in order to test its own preparedness for a crisis. It then documents the results of these exercises and, where necessary, carries them over into appropriate measures to improve its organisational and technical preconditions.

## 2.6 Bank levy

In accordance with section 18a of the German Act Establishing the Federal Financial Supervisory Authority (*Finanzdienstleistungsaufsichtsgesetz*), BaFin has managed the restructuring fund (RSF) as a Federal Government fund since the start of 2018.<sup>31</sup> The responsibilities of the RSF include collecting the contributions to the bank levy for the SRF and transferring them to the latter.

The objective is to enable the SRF as part of the SRM to use the institutions' contributions to build up

<sup>31</sup> Federal Law Gazette I 2016, page 3179.

available funds within eight years equivalent to at least one percent of the covered deposits of all the credit institutions authorised in all of the participating member states. The initial period of the European fund runs until the end of 2023.

The share of the German institutions in the target volume for the bank levy amounted to around €2 billion in 2018 (prior year: around €1.7 billion). The high rate of growth of covered deposits as the determining factor for the target volume of the fund was the main reason that the target volume and the volume of contributions had to be increased year-on-year.

The bank levy was calculated using a consistent methodology by the SRB, which also administers the SRF. In the initial period, the institutions' contributions are firstly allocated to national compartments of the fund corresponding to their home countries. This ensures that institutions experiencing difficulties during the initial period are stabilised primarily using national funds. It is envisaged that the national compartments will be gradually merged by 2024 and finally dissolved.

As the competent NRA, BaFin collected the bank levy in Germany for the first time in 2018 and transferred it to the SRF at the end of June. The 1,516 CRR credit institutions and CRR investment firms forming part of a group under ECB supervision that are liable to pay contributions have paid total contributions amounting to almost €2 billion for the SRF, including pro rata contributions from 2015. The contributions collected under European regulations at that time were transferred to the SRF in 2016 and credited in stages for the assessment of the annual contributions.

The annual contributions of the 52 CRR investment firms under stand-alone supervision and of the domestic Union branches, which remain in the national fund (RSF), totalled €10 million in 2018. The RSF has a volume of around €2.3 billion and primarily comprises the annual contributions to the bank levy for the years from 2011 to 2014, which were collected on a national basis at that time. Since 2015, the contributions to the bank levy collected from the CRR investment firms under stand-alone supervision and the EU branches of third-country institutions have also been paid into the RSF.

In the year under review, €1.24 billion of the total amount of the bank levy was contributed by major commercial and regional banks, €318 million by *Landesbanks* and leading institutions within the savings bank and cooperative sector, €162 million by certain other institutions such as mortgage banks and financial services providers, €169 million by *Sparkassen* and €98 million by cooperative banks. For 769 smaller institutions, contributions are determined using lump-sum treatment. The calculation of the larger institutions' contributions includes a risk assessment based on a variety of indicators.

For the 2018 bank levy, the risk pillar "Stability and variety of sources of funding" with the liquidity coverage ratio (LCR) risk indicator was included in the calculation of the annual contributions for the first time in accordance with Commission Delegated Regulation (EU) 2015/63<sup>32</sup>. All of the statutorily prescribed risk pillars are expected to be included in the calculation of the contributions for the first time for the 2021 bank levy. The reporting data are now collected via BaFin's reporting and publishing platform, the MVP Portal.

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<sup>32</sup> Delegated Regulation (EU) 2015/63, OJ EU L 11/44.



# V

## Supervision of insurance undertakings and *Pensionsfonds*

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# 1 Bases of supervision

## 1.1 Global regulatory framework

### 1.1.1 Global capital standards

**I**n 2018, the International Association of Insurance Supervisors (IAIS) conducted the penultimate major field test aimed at trying out and finalising the global Insurance Capital Standard (ICS).<sup>1</sup> After more than five years, therefore, the ICS project is now turning into the home stretch towards ICS 2.0. The standard is intended to be implemented from 2020 in the context of a five-year monitoring period. The project is essentially well on track. This is also shown by the fact that the changes envisaged in comparison with ICS 1.0, which was adopted in the summer of 2017, can be better understood as moderate further developments.

These modifications essentially comprise discounting liabilities, testing out internal models as one of the “other methods” of achieving the targets set for ICS and the introduction of a new risk module for elements of spread risk. The positive aspects of these developments, which BaFin has also played an active part in driving ahead, include in particular their distinct European

profile. The basis is the compromise known as the Kuala Lumpur Agreement from 2017 which committed to market-adjusted valuation, a positive development from a German point of view. The review of the long-term use of internal models in the ICS also forms part of the Kuala Lumpur Agreement. BaFin continues to be very interested in integrating the internal models into the ICS and supports the review.

In parallel to the penultimate field test, the IAIS published a final comprehensive consultation document on the way to ICS 2.0. In this document, the IAIS first of all describes the principal elements of the future minimum standard. At the same time, it asks for feedback on issues that have not yet been finally concluded. The calculation of the yield curve and the determination of the risk margin, both of which have a significant impact on earnings, are particularly noteworthy here.

In addition to finalising ICS 2.0, the IAIS will also concentrate on preparations for the monitoring period in 2019. This will commence at the start of 2020 following the adoption of ICS 2.0. BaFin is assisting the smooth operation of the monitoring period for the Internationally Active Insurance Groups (IAIGs) involved from Germany.

<sup>1</sup> The final field test will take place in 2019 between May and July.

## 1.1.2 Identification of G-SIIs and ABA

At the end of 2017, the IAIS circulated an initial framework concept for an activities-based approach (ABA) for consultation. In the course of further work, the IAIS held discussions on the interaction of the ABA with the entity-based approach (EBA), also known as the G-SII approach, for global systemically important insurers (G-SIIs). On the basis of those discussions, the IAIS developed the Holistic Framework, intended to combine the two approaches with each other. BaFin had already been actively working towards such an approach<sup>2</sup> in 2015, but had still classified it as a hybrid approach at that time.

The IAIS finally presented the revised and updated concept to the public in a new consultation paper in mid-November.<sup>3</sup> The proposals are essentially based on the previously familiar sources as well as transmission channels for systemic risks. To that extent, it is less a question of a revolution and more an evolution. However, consideration of the individual undertaking is now only one aspect among several. At the same time, the IAIS – together with national supervisors – intends to keep an eye on events in the principal insurance markets in the form of a global monitoring exercise. The trends observed in the course of the analyses form the basis for discussions which – if required – aim to generate appropriate supervisory responses. The systemic risk of individual insurance groups remains an important topic in these discussions. The IAIS is therefore proposing further improvements to the existing valuation methodology.

To date, the IAIS toolbox for systemic risks has contained the G-SII policy measures. For the Holistic Framework, the IAIS is now proposing to add to the existing toolbox, which consists of the Insurance Core Principles (ICPS) and the Common Framework (ComFrame) for large internationally active insurance groups. This would result in the existing strongly micro-prudential focus being supplemented by a macro-prudential perspective. That would lead in turn to a significant increase in the group of undertakings required to address potential systemic risks. For this reason, it is particularly important to handle the principle of proportionality in an appropriate manner.

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2 See Hufeld, A Regulatory Framework for Systemic Risk in the Insurance Industry. In: Hufeld, Felix; Kojien, Ralph S.J.; Thimann, Christian: The Economics, Regulation, and Systemic Risk of Insurance Markets, Oxford University Press, October 2016.

3 <http://www.iaisweb.org/page/consultations/closed-consultations/2019/holistic-framework-for-systemic-risk-in-the-insurance-sector>.

The IAIS is planning to apply the new framework from 2020. It then intends to review how the different elements have been implemented by the end of 2022. For its part, BaFin is particularly keen to ensure that the necessary supervisory tools are firmly anchored in the respective supervisory regime and are also applied globally on a consistent basis. In BaFin's view, the framework must be fully implemented on a national basis. Otherwise it would not be possible to do without a G-SII designation – which could be temporarily suspended depending on the ultimate form of the Holistic Framework – by the Financial Stability Board (FSB).

## 1.2 Regulation in the European Union

### 1.2.1 Solvency II

#### 1.2.1.1 Solvency II Review

##### **Review of the standard formula**

In the course of the ongoing Solvency II Review, the European Commission put forward a revised version of the Delegated Regulation<sup>4</sup>. The latter contains implementing provisions relating to Solvency II. The revised version was based on technical recommendations by the European Insurance and Occupational Pensions Authority (EIOPA), to which the European Commission conformed for the most part.

The European Commission did not, however, adopt EIOPA's recommendations relating to interest rate risk. It deferred the review of interest rate risk to the general review process in 2020, the 2020 Review, instead. BaFin, on the other hand, continues to consider it urgently necessary to update interest rate risk and therefore supports EIOPA's proposal.

The revised version of the Delegated Regulation provides for the recalibration of various risk factors, in particular for the purpose of determining non-life underwriting risk. It also contains simplifications for individual risk modules such as counterparty default risk. BaFin welcomes these simplifications. Moreover, it will be possible to use lower risk factors for lower-risk unrated loans/bonds and lower-risk unlisted equities in future subject to certain conditions. Finally, the guidelines for calculating the loss-absorbing effect of deferred taxes were expanded in the Delegated Regulation. The European Commission is expected to

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4 Delegated Regulation (EU) 2015/35, OJ EU L 12/1.

submit the revised Delegated Regulation to the Council and the European Parliament in the first quarter of 2019. The latter then have the right to object for a three-month period.

### 2020 Review

In a further review, the 2020 Review, the European Commission will review selected provisions of the Solvency II framework directive. Recommendations for changes must be submitted to the Council and the European Parliament in 2020. The European Commission sent an initial request for information to EIOPA in April 2018; a wide-ranging call for advice was also addressed to EIOPA in February 2019.<sup>5</sup>

The review of the long-term guarantees (LTG) measures plays a central part in the Review. This includes a particular focus on the reduction of artificial volatility.

In addition to the LTG measures, the 2020 Review is intended to cover elements of the standard formula, risk mitigation techniques and the minimum capital requirement (MCR). The Commission is also seeking responses from EIOPA to specific questions relating to topics such as macro-prudential instruments, restructuring and resolution plans, group supervision, own funds, reporting systems and proportionality. BaFin is actively contributing to all the relevant working groups and among other things is arguing for comprehensive improvements to the principle of proportionality – in particular in relation to qualitative and quantitative reporting obligations as well. In addition, BaFin is aiming to develop the framework further in order to present products with long-term guarantees in a way which more accurately reflects the associated risks. EIOPA has to send its answer to the call for advice to the Commission by 30 June 2020.

In view of the wide range of topics covered by the Review, which was already anchored in the Omnibus II Directive<sup>6</sup>, EIOPA has performed significant preparatory work in recent years with close cooperation from BaFin. The work has been taken up to a large extent in the current call for advice. The annual reports on the LTG measures<sup>7</sup> and the EIOPA recommendation on the

recalibration of interest rate risk are particularly worth mentioning in this context<sup>8</sup>.

### 1.2.1.2 Proportionality

The proportionality principle has acquired central significance, not least as a result of the transition to a principles-based supervisory approach (see info box “Insurance Supervision annual conference” on page 104). The proportionality principle ensures that implementation of the requirements of supervisory law should be flexible and in keeping with the risk situation of the respective insurance undertaking. It opens up further scope for discretion in determining how the requirements are applied, which both the insurance undertakings and the supervisory authorities must make use of. This can lead to different perspectives and therefore also to divergent approaches in practice, especially in the initial phase of a new supervisory regime. Supervisors and undertakings must therefore engage in a wide-ranging dialogue with each other.

Solvency II represents a challenge especially for smaller and medium-sized insurance undertakings. In order to reduce the burden to a level that is appropriate and commensurate with the degree of risk, it is particularly important for these insurers to apply the proportionality principle effectively as a corrective.

#### Proportionality principle has proven its worth

In BaFin’s opinion, the proportionality principle has so far proven its worth. This does not mean, however, that it has been applied in the best possible manner to general satisfaction always and everywhere since the new supervisory regime came into force and that there is no need for further optimisation. On the contrary: the application of the principle is an ongoing process, which has to be developed further in a dialogue between supervisors, undertakings and industry representatives. This is because real, practical problems relating to its application were identified once Solvency II went live.

In the course of the 2020 Solvency II Review, BaFin will address problems that it has identified in the application of the proportionality principle at national level. It will also advocate expanding the scope for discretion, so that the proportionality principle results in an appropriately reduced burden in particular for lower-risk insurance undertakings, including the niche insurers.

5 <https://eiopa.europa.eu/publications/requests-for-advice>.

6 Directive 2014/51/EU, OJ EU L 153/1.

7 The third LTG report, produced with the active participation of BaFin, was published on 18 December 2018 and describes how the insurers apply the measures, the impact of measures and the extent to which they are used in the various markets, see [https://eiopa.europa.eu/Publications/Reports/2018-12-18%20\\_LTG%20AnnualReport2018.pdf](https://eiopa.europa.eu/Publications/Reports/2018-12-18%20_LTG%20AnnualReport2018.pdf).

8 See chapter 7 from page 125 of the report at [https://eiopa.europa.eu/Publications/Consultations/EIOPA-18-075-EIOPA\\_Second\\_set\\_of\\_Advice\\_on\\_SII\\_DR\\_Review.pdf](https://eiopa.europa.eu/Publications/Consultations/EIOPA-18-075-EIOPA_Second_set_of_Advice_on_SII_DR_Review.pdf).

## Insurance Supervision annual conference

On 13 November 2018, the 8th Insurance Supervision annual conference took place in Bonn. In his opening speech to around 450 representatives of insurance undertakings and industry associations, Chief Executive Director Dr Frank Grund confirmed that BaFin will play an active part in the forthcoming Solvency II Review. „For me, it is important that we don't talk down Solvency II. The supervisory regime has fundamentally proven its worth. But of course it can be made even better“, commented Grund.

After a talk on the future of retirement provision by Prof. Bernd Raffelhüschen from the University of

Freiburg, the topics of proportionality, digitalisation and the sustainability of investments were examined and developed in three panel discussions.

A debate between Grund and members of the Bundestag Dr Gerhard Schick, Bündnis 90/Die Grünen, and Frank Schäffler, FDP, rounded off the programme. The subjects under discussion included the cap on commissions as a policy instrument, among other items. At the end of the debate, the participants answered questions from the audience.

BaFin's objective, among other things, is to reinforce the principle of proportionality in the context of reporting in general. This could be achieved, for example, by a new design for narrative reports or a reduced number of reporting forms.

### 1.2.2 Decision on collaboration in the supervision of cross-border insurance

On 10 October 2018, the Board of Supervisors of EIOPA adopted an important Decision on international collaboration in insurance supervision. The Decision contains guidelines on the obligations of the member states of the European Economic Area (EEA) to collaborate in the supervision of cross-border distribution activities of insurance undertakings and insurance intermediaries under the Insurance Distribution Directive (IDD) and the related Delegated Regulations.<sup>9</sup> In addition to BaFin, the Federal Ministry for Economic Affairs and Energy (*Bundesministerium für Wirtschaft und Energie*) also affirmed that it would comply with the principles for collaboration and the exchange of information set out in the Decision. Furthermore, the "General Protocol" governs the collaboration of the supervisory authorities in the supervision of undertakings<sup>10</sup>.

<sup>9</sup> EIOPA, Decision of the Board of Supervisors on the cooperation of the competent authorities of the Member States of the European Economic Area with regard to Directive (EU) 2016/97 of the European Parliament and of the Council of 20 January 2016 on insurance distribution.

<sup>10</sup> EIOPA, Decision on the collaboration of the insurance supervisory authorities.

### 1.3 Occupational retirement provision

#### Implementation of the IORP II Directive

The IORP II Directive<sup>11</sup>, which replaced the existing IORP Directive<sup>12</sup>, was required to be transposed into national law by 13 January 2019. The German legislature has therefore adopted the "Act Implementing Directive (EU) 2016/2341 of the European Parliament and of the Council of 14 December 2016 on the Activities and Supervision of Institutions for Occupational Retirement Provision (IORPs) (new version) (*Gesetz zur Umsetzung der Richtlinie (EU) 2016/2341 des Europäischen Parlaments und des Rates vom 14. Dezember 2016 über die Tätigkeiten und die Beaufsichtigung von Einrichtungen der betrieblichen Altersversorgung (EbAV)*) (Neufassung)". It was promulgated in the Federal Law Gazette on 31 December 2018.<sup>13</sup>

The new provisions for *Pensionskassen* and *Pensionsfonds* contain changes relating principally to the system of governance and the obligations to provide information. With respect to the system of governance, provisions have been added in particular for the key functions required to be established and the own risk assessment. *Pensionskassen* and *Pensionsfonds* are now required to have an independent risk control function, an internal audit function and, where necessary, an actuarial function.

<sup>11</sup> Directive (EU) 2016/2341, OJ EU L 354/37.

<sup>12</sup> Directive 2003/41/EC, OJ EU L 235/10.

<sup>13</sup> Federal Law Gazette I 2018, page 2672.



The obligations to provide information to the beneficiaries are expanded as a consequence of the Directive. The German Insurance Supervision Act (*Versicherungsaufsichtsgesetz*) therefore now provides, among other things, for a pension benefit statement with standard minimum contents which must be provided at least every 12 months. These information requirements will be specified in more detail in a regulation.

On the basis of the IORP II Directive, the German legislature has also incorporated provisions relating to cross-border portfolio transfers into the Insurance Supervision Act. These provisions allow portfolios or sub-portfolios of an IORP to be transferred to another IORP domiciled in a different EU member state.

In addition to implementing the IORP II Directive, the implementing act contained further amendments to the Insurance Supervision Act. For example, there are now statutory provisions enabling mutual insurance associations to raise an additional initial fund for the purpose of strengthening their capital. It is also clarified that *Pensionsfonds* may provide funeral expenses benefits.

EIOPA has established two working groups focusing on the implementation of the IORP II Directive. The Project Group on the Pension Benefit Statement (PBS) and Other Information Documents of IORP II has been working on existing practice under the IORP I Directive in the different member states and has already submitted two reports. The findings of the "Project Group on IORP II Implementation: Governance and Risk Evaluation" are expected during the course of 2019.

## 1.4 Evaluation of the Life Insurance Reform Act

In order to reflect the effects of the low interest rate environment, the legislature has amended the statutory requirements for life insurers by means of the German Life Insurance Reform Act (*Lebensversicherungsreformgesetz*), to ensure that all policyholders receive their guaranteed benefits over the long term.

The Federal Ministry of Finance (*Bundesministerium der Finanzen* – BMF) evaluated the effectiveness of the LVRG as at the 1 January 2018 reference date. The findings have been summarised in a report.<sup>14</sup> The report deals

with the impact of the Life Insurance Reform Act. It also addresses other important topics, such as the structure of the *Zinszusatzreserve*, the future treatment of the maximum technical interest rate and questions relating to portfolio run-offs.

### 1.4.1 Findings of the evaluation report

According to the evaluation report, the measures contained in the Life Insurance Reform Act have largely proved to be a success. This is shown by the fact that the life insurers have been able to provide the benefits promised and comply with all regulatory requirements – in particular further building up the *Zinszusatzreserve*. This has been possible despite a further decline in the level of interest rates since the Life Insurance Reform Act came into force, with the associated trend towards an increased risk potential. Furthermore, the insurers have complied with the stricter requirements for transparency. There is nevertheless a need for action on particular points. The evaluation report lists the key features of the further measures required in this context.

### 1.4.2 Key features of the further measures required

#### **Readjustment of the *Zinszusatzreserve***

The *Zinszusatzreserve* was introduced in 2011. Its purpose is to ensure that, in the persisting low interest rate environment, the insureds receive the benefits promised to them over the long term as well<sup>15</sup>. The guarantees have now been secured to a considerable extent. While there is a need to build up the *Zinszusatzreserve* further in view of the low returns the undertakings are earning on new investments, this can be done in smaller stages. At the same time, it is proposed to extend the period over which the *Zinszusatzreserve* is released, so that it helps to fund the interest guarantees on behalf of the insureds over a longer time frame.

#### **Statutory cap on commissions**

Further efforts to reduce costs in the life insurance sector are necessary.

Commissions continue to be permitted under the European directive on insurance distribution which was transposed into German law in 2017<sup>16</sup>. Any inappropriate incentives must be avoided, however. The Federal government is therefore considering the introduction of a statutory cap on commissions, which is intended

<sup>14</sup> [https://www.bundesfinanzministerium.de/Content/DE/Downloads/Finanzmarktpolitik/2018-06-28\\_Evaluierungsbericht-zum-Lebensversicherungsreformgesetz.pdf?\\_\\_blob=publicationFile&v=1](https://www.bundesfinanzministerium.de/Content/DE/Downloads/Finanzmarktpolitik/2018-06-28_Evaluierungsbericht-zum-Lebensversicherungsreformgesetz.pdf?__blob=publicationFile&v=1).

<sup>15</sup> See also 2.6.1.

<sup>16</sup> Federal Law Gazette I 2017, page 2789.

to include payment protection insurance in particular. This would enable the issue of excessive distribution costs to be addressed at the same time.

### Further points from the evaluation report

Other topics addressed in the evaluation report focus on a participation incentive for owners for the funding of the *Zinszusatzreserve*, more detailed statutory rules on profit transfer agreements, the specification of a maximum technical interest rate under Solvency II, clarification of the statutory provisions relating to the guarantee fund and clearer requirements for the calculation of actual costs.

BaFin is contributing its expert knowledge to assist in implementing the proposed measures. For example, with the Third Regulation Amending Regulations under the Insurance Supervision Act (*Dritte Verordnung zur Änderung von Verordnungen nach dem Versicherungsaufsichtsgesetz*)<sup>17</sup>, amendments to the Premium Reserve Regulation (*Deckungsrückstellungsverordnung*) and the Regulation on the Supervision of Pensionsfonds (*Pensionsfonds-Aufsichtsverordnung*) have already been achieved in order to implement the necessary readjustment of the *Zinszusatzreserve*. The new rules were already available at the 31 December 2018 reporting date as a result. Their effect is that the “corridor approach” now limits the annual changes in the reference interest rate used to determine the amount of the reserve.<sup>18</sup>

## 1.5 BaFin Circulars

### 1.5.1 Supervisory Requirements for IT in Insurance Undertakings (VAIT)

In July 2018 BaFin published the Supervisory Requirements for IT in Insurance Undertakings (*Versicherungsaufsichtliche Anforderungen an die IT*)<sup>19</sup>. The VAIT<sup>20</sup> reflect the particular significance of information technology (IT) for insurance undertakings.<sup>21</sup> The Circular contains guidance on interpreting the requirements for the system of governance in the Insurance Supervision Act, to the extent that they relate to the technical and organisational resources of the undertakings.

17 Federal Law Gazette I 2017, page 1653.

18 For further details, see the information provided by BaFin on the corridor approach: [www.bafin.de/dok/11850558](http://www.bafin.de/dok/11850558).

19 Circular 10/2018 – Supervisory Requirements for IT in Insurance Undertakings (VAIT) (only available in German).

20 See chapter II 6.4.

21 See BaFinJournal July 2018, page 4 (only available in German).

The aim of the VAIT is to provide the management boards of the undertakings with a flexible and practice-oriented framework for the IT structure, in particular for the management of the IT resources and for IT risk management. The Circular is applicable to all insurance undertakings and *Pensionsfonds* subject to supervision by BaFin. It does not apply to special purpose insurance companies within the meaning of section 168 of the Insurance Supervision Act and guarantee schemes within the meaning of section 223 of the Insurance Supervision Act.

### Common IT standards

The Circular addresses topics which BaFin currently considers to be particularly important. The related supervisory requirements are not exhaustive with regard to depth or scope of regulation.

All undertakings therefore still have a fundamental obligation, beyond the detailed provisions of the VAIT, to observe common IT standards and keep their technology up to date as well. The principles-based requirements of the Circular reflect the principle of proportionality.

For undertakings falling within the scope of the Solvency II supervisory regime, the obligations contained in the Minimum requirements under supervisory law on the system of governance of insurance undertakings (*Mindestanforderungen an die Geschäftsorganisation*) remain unaffected. The VAIT have a modular structure. This allows BaFin to react flexibly to current developments.

### 1.5.2 Distribution circular

As a result of the implementation of the European directive on insurance distribution<sup>22</sup>, BaFin carried out a fundamental revision of its existing distribution circular 10/2014 in 2018. It had been preceded by the transposition of the directive into German law by means of the implementing act of 20 July 2017.<sup>23</sup> This resulted in new requirements relating to direct distribution, the product approval process, professional development and to distribution remuneration, among other things. In addition, the Insurance Supervision Act governs national specificities such as the prohibition on special allowances, in particular the passing on of commissions, and the pass-through of the majority of the costs

22 Directive (EU) 2016/97/EU, OJ EU L 26/19.

23 Federal Law Gazette I 2017, page 2789.

for insurance mediation if an insurance consultant is engaged (pass-through provision).

In its new Circular 11/2018 on collaboration with insurance intermediaries and on risk management in distribution dated 17 July 2018 and in an accompanying letter, BaFin gives guidance on the application of the new distribution provisions in practice, and at the same time sets out what it expects from the insurance industry.<sup>24</sup> The Circular leaves much of the guidance from the previous circular unchanged, but places an emphasis on topics such as the ban on sharing commissions, distribution remuneration, incentives and conflicts of interest.

The ban on sharing commissions, which was primarily governed by legal regulations in the past, has been established in statute in the Insurance Supervision Act since 29 July 2017 and also in the German Industrial Code (*Gewerbeordnung*) since 23 February 2018. Questions of interpretation arose in particular in relation to the two exemptions, relating firstly to low-value inducements<sup>25</sup> and secondly to a permanent reduction in premiums for the mediated contract<sup>26</sup>.

The second exemption gave rise to much discussion, in particular for the sharing of commissions by insurance intermediaries. On this point, BaFin made it clear at an early stage that according to the wording of section 48b (4) sentence 1 of the Insurance Supervision Act, there has to be an involvement by the insurance undertaking, in addition to an arrangement between the insurance intermediary and its customer.<sup>27</sup> This is the only way to ensure that a permanent reduction in premiums in the interest of the customer occurs not just in economic terms, but is safeguarded in the insurance contract itself, and it also ensures that the reduction does not depend on the creditworthiness of the insurance intermediary. The Administrative Court in Frankfurt am Main has confirmed this opinion in summary proceedings.<sup>28</sup> The appeal by the applicant insurance broker against the decision of first instance was rejected by the Higher Administrative Court of Hesse, although the court did not address the terms of the ban on the passing-on of commissions.<sup>29</sup>

Another significant group of issues for the insurance industry in practice relates to the remuneration of insurance intermediaries. For all insurance products, the remuneration of insurance undertakings and their employees for distribution activities may not conflict with their obligation to act in the best possible interests of customers at all times.<sup>30</sup> In this connection, commission-based distribution, non-performance-related remuneration – in particular of salaried employees in the sales network – and fee-based advice continue to exist in parallel. BaFin also makes important statements in the Circular on chains of brokers, inducements to third parties financially linked to the insurance intermediary and the criteria for calculating commissions, group insurance contracts and the intermediation of net products.

### 1.5.3 Actuarial expert reports

In January 2018, BaFin published its guidance on the preparation of actuarial expert reports for *Pensionskassen* as Circular 2/2018.<sup>31</sup> It replaces Circular 9/2008 (VA).

BaFin has updated the legal references in the Circular to reflect the current status of the Insurance Supervision Act and the regulations based on it. It also reflects the information requirements relating to the option for deregulated *Pensionskassen* of recognising a collective portion of the provision for bonuses pursuant to section 140 (4) of the Insurance Supervision Act.

BaFin also updated its guidance on the preparation of actuarial expert reports for *Pensionsfonds* in Circular 3/2018<sup>32</sup>.

The Regulation on the Supervision of *Pensionsfonds* (*Pensionsfonds-Aufsichtsverordnung*)<sup>33</sup> issued in 2016 resulted in the need to revise the existing Circular 8/2009 (VA). In addition, the information requirements relating to the option available to *Pensionsfonds* of establishing a collective portion of the provision for bonuses and of commitments entered into pursuant to section 236 (3) of the Insurance Supervision Act (non-insurance-based pension payments) were expanded. Furthermore, additional information is required in future for commitments pursuant to

24 [www.bafin.de/dok/11277616](http://www.bafin.de/dok/11277616) (only available in German).

25 Section 48b (2) of the Insurance Supervision Act.

26 Section 48b (4) sentence 1 of the Insurance Supervision Act.

27 See BaFinJournal October 2017, page 22 (only available in German).

28 Frankfurt Administrative Court (*Verwaltungsgericht*), decision of 28 September 2018 (7 L 3307/18.F).

29 Higher Administrative Court (*Verwaltungsgerichtshof*) of Hesse, decision of 5 February 2019 (6 B 2061/18).

30 Section 48a (1) sentence 1 of the Insurance Supervision Act.

31 Circular 2/2018 – Guidelines for the preparation of actuarial expert reports for *Pensionskassen* (only available in German).

32 [www.bafin.de/dok/10402748](http://www.bafin.de/dok/10402748) (only available in German).

33 Federal Law Gazette I 2016, page 842.

section 236 (2) of the Insurance Supervision Act (traditional non-insurance-based business).

## 1.5.4 Solvency of financial conglomerates

On 20 February 2018 BaFin published its Circular 04/2018 (VA) on solvency reporting for financial conglomerates. It deals with additional supervision for financial conglomerates relating to an appropriate level of own funds. The scope of the Circular includes all undertakings of a financial conglomerate required to be included in the calculation of own funds under section 18 (1) of the German Financial Conglomerates Supervision Act (*Finanzkonglomerate-Aufsichtsgesetz*).

In particular, the Circular contains detailed requirements for the disclosures necessary to demonstrate an appropriate level of own funds at the level of a financial conglomerate.

Three possible methods are prescribed for the calculation of the solvency of financial conglomerates: They are "Calculation on the basis of the consolidated financial statements" (method 1), the "Deduction and aggregation method" (method 2) and finally the "Combination method" (method 3), which combines methods 1 and 2. The undertakings must submit the calculation of the solvency of financial conglomerates once a year to BaFin and the Deutsche Bundesbank, and also to the European Central Bank (ECB) in the case of significant conglomerates managed by a bank.

# 2 Supervision in practice

## 2.1 Risk classification

BaFin allocates the insurance undertakings it supervises to risk classes that it uses to define how closely the insurers are supervised. Insurers are allocated to classes using a two-dimensional matrix that reflects their market impact and quality. The market impact of life insurers, *Pensionskassen* and *Pensionsfonds* is measured on the basis of their total investments. The relevant parameter for health insurers, property/casualty insurers and reinsurers is those undertakings' gross premium income.

Market impact is measured on a four-tier scale of "very high", "high", "medium" and "low". The quality of the insurers is based on an assessment of the following factors: net assets, financial position and results of operations; growth and quality of management.

BaFin assesses the first two factors using insurance-specific (mainly quantitative) indicators, while it assesses management quality using qualitative criteria. The rating system adds together the ratings of the individual factors to form an overall rating on a four-tier scale from "A" (high quality) to "D" (low quality).

Table 23 (page 109) shows the assessment based on the data as at 31 December 2018.

### Number of good-quality insurers at previous year's level

For the purposes of the risk classification, BaFin classified 74.5% of the insurers in the higher quality range, i.e. as "A" or "B". At the same time, a modest increase in the number of undertakings assessed as "B" was recorded, while the number of undertakings rated "C" declined. As in the previous years, BaFin did not rate any insurers with high or very high market relevance as an undertaking with low quality.

### Results in the individual insurance classes

There were no great changes either for the health insurance undertakings or for the property and casualty insurers in comparison with the prior year. The proportion of undertakings in the upper quality bracket in the 2018 reporting year was again over 80% for the property/casualty insurers, and again amounted to over 70% for the health insurance undertakings.

The life insurers achieved modest improvements, on the other hand. The proportion of life insurers rated "B" rose year-on-year by around 5%, while at the same time the proportion assessed as "C" declined by around 5%. Most of the undertakings therefore continued to be classified in the medium quality range.

A shift in the quality assessment from "C" to "B" was also observed for the *Pensionsfonds* and *Pensionskassen*.

The reinsurers also recorded minor changes, although the majority or around 79% of the undertakings continued to be classified in the upper quality range.

### Small increase in the number of classified insurers

The number of insurance undertakings and *Pensionsfonds* classified in the 2018 reporting year rose slightly in contrast to previous years.

### Classification of insurance groups

As well as classifying the risks associated with individual insurance undertakings, BaFin also classifies all insurance groups subject to Solvency II for which it has responsibility for group supervision at group level for 2018.

**Table 23: Risk classification results**

As at 31 December 2018

Undertakings in %		Quality of the undertaking				Total
		A	B	C	D	
Market impact	very high	0.0	1.9	0.8	0.0	2.7
	high	1.3	7.9	2.9	0.0	12.1
	medium	2.1	17.3	6.3	0.2	25.9
	low	6.7	37.3	13.6	1.7	59.3
<b>Total</b>		<b>10.1</b>	<b>64.4</b>	<b>23.6</b>	<b>1.9</b>	<b>100.0</b>

In contrast to a purely mathematical aggregation of the classification results of the individual undertakings, this quality assessment uses additional qualitative and quantitative group-specific inputs, such as profit transfer and control agreements. The annual group-level risk classification reflects the growing importance of the supervision of insurance groups. It was updated and expanded with the introduction of Solvency II. The data resulting from BaFin's group-level risk classification thus generate significant added value and provide aggregated information on the overall position of the group.

## 2.2 On-site inspections

On-site inspections are planned using a risk-based approach. As well as the results of the risk classification, one of the factors that BaFin takes into account is whether an insurer was subject to an on-site inspection in the recent past. Ad hoc on-site inspections are also conducted.

In the year under review, BaFin's Insurance Supervision Sector conducted a total of 104 on-site inspections, similar to the number conducted in 2016, whereas 115 were carried out in 2017. The slight decline in on-site inspections compared with the prior year was partly caused by the need to defer some inspections to the following year.

The following risk matrix (Table 24) shows the breakdown of the inspections by risk class.

## 2.3 Priority areas for Insurance Supervision

In order to make efficient use of its resources, Insurance Supervision defines priority areas on an annual basis. For the purpose of selecting them, it identifies, assesses and prioritises all relevant supervisory topics arising from operational supervision. Its planning also encompasses those issues that have particular significance for the

**Table 24: Breakdown of on-site inspections by risk class in 2018**

On-site inspections		Quality of the undertaking				Total	Undertakings in %
		A	B	C	D		
Market impact	very high	0	3	0	0	3	3.1
	high	1	18	3	0	22	22.4
	medium	2	11	4	0	17	17.3
	low	4	36	12	4	56	57.1
<b>Total*</b>		<b>7</b>	<b>68</b>	<b>19</b>	<b>4</b>	<b>98</b>	<b>100.0</b>
<b>Undertakings in %</b>		<b>7.1</b>	<b>69.4</b>	<b>19.4</b>	<b>4.1</b>	<b>100.0</b>	

\* Six on-site inspections were also conducted at unclassified undertakings, bringing the total to 104 inspections.

sector as a whole, whether from a regulatory or a strategic point of view. If there are changes in the general conditions affecting the industry, this can be taken into account where necessary. The priority work areas for Insurance Supervision in 2018 were as follows:

- Cyber security<sup>34</sup>
- Analysis of a possible search-for-yield approach for insurers and *Pensionsfonds* when making new investments<sup>35</sup>
- Sustainability in investment by insurers and *Pensionsfonds*<sup>36</sup>
- Development of premiums, claims and earnings in property and casualty insurance<sup>37</sup>
- Claims provisions (for selected property and casualty insurers)<sup>38</sup>

### Economic scenario generators

For certain undertakings, BaFin also conducted a closer investigation of how they are using economic scenario generators (ESGs). These ESGs enable undertakings to measure the technical provisions for products with interest guarantees and discretionary bonuses stochastically. By simulating typically 1,000 to 5,000 future economic scenarios, the undertakings can model their portfolios with the help of assumptions about the reactions of policyholders and management to a variety of economic situations.

The Solvency II Directive<sup>39</sup> and the related Delegated Regulation<sup>40</sup> contain only very general provisions on this subject which are set out in detail at a subordinate legal level, not least including BaFin's interpretative decision dated 10 November 2016.<sup>41</sup> Nevertheless, there remains a certain degree of freedom in applying these requirements which may be material in particular cases.

BaFin is therefore using the knowledge acquired to date relating to ESGs as an opportunity to undertake deeper quantitative analyses across the industry. It is using data and documentation already available at the undertakings for this purpose.

### Recovery and resolution planning

Issues relating to recovery and resolution planning for insurance undertakings represented a further priority area.

The starting point was the expanded supervision of G-SIIs in accordance with the Key Attributes of Effective Resolution Regimes for Financial Institutions issued by the FSB in 2014. The components of this expanded supervision include a prospective recovery plan and a resolution plan for the particular G-SII.

BaFin is already making use of the option of requiring insurers to submit prospective general recovery plans. It is permitted to do this by the provisions in section 26 (1) of the Insurance Supervision Act for individual undertakings and section 26 (1) in conjunction with section 275 (1) of the Insurance Supervision Act for group undertakings. In 2018, BaFin was thus able to undertake an initial evaluation of general recovery plans on the legal basis of the Insurance Supervision Act for large German insurance groups with international operations.

### 2.4 EIOPA stress test for insurance groups

EIOPA once again carried out a stress test for insurers across the EU in 2018. The stress test was based on the Solvency II valuation standard and was aimed at large European insurance groups. The participants in the test also included five insurance groups from Germany: Allianz, Munich Re, HDI, R+V Versicherung and the HUK-COBURG insurance group.

#### EIOPA stress test analyses various potential risks

The objective of the 2018 EIOPA stress test was to assess the resilience of the European insurance sector in the face of adverse developments and to identify vulnerabilities. For this purpose, the insurance groups were required to calculate a baseline scenario and three stress scenarios as at the 31 December 2017 reference date. They also had to answer qualitative questions, for example relating to cyber risks.

The yield-curve-up scenario, the first stress scenario, assumed a sharp increase in interest rates with significant capital market disturbances, accompanied by a high cancellation rate for life insurance contracts and cost increases for non-life insurance.

The yield-curve-down scenario, the second stress scenario, assumed a decline in interest rates with a long-term low interest rate environment and a simultaneous increase in life expectancy.

34 See chapter II 6 and BaFinJournal August 2018, page 10f (only available in German).

35 See 2.5.2.

36 See 2.5.3.

37 See 2.6.3.

38 See 2.6.3.

39 Directive 2009/138/EC, OJ EU L 335/1.

40 Delegated Regulation (EU) 2015/35, OJ EU L 12/1.

41 [www.bafin.de/dok/8524334](http://www.bafin.de/dok/8524334).

The third scenario simulated natural disasters, including storms, floods and earthquakes, in different regions of Europe.<sup>42</sup>

To enable the impact of the stress scenarios to be evaluated, the participating insurance groups were first of all required to recalculate the solvency capital requirements as well.

The results indicate that the European insurance sector proved to be fundamentally robust in the stress scenarios. The results for the German participants also confirm the impression for Europe as a whole. As expected, a long-term low interest rate environment continues to represent a challenge for the German insurance industry.

## 2.5 Investments of primary insurers

### 2.5.1 Overview

As at 31 December 2018, the carrying amount of the aggregate investments managed by German primary insurers under BaFin's supervision amounted to €1,556 billion (previous year: €1,517 billion), as shown in Table 25 (page 112).<sup>43</sup> Aggregate investments grew by 2.5% (+€39 billion) in 2018. Broken down by insurance classes, property and casualty insurers (+5.9%) and health insurers (+3.6%) recorded the largest percentage increases. Only the funeral expenses funds recorded a decline in investments compared with the prior-year figure.

#### Priority area

As in previous years, investments continued to focus on fixed-income securities and promissory note loans. There were minor shifts in fixed-rate investments. For example, the share of directly held listed bonds rose by 7.3% to €288 billion in the year under review, while the share of investments at credit institutions declined year on year.

Indirect investments held by insurance undertakings via investment funds again recorded above-average growth in 2018 (+3.0%), and – as in the previous year – now account for over one-third of the aggregate investments of all primary insurers at €558 billion. As in previous years, the assets acquired via investment funds consist

mostly of listed securities. Aggregate direct investments in property rose by 2.2% year on year to €36 billion.

### 2.5.2 Search for Yield<sup>44</sup>

In view of the persisting low interest rate environment, new investments and reinvestments of assets are a subject of particular interest for insurance supervision. This enables reactions in response to risks to be estimated and reveals developing investment trends.

BaFin investigated new investments and reinvestments in the case of 18 on-site inspections of insurance undertakings. The undertakings made new investments representing on average 12% of the investment portfolio. Most of the undertakings added to their portfolio of funds, with corporate and government bonds predominating. In addition, each of the undertakings inspected was attempting to develop its own expertise in a particular alternative type of investment, such as private equity or private debt for smaller undertakings. Infrastructure investments, on the other hand, are especially attractive to the larger undertakings, although they represent only a small portion of the investment portfolio.

High-yield investments accounted for only an insignificant share of the total. BaFin observed growth in risky investments at only a few undertakings.

### 2.5.3 Sustainable investment activity in the insurance sector

As providers of insurance products, insurers suffer an immediate and ever-increasing impact from the direct effects of climate change, such as natural disasters in the form of floods, storms and heat waves. But the issue of climate change is also becoming more important for insurers from an investment point of view – primary insurers are among the largest institutional investors in Germany, after all.

The European Commission's legislative proposals<sup>45</sup> dated May 2018 demonstrate that insurers will have to address the issue of sustainability in their investment activities. This is because the proposals contain regulatory requirements relating to sustainability that go beyond the provisions currently applying to insurers.

<sup>42</sup> See BaFinJournal August 2018, page 32 f. (only available in German).

<sup>43</sup> For details of the investments of the individual insurance classes and the *Pensionsfonds*, see 2.6.

<sup>44</sup> See 2.3.

<sup>45</sup> <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:52018DC0097&from=EN>.

**Table 25: Investments of primary insurers\***

Investments of primary insurers (carrying amounts, HGB)	Portfolio as at 31 December 2018		Portfolio as at 31 December 2017		Change in 2018	
	in € million	in %	in € million	in %	in € million	in %
	Land, land rights and shares in real estate companies, REITs and closed-ended real estate funds	35,835	2.3%	35,063	2.3%	772
Fund units, shares in investment stock corporations and investment companies	558,448	35.9%	542,047	35.7%	16,401	3.0%
Loans secured by mortgages and other land charges and shareholder loans to real estate companies	64,289	4.1%	63,019	4.2%	1,270	2.0%
Securities loans and loans secured by debt securities	1,611	0.1%	1,183	0.1%	428	36.2%
Loans to EEA/OECD states, their regional governments and local authorities and international organisations	130,699	8.4%	128,681	8.5%	2,018	1.6%
Corporate loans	16,777	1.1%	16,185	1.1%	592	3.7%
ABSs/CLNs	5,464	0.4%	5,514	0.4%	-50	-0.9%
Policy loans	2,545	0.2%	2,660	0.2%	-115	-4.3%
<i>Pfandbriefe</i> , municipal bonds and other bonds issued by credit institutions	188,290	12.1%	193,114	12.7%	-4,824	-2.5%
Listed bonds	287,497	18.5%	267,892	17.7%	19,605	7.3%
Other bonds	24,581	1.6%	23,617	1.6%	964	4.1%
Subordinated debt assets/profit participation rights	23,105	1.5%	23,219	1.5%	-114	-0.5%
Book-entry securities and open market instruments	696	0.0%	644	0.0%	52	8.1%
Listed equities	1,698	0.1%	1,633	0.1%	65	4.0%
Unlisted equities and interests in companies, excluding private equity holdings	36,316	2.3%	34,733	2.3%	1,583	4.6%
Private equity holdings	21,511	1.4%	18,841	1.2%	2,670	14.2%
Investments at credit institutions	135,525	8.7%	139,062	9.2%	-3,537	-2.5%
Investments covered by the enabling clause	19,701	1.3%	18,961	1.2%	740	3.9%
Other investments	1,154	0.1%	1,056	0.1%	98	9.3%
<b>Total investments</b>	<b>1,555,742</b>	<b>100.0%</b>	<b>1,517,124</b>	<b>100.0</b>	<b>38,618</b>	<b>2.5%</b>
Life insurers	925,928	59.5%	909,156	59.9%	16,772	1.8%
<i>Pensionskassen</i>	166,297	10.7%	164,090	10.8%	2,207	1.3%
Funeral expenses funds	2,004	0.1%	2,055	0.1%	-51	-2.5%
Health insurers	282,758	18.2%	273,044	18.0%	9,714	3.6%
Property/casualty insurers	178,758	11.5%	168,779	11.1%	9,979	5.9%

\* The figures are based on the primary insurers' quarterly reports for the second quarter of 2018 and are only preliminary.



### Industry survey

BaFin conducted an industry survey on investment activity in the insurance sector during the year under review. Its aim was to use the survey to establish the nature and extent of sustainable investment by the German insurance industry.<sup>46</sup>

The current reporting system for investments does not provide information on insurers' sustainable investment activity. The survey was therefore necessary in order to determine how and to what extent the insurance sector observes the ESG (environmental, social and governance) criteria when making investments.

The survey encompassed all primary insurers and reinsurance undertakings – with the exception of the funeral expenses funds – as well as institutions for occupational retirement provision subject to supervision by BaFin. The basis for the figures submitted was the balance sheet as at 31 December 2017. Since the concept of sustainability, on which the questionnaire was based, has not yet been defined in law, each undertaking's understanding of the issue was the main factor determining their responses.

### Results of the survey

The survey found that the relevant insurers themselves classified around 73% of their investments covered by the survey as sustainable.

The findings show that 57% of the undertakings take environmental concerns into consideration when selecting investments. 56% attach importance to social criteria and nearly 55% to governance issues. Just under 16% of the undertakings have signed the Principles for Responsible Investment<sup>47</sup> or comply with the Principles for Sustainable Insurance<sup>48</sup>. Both sets of principles were initiated by the United Nations.

Nearly 41% of the insurers participating in the industry survey indicated their intention of expanding their ESG investments.<sup>49</sup>

### Workshops

BaFin held discussions with insurers and institutions for occupational retirement provision in two workshops

on the topic "Sustainable investment activity in the insurance sector – Integration of ESG criteria into risk management". The main issue was how to implement the regulatory requirements for sustainable investment in the risk management system and what particular challenges that poses.<sup>50</sup>

## 2.6 Developments in the individual insurance classes

The following figures for 2018 are only preliminary. They are based on the interim reporting as at 31 December 2018.

It should also be noted that, in accordance with section 45 of the Insurance Supervision Act, BaFin has exempted certain undertakings falling within the scope of the Solvency II Directive from elements of the interim reporting requirements.<sup>51</sup>

### 2.6.1 Life insurers

#### Business trends

New direct life insurance business in 2018 amounting to approximately 5.1 million new policies exceeded the previous year's level of 4.9 million. The total value of new policies underwritten also rose by 4.8% to around €278.5 billion compared with €265.8 billion in the previous year.

The share of the total number of new policies accounted for by term insurance policies increased year on year from 35.4% to 37.5%.

The share attributable to pension and other insurance contracts declined from 55.5% to 53.8% over the same period. The proportion of endowment life insurance policies also fell by 0.5 percentage points to 8.6%.

Early terminations of life insurance policies (surrender, conversion to paid-up policies and other forms of early termination) remained unchanged from the prior-year level at 2.2 million contracts. In contrast, the total sum insured of policies terminated early rose to €105.2 billion compared with €98.5 billion in the previous year.

46 See BaFinJournal July 2018, page 17 ff. (only available in German).

47 <https://www.unpri.org>.

48 <http://www.unepfi.org/psi>.

49 For the results of the industry survey, see [www.bafin.de/dok/11083362](http://www.bafin.de/dok/11083362) (only available in German).

50 See BaFinJournal July 2018, page 17 ff. (only available in German) and BaFinJournal December 2018, page 11 f.

51 For the number of undertakings under supervision, see the Appendix, page 175.

There were a total of approximately 83.0 million direct life insurance contracts at the close of 2018, compared with 83.7 million in the previous year. However, the sum insured increased by 1.0% to €3,134 billion. Term insurance policies recorded a marginal decrease in the number of contracts from 12.9 million to around 12.8 million, and a decline in the sum insured from €827.9 billion to €815.7 billion. Pension and other insurance policies continued the positive trend of previous years, with the number of contracts growing from 54.4% to 55.8% as a proportion of the total. The share of the total sum insured rose from 55.6% to around 57.4%.

Gross premiums written in the direct insurance business of the German life insurers increased to €87.4 billion in the year under review (previous year: €85.6 billion).

### Investments

Aggregate investments increased in the year under review by 4.8% from €906.1 billion to €949.2 billion. Net hidden reserves fell to €105.5 billion at the year-end compared with €132.6 billion in the previous year. This corresponds to 11.1% of the aggregate investments, following 14.6% in the prior year.

Preliminary figures show a decline in the average net investment return to 3.6% in 2018, significantly lower than the prior-year level of 4.4%. One reason for the fall in the net return is likely to be the readjustment of the *Zinszusatzreserve* and the resulting lower figure for realisations of valuation reserves.

### Projections

BaFin again prepared projections for the life insurers in 2018 (see info box). BaFin uses the projections primarily to analyse how two different capital market scenarios affect the insurers' performance for the current financial year.

The analysis of the projections confirmed BaFin's assessment that the life insurers would be able to satisfy their contractual obligations. However, should the low interest rate environment persist and take another turn for the worse, it is to be expected that the economic position of the undertakings will deteriorate further. BaFin will therefore continue to monitor the insurers closely to ensure that they analyse their future financial development in a continued low interest rate environment at an early stage and in a forward-looking and critical manner. It is essential that the life insurers introduce appropriate measures in good time and make the relevant preparations.

### At a glance

## Life insurance projections

The projection as at the 30 September 2018 reference date focussed on examining the medium- to long-term impact of the low level of interest rates on the life insurers. For this purpose, BaFin collected data on the forecast financial performance in accordance with the German Commercial Code (*Handelsgesetzbuch*) for the 2018 financial year and the following 14 financial years. BaFin assumed that new investments and reinvestments were made solely in fixed-interest investments with an interest rate of 1.2% and otherwise unchanged conditions in the capital markets. In a second scenario, the life insurers were able to simulate new investments and reinvestments and the performance of the capital markets according to their individual corporate planning.

### Solvency II

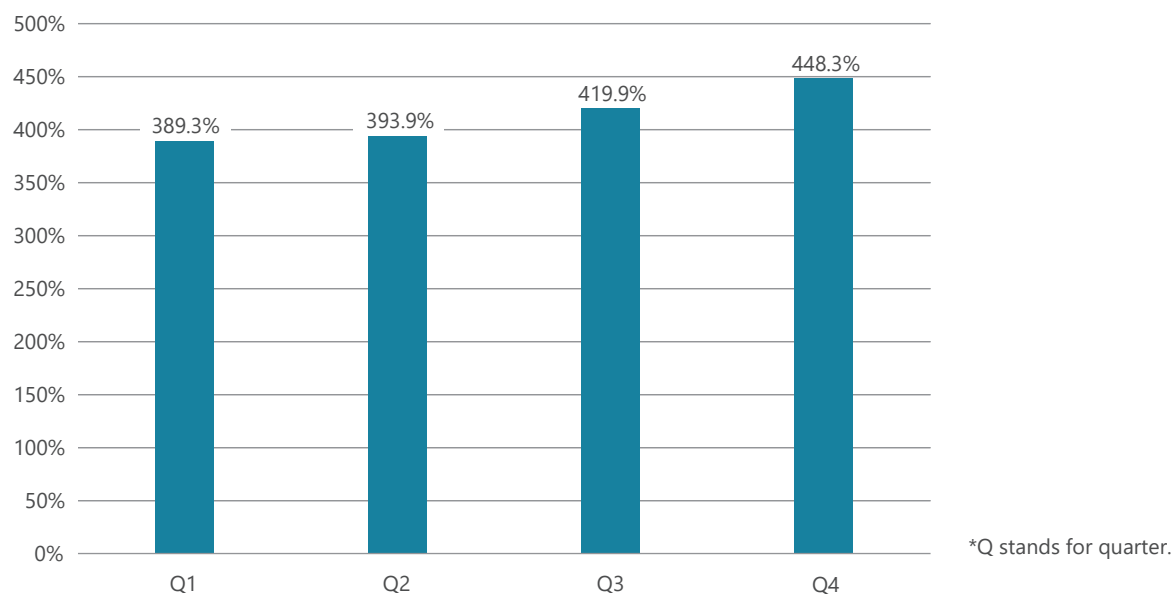
84 of the 85 life insurers supervised by BaFin fell within the scope of Solvency II at the reporting date. For the purpose of calculating the solvency capital requirement (SCR) at the close of 2018, a total of 73 of the 84 undertakings employed the standard formula while 11 undertakings used a (partial) internal model. None of the life insurers used undertaking-specific parameters.

Of the total of 84 life insurers, 44 applied the volatility adjustment in accordance with section 82 of the Insurance Supervision Act and the transitional measure for technical provisions pursuant to section 352 of the Insurance Supervision Act. 10 life insurers used only the transitional measure for technical provisions, and 10 undertakings employed the volatility adjustment as the only measure. One undertaking applied the transitional measure for risk-free interest rates under section 351 of the Insurance Supervision Act, i.e. the transitional discount curve, in combination with the volatility adjustment. In total, therefore, 55 life insurers used the volatility adjustment, 54 life insurers the transitional measure for technical provisions and 1 life insurer the transitional discount curve.

### SCR coverage

All of the life insurance undertakings were able to report adequate SCR coverage as at 31 December 2018. The SCR ratio of the undertakings not exempted from

**Figure 5: Development of SCR coverage ratios**



elements of interim (quarterly) reporting pursuant to section 45 of the Insurance Supervision Act (eligible own funds of the sector in relation to the SCR of the sector) amounted to 448.3% compared with 382.1% in the previous year.

Figure 5 shows the SCR coverage ratios of the life insurance undertakings subject to interim reporting obligations over time.

**Composition of the SCR**

As at 31 December 2018, the SCR of the life insurance undertakings subject to interim reporting obligations declined to €26.9 billion compared with €31.7 billion in the previous year. Measured by the gross basic SCR, 73% on average of the capital requirements of the undertakings applying the standard formula in 2017 was attributable to market risk (excluding diversification effects). In addition, a significant proportion of the SCR related to underwriting risks for life (34%) and health (21%) insurance. By contrast, counterparty default risks (2%) were generally less important. The percentages quoted add up to more than 100% because diversification effects, which reduced the gross basic SCR, have not yet been included. They amounted to 30%.

The SCR required to be covered is calculated on the basis of the gross basic SCR, taking other variables into account. In this context, the loss-absorbing effects of technical provisions (71%) and deferred taxes (8%) reduced the figure, while operational risk (3%) resulted in a slight increase.

**Composition of own funds**

The own funds eligible for the SCR of the life insurance undertakings subject to the interim reporting requirements amounted to €120.5 billion as at 31 December 2018. In the previous year, 98% of the eligible own funds were accounted for by basic own funds and 2% by ancillary own funds. 96% of the eligible own funds were attributable to the highest class of own funds (Tier 1) and the majority of the remainder to the second-highest class (Tier 2). On average, the reconciliation reserve accounted for 66% of the industry’s basic own funds, while surplus funds accounted for 27%. Other noteworthy components at the reporting date were share capital including issuing premiums (4%) and subordinated liabilities (3%).

**Remediation plans**

If undertakings apply one of the transitional measures incorporated in Solvency II and are showing inadequate coverage of the SCR without that measure, they must submit a remediation plan in accordance with section 353 (2) of the Insurance Supervision Act. In the plan, the undertaking must set out the step-by-step introduction of measures planned to generate sufficient own funds or to reduce its risk profile, so that compliance with the solvency capital requirements is ensured without the use of transitional measures at the latest by the end of the transitional period on 31 December 2031.

**26 insurers affected**

26 of the life insurers under supervision by BaFin at the reporting date have been required to submit a

remediation plan since the introduction of Solvency II, because they were unable to guarantee adequate SCR coverage without employing transitional measures. BaFin is in close contact with these undertakings in order to ensure that the SCR is complied with on a long-term basis at the latest following the end of the transitional period. The undertakings concerned are required to comment on the stage of development of the measures in the annual progress reports, even if adequate SCR coverage has been restored in the meantime without the application of transitional measures.

### **Stabilisation of discretionary bonuses**

The majority of the life insurers are retaining the 2018 level of discretionary bonuses for 2019, putting an end to the downward trend seen in recent years. The current total return, i.e. the sum of the guaranteed technical interest rate and the participation in the interest surplus, for the tariffs available in the market for endowment insurance contracts is unchanged at an average of 2.3% for the sector. This figure was 2.3% in 2018 and 2.5% in 2017.

### **Development of the *Zinszusatzreserve***

Since 2011, life insurers have been required to build up an additional interest provision, the *Zinszusatzreserve* (ZZR), to prepare for lower investment income in the future on the one hand and the guarantee obligations on the other, which remain high.<sup>52</sup> Including the readjustment, their expense for this in 2018 was well over €5.9 billion. The cumulative ZZR at the end of 2018 therefore amounted to €65.7 billion. The reference interest rate used to calculate the ZZR was 2.09% at the end of 2018.

#### **2.6.1.1 Run-off**

The topic of external run-offs in the life insurance industry once again represented a priority area for Insurance Supervision in 2018. In contrast to an internal run-off, in the case of an external run-off the life insurance undertaking does not remain in the existing insurance group but becomes part of a new group. At the 2018 year-end, 6 life insurers and 2 *Pensionskassen* were in external run-off; all of them have the legal form of a stock corporation. In one case, the portfolio of a branch of a Swiss undertaking was transferred to a German stock corporation.

Insurance groups whose business model consists of winding up closed insurance books are referred to

as run-off platforms. A change by a group to a run-off platform is generally effected as a sale of the undertaking. Sales of undertakings normally trigger a qualifying holding procedure under section 18 of the Insurance Supervision Act. In this context, BaFin regularly reviews whether the transaction affects the interests of the persons insured – for example, the nature of the acquirer's intended plans for the business and the expected impact on capital resources and customers.<sup>53</sup>

If the extensive documentation, business plans and multi-year forecasts relating to the development of the business required to be submitted reveal potential weaknesses, BaFin requires appropriate precautions to be taken for the protection of customers. These measures may include a guarantee strategy, which could comprise specific investor guarantees and the adequate capitalisation of holding companies.

### **Ongoing supervision**

By concentrating its supervisory activities relating to run-off platforms in the life insurance sector, BaFin has pooled its expertise relating to this business model.

If an undertaking is sold, BaFin's first step is to examine whether and in what manner the undertakings are implementing or have implemented the business plans submitted in the qualifying holding procedure, and whether they comply with any guarantee strategy that may be in place. BaFin also examines major personnel and organisational changes closely. It makes on-site visits to the undertakings for this purpose.

If the size of the portfolios decreases, this may have a negative impact on costs in the long term and restrict the ability of the portfolio to balance risks. BaFin monitors this issue as part of its review of the analysis of profit in accordance with the German Insurance Reporting Regulation (*Verordnung über die Berichterstattung von Versicherungsunternehmen gegenüber der Bundesanstalt für Finanzdienstleistungsaufsicht*).

In the case of undertakings no longer accepting new business, the motivation to provide appropriate discretionary bonuses and good customer service is removed. One area to which BaFin pays close attention is therefore compliance with the provisions relating to participation in profits, in this case principally the Minimum Allocation Regulation (*Mindestzuführungsverordnung*). For the purpose of

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<sup>52</sup> See 1.4.2.

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<sup>53</sup> <https://www.bafin.de/dok/11121600>.

assessing an undertaking's quality of service, BaFin also obtains information from consumer complaints<sup>54</sup> and relating to cancellation behaviour.

## 2.6.2 Private health insurers

### Business trends

The 46 private health insurers supervised by BaFin generated premium income totalling around € 40 billion in 2018. This represents an increase of 1.9% over 2017. The growth in premiums was therefore lower than in the previous year. It was mainly attributable to new business, especially in supplementary insurance, and to premium adjustments.

Comprehensive health insurance, with around 8.7 million persons insured and premium income of €28 billion – representing 70% of total premium income – continued to be the most important business line by far for the private health insurers in 2018. Including the other types of insurance, such as compulsory long-term care insurance, daily benefits insurance and the other partial health insurance types, the private health insurance undertakings insure approximately 42 million people.

### Investments

The health insurers increased the carrying amount of their investment portfolio by 4.8% to approximately €288 billion in the year under review. Investment remained focused on fixed-income securities. BaFin did not identify any significant shifts between the asset classes.

The main macroeconomic factor affecting private health insurers is still the low interest rate environment. Since interest rates in the year under review remained at an extremely low level, the health insurers' reserve situation remains comfortable especially thanks to high valuation reserves in fixed-income securities. At 31 December 2018, net hidden reserves in investments amounted to around €36 billion, or roughly 13% of investments (previous year: 15%).

Preliminary figures put the average net investment return in the year under review at around 3.1%, and therefore below the level of the previous year (3.5%).

### Solvency

Since Solvency II came into effect on 1 January 2016, Solvency I has applied only to six health insurers qualifying as small insurance undertakings within the

meaning of section 211 of the Insurance Supervision Act. Preliminary figures indicate that all six undertakings will comply with the solvency rules applicable to them as at 31 December 2018.

The remaining 40 health insurers were subject to the Solvency II reporting obligations at the end of 2018. The majority of these health insurers apply the standard formula for the purpose of calculating the solvency capital requirement (SCR). Four undertakings used a partial or full internal model. None of the undertakings used undertaking-specific parameters.

### Transitional measures

In the year under review, one health insurer applied the volatility adjustment in accordance with section 82 of the Insurance Supervision Act and the transitional measure for technical provisions pursuant to section 352 of the Insurance Supervision Act. One health insurer used only the transitional measure for technical provisions, while four undertakings employed the volatility adjustment as the only measure. The health insurers did not apply the transitional discount curve, i.e. the transitional measure for risk-free interest rates pursuant to section 351 of the Insurance Supervision Act. Undertakings that apply a transitional measure and reported a shortfall without that measure must submit a remediation plan in accordance with section 353 (2) of the Insurance Supervision Act. None of the health insurers has so far been required to submit a remediation plan of that type.

All of the undertakings demonstrated more than adequate coverage of the SCR at 31 December 2018 – as well as at all the quarterly reporting dates in 2018. Figure 6 "Development of SCR coverage ratios" (page 118) shows the SCR coverage ratios for the sector.

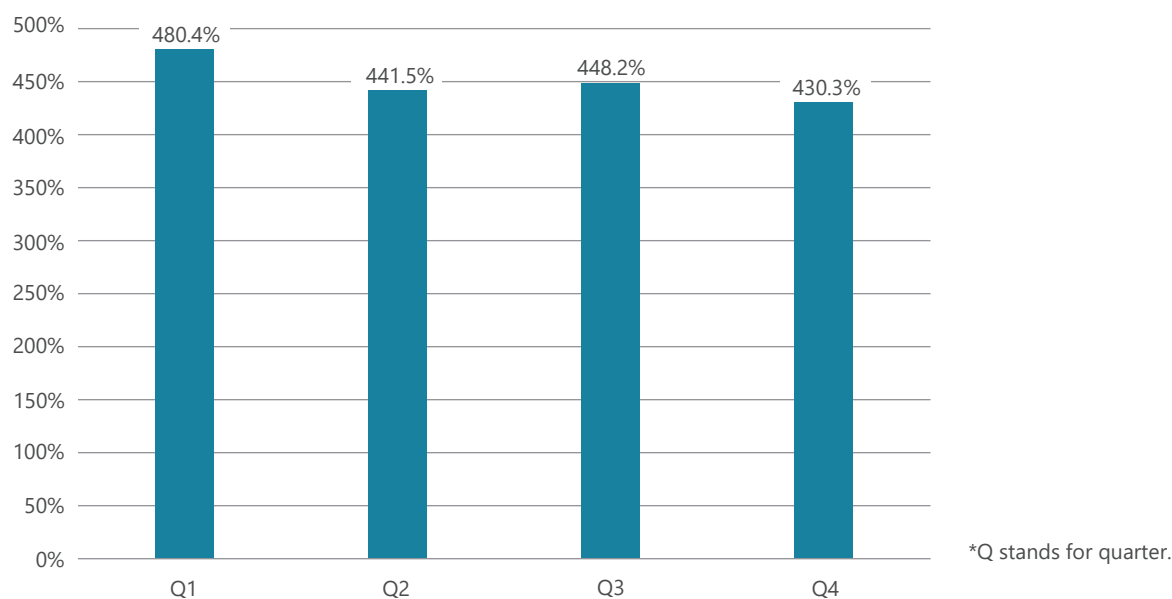
As at 31 December 2017, the SCR coverage ratio amounted to 495%.<sup>55</sup> Only a limited comparison can be made between this figure and the data for the quarterly reporting dates, however, since some undertakings were exempted from elements of the interim reporting requirements in accordance with section 45 of the Insurance Supervision Act. The variations in the coverage ratios are mainly caused by changes in the interest rate environment and in own funds, in particular the surplus funds.

The sector SCR for all private health insurers subject to interim reporting obligations amounted to €6.3 billion

<sup>54</sup> See also chapter II 2.4.3.

<sup>55</sup> Year-end figure.

**Figure 6: Development of SCR coverage ratios**



as at 31 December 2018. The health insurers are primarily exposed to market risk. This was responsible for around 81% of the capital requirements for users of the standard formula at the close of the previous year. Around 38% of the capital requirements at that date related to the underwriting risk for health insurance. The eligible own funds for all health insurers subject to interim reporting obligations amounted to approximately €27.3 billion as at 31 December 2018. The health insurers report the majority of their own funds in the reconciliation reserve. At the end of the previous year, the proportion was approximately two-thirds. The surplus funds are another major component of own funds, accounting for just under one-third. Other components of own funds such as share capital including the attributable issuing premium were comparatively unimportant.

**Projections**

BaFin also carried out a projection exercise for health insurers in 2018 in order to simulate the effects of unfavourable developments in the capital market on their performance and financial stability (see info box).

39 insurers took part in the projection exercise. Only seven undertakings were exempted from taking part by BaFin. These were insurers offering Non-SLT health insurance. These undertakings do not have to establish a provision for increasing age and do not have to generate a specific technical interest rate.

*At a glance*

**Health insurance projections**

The projection as at the 30 September 2018 reference date focussed on examining the medium-term impact of the low level of interest rates on the health insurers. For this purpose, BaFin collected data on the forecast financial performance in accordance with HGB for the 2018 financial year and the following four years – in each case in different unfavourable capital market scenarios. In one scenario, BaFin assumed that new investments and reinvestments were made solely in fixed-interest investments with an interest rate for new investments of 1.2%. In a second scenario, the health insurers could simulate new investments and reinvestments according to their individual corporate planning.

The overall conclusion is that even a persistent low interest rate environment would be tolerable for the health insurers from an economic point of view. As expected, the data generated show that in a low interest rate scenario the risk attaching to new investments and reinvestments continues to arise and that investment returns decline. This demonstrates that the technical interest rate must be gradually brought down by means of premium adjustments.

## ACIR and technical interest rate

The health insurers base the determination of the technical interest rate on the actuarial corporate interest rate (ACIR) (see info box).

### Definition

## Actuarial corporate interest rate

The business model of SLT health insurance (operated using Similar to Life Techniques) is based on premium rates which must be reviewed annually to ascertain whether they are appropriate. This involves an examination of all the assumptions on which the premium calculation is based – in particular those relating to the development of the net return on investments. Insurers estimate this development and the safety margin, which must also be factored into these assumptions, on the basis of the actuarial corporate interest rate (ACIR) developed by the German Association of Actuaries (*Deutsche Aktuarvereinigung – DAV*). Insurers must report their ACIR to BaFin each year. This determines whether they are also required to lower the technical interest rate for existing tariffs if they are required to adjust their premiums.

The ACIR figures calculated in the 2018 financial year are below the maximum technical interest rate of 3.5% stipulated in the German Health Insurance Supervision Regulation (*Krankenversicherungsaufsichtsverordnung*) throughout the sector. As a result of the continuing low interest rate environment, the ACIR figures have again fallen in comparison with previous years. The relevant technical interest rates used for the purposes of premium rates will therefore have to be reduced further in most cases. The ACIR guideline contains a procedure for this purpose which allows the responsible actuary and the actuarial trustee involved in the premium adjustment to determine an appropriate and reliable technical interest rate for the particular entity under consideration.

Around half of the portfolio is affected by the premium adjustments for comprehensive health insurance pending in 2019. The average premium adjustment for the sector amounts to approximately 4.8%. The health insurers have used a total of approximately €1.6 billion of the provisions for bonuses to limit the increases in premiums.

## Judgement of the Federal Court of Justice on the invalidity of premium adjustments

The Federal Court of Justice (*Bundesgerichtshof – BGH*) decided in its judgement of 19 December 2018<sup>56</sup> that a premium adjustment for private health insurance made by an insurer with the consent of an “independent trustee” pursuant to section 203 (2) of the German Insurance Contract Act (*Versicherungsvertragsgesetz*) is not to be considered as invalid solely because the independence of the trustee may be denied.

According to the judgement, independence was a precondition only for the appointment of the trustee in accordance with the provisions of supervisory law, and not for the validity of the declaration made by the trustee after appointment. There was therefore no requirement for the civil courts to review the trustee’s independence separately in a legal dispute relating to a premium adjustment. To that extent, the supervisory authority alone had to ensure, on the basis of the powers granted to it by the legislation, that the insurance undertaking was entrusting the review of the premium calculation to an independent and professionally knowledgeable trustee; the policyholders’ interests were protected by the fact that, in a legal dispute relating to a premium increase before the civil courts, a wide-ranging substantive review of the propriety of the premium adjustment made is carried out.

The Federal Court of Justice further stated that, in particular, it would run counter to the purpose of the relevant provisions in section 12b (2), (2a) of the Insurance Supervision Act, old version, (or now section 155 of the Insurance Supervision Act), and section 203 (2) sentence 1 of the Insurance Contract Act if a premium adjustment were to fail solely due to a lack of independence of the responsible trustee despite the fact that the substantive preconditions had been met. This was because the primary objective of the provisions relating to premium adjustments was to guarantee that insurers were able to meet their obligations to pay insurance benefits over the long term. Accordingly, the provisions of section 12b (2), (2a) of the Insurance Supervision Act, old version, (now section 155 of the Insurance Supervision Act) not only give insurers the right to make a premium adjustment subject to the preconditions referred to in those provisions, but at the same time establish a corresponding obligation.

<sup>56</sup> Federal Court of Justice, judgement of 19 December 2018 (case ref. IV ZR 255/17) and BGH press release No. 194/2018.

On the basis of the comprehensive factual and legal review of the premium adjustment by the civil courts using the detailed, strict and mandatory substantive legal guidelines, the necessary effective legal protection for policyholders against premium adjustments made by the insurer was also guaranteed, without the need for them to be enabled for this purpose to conduct a separate review of the independence of the trustee and therefore of the supervisory preconditions for the appointment as trustee. The objective correctness of the trustee's consent to the premium adjustment is therefore incidentally reviewed at the same time.

## 2.6.3 Property and casualty insurers

### Business trends

Property and casualty insurers recorded a 2.9% year-on-year increase in gross premiums written in the direct insurance business in 2018 to €78.2 billion (previous year: €76.0 billion).

Gross expenditures for claims relating to the year under review rose by 2.9% to €25.1 billion (previous year: €24.4 billion). Gross expenditures for claims relating to prior years also rose by 6.4% to €20.1 billion. Provisions recognised for individual claims relating to the year under review amounted to €21.9 billion, compared with €21.1 billion in the previous year; provisions recognised for individual claims relating to prior years amounted in total to €66.3 billion, compared with €63.5 billion in the previous year.

### Motor vehicle insurance

With gross premiums written amounting to €28.4 billion, motor vehicle insurance was by far the largest insurance class. This represented growth of 3.3% over the previous year. As in the previous years, the increase is attributable both to a rise in the number of policies and to higher average premiums. Gross expenditures for claims relating to the year under review fell by 2.1% year on year, while gross expenditures for claims relating to previous years were up 10.7%. Gross provisions recognised for individual claims relating to the year under review remained at the prior-year level, while they increased by 2.2% for outstanding claims relating to 2017.

### General liability insurance

Property and casualty insurers collected premiums of €10.2 billion (+4.1%) for general liability insurance. Claims relating to the year under review remained unchanged in comparison with the previous year at €1.0 billion. Property and casualty insurers paid out €3.3 billion for claims relating to prior years (previous

year: €3.1 billion). Gross provisions for individual claims, which are particularly important in this insurance class, rose by 3.0% to €3.3 billion for outstanding claims relating to the year under review. Gross provisions for outstanding claims relating to prior years rose by 4.4% to €21.3 billion.

### Fire insurance

Insurers recorded gross fire insurance premiums written of €2.4 billion (+4.8%). Gross expenditures for claims relating to the year under review fell sharply by 23.1% to €607.3 million.

### Residential buildings and contents insurance

Insurers collected premiums for comprehensive residential buildings insurance and comprehensive contents insurance of €10.6 billion (+5.0%). Expenditures for claims relating to the year under review grew by 15.2% year on year. Gross provisions recognised for individual claims relating to the year under review increased by 14.1%. Expenditures for claims relating to previous years increased by 4.4%. Provisions for claims relating to previous years rose by 10.0%.

### Accident insurance

Premium income for general accident insurance amounted to €6.6 billion, or 1.5% higher than the prior-year level. Gross expenditures for claims relating to the year under review amounted to €438.9 million. An unchanged amount of €2.4 billion was reserved for outstanding claims relating to the year under review.

### Solvency I

The Solvency II supervisory system came into force on 1 January 2016. Solvency I now only applies to around 11% of property and casualty insurers which constitute small insurance undertakings within the meaning of section 211 of the Insurance Supervision Act.

At 410%, the solvency margin ratio for German property and casualty insurers subject to Solvency I at the end of 2017<sup>57</sup> was significantly higher than the previous year's figure of 349%. The reason for the increase was the smaller population of property and casualty insurers still falling within the scope of Solvency I.

### Solvency II

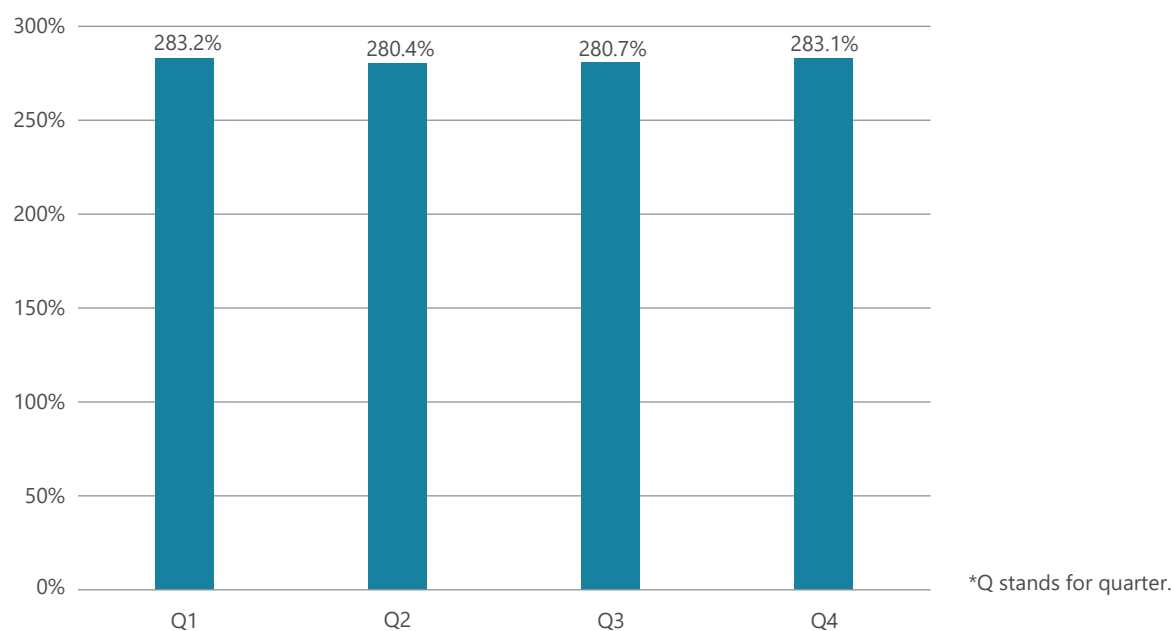
As at 31 December 2018, 89% of property and casualty insurers were subject to supervision in accordance with Solvency II. 92% of all property and casualty insurers

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<sup>57</sup> The disclosures relate to the 2017 financial year since projections are not prepared for property and casualty insurers.



**Figure 7: Development of SCR coverage ratios**



subject to reporting obligations under Solvency II used the standard formula to determine their solvency capital requirement (SCR). 7 insurance undertakings calculated the SCR on the basis of an internal model while 9 used a partial internal model. 9 insurers took up the statutory option of incorporating undertaking-specific parameters into the calculation of the SCR. Most of them were legal expenses insurers.

All property and casualty insurers were able to report adequate SCR coverage as at 31 December 2018. The SCR coverage ratio for the industry amounted to 283% (see Figure 7).

The SCR of the property and casualty insurers subject to interim reporting obligations for 2018 was €35.4 billion. The minimum capital requirement (MCR) for the industry as a whole amounted to €11.8 billion. The most important risk drivers by far for property and casualty insurance were market risk and underwriting risk for non-life insurance. These represented 61% and 53%, respectively, of the basic solvency capital requirement. Underwriting risk for health insurance (7%) and counterparty default risk (4%) were much less significant. The diversification effect reducing the capital requirements amounted to 26%, while the loss-absorbing effects of deferred taxes represented 20% of the basic solvency capital requirement.

Those German property and casualty insurers falling within the scope of Solvency II had eligible own funds for the purposes of SCR coverage amounting in total

to €100.1 billion as at 31 December 2018. Of total eligible own funds, around 96.2% were attributable to the highest category of own funds (Tier 1). The share of Tier 2 own funds was 3.4%. Tier 3 own funds accounted for a proportion of 0.4%. The property and casualty insurers report the majority of eligible own funds in the reconciliation reserve. As at 31 December 2018, this proportion was approximately 87% of basic own funds.

The relatively unchanged coverage ratio – in comparison with the life insurance sector, for example – mainly reflects the fact that property and casualty insurers do not issue long-term guarantees and that the average term of their investments is shorter. The undertakings are therefore considerably less sensitive and volatile in response to movements in the capital markets.

**Development of premiums, claims and earnings in property and casualty insurance**

With the aid of business intelligence software, BaFin is examining the development of premiums, claims experiences and earnings in property and casualty insurance more closely. This enables it to identify long-term trends and potential negative developments for the sector and individual undertakings. It also enables BaFin to take legal supervisory measures in good time, where necessary.

The open architecture means that the existing reporting system can be linked in to the new Solvency II reporting framework.

### Claims provisions (for selected property and casualty insurers)

Under the provisions of Solvency II, technical provisions in property and casualty insurance must be recognised at their transfer value. The latter is comprised of the best estimate and the risk margin. The transfer value has considerable significance for the determination of own funds and of the SCR. BaFin therefore considers it highly important to review its derivation from a risk-oriented point of view.

For this reason, it carried out closer checks in on-site inspections in 2018 on how the undertakings calculate their technical provisions and how they report them in the solvency statement. Among other tools, BaFin employed a specialised software programme for determining reserves, which was implemented in 2017.

## 2.6.4 Reinsurers

### Business trends

Claims expenditures for the reinsurers returned to expected levels in 2018 following the exceptionally high losses in 2017. Natural disasters are estimated to have caused total economic losses amounting to US\$160 billion worldwide in 2018. This amount was substantially lower than the previous year's figure of US\$350 billion and below the 10-year average of US\$190 billion.<sup>58</sup> Of the total economic losses from natural disasters in 2018, losses amounting to US\$80 billion were insured. This amount was also significantly lower than the prior-year figure of US\$140 billion. However, it exceeded the 10-year average (US\$61 billion) by around one-third.

Around US\$16.5 billion of the insured losses caused by natural disasters related to the Camp Fire forest fire in California. This represents the highest loss to date for the insurance industry caused by a forest fire. In addition to further forest fires, 2018 was also notable for hurricanes, of which hurricane Michael and typhoon Jebi caused the greatest losses. Storms David (Friederike) and Eleanor (Burglind) were responsible for a high level of losses for the insurance industry in Europe as well (around US\$3 billion). Germany accounted for around two-thirds of the losses.

The absence of unusually high losses in 2018 strengthened the reinsurers' resilience following the negative impact of the record losses in the previous year. No relief, however, came from the premium trend

in 2018: in the traditional reinsurance cycle, severe natural disasters are usually followed by substantial premium increases to compensate for high claims expenditures. In spite of the record losses, however, the latest figures do not seem to follow this cycle. Whereas some of the regions and classes of insurance with high claims expenditures saw two-digit premium increases, premiums in other markets and insurance classes remained fairly stable. Renewals in January 2019 also saw a continuation of the sideways trend in reinsurance prices from the point of view of the market as a whole.

The unusual trend in premiums that followed the record losses of 2017 is due to an oversupply of capacity. Neither reinsurers nor investors in the alternative reinsurance market reduced capacity; in fact, they stepped up the capacity they hold.

The alternative reinsurance market (ART market) is still interesting for investors, in spite of the record losses in 2017. Factors contributing to the popularity of the alternative reinsurance market are not only the relatively attractive yields, but also the comparatively low correlation between insurance risk and market risk. The market for catastrophe bonds (insurance-linked securities – ILS) recorded peak levels in 2018. In 2018, ILS amounting in total to US\$13.9 billion were issued (2017: US\$12.6 billion) – more than ever before. At US\$37.8 billion, the aggregate value of catastrophe bonds outstanding even set a new record.<sup>59</sup> According to the broker Aon Benfield, the ART market had a volume of approximately US\$98 billion as at the end of the second quarter of 2018 and made up around 16.2% of the entire reinsurance market.<sup>60</sup> Collateralised reinsurance accounted for the largest share, followed by ILS.

### Solvency II

Of the 33 German reinsurance undertakings subject to financial supervision by BaFin, 30 are required to comply with the Solvency II reporting obligations. They had own funds amounting to around €212.5 billion as at 31 December 2017 (previous year: €209.4 billion). At the same date, the solvency capital requirement amounted to €63.1 billion (prior year: €61.2 billion). This represented an average SCR coverage ratio of around 337% (previous year: 342%), slightly below the industry average (approximately 346%). The minimum capital requirement (MCR) coverage amounted to 985% on average at the reporting date (previous year: 981%).

<sup>58</sup> Munich Re: Press release 8 January 2019.

<sup>59</sup> ARTEMIS: Q4 2018 Catastrophe Bond & ILS Market Report.  
<sup>60</sup> Aon Benfield: Reinsurance Market Outlook September 2018.

The range of the coverage ratios within the reinsurance sector is considerable, especially with respect to the MCR. As at 31 December 2017, the reinsurers reported SCR coverage ratios between around 125% and 560%, and MCR coverage ratios between 122% and 2,240%. None of the reinsurance undertakings reported inadequate capital coverage as at 31 December 2017.

### Heterogeneous market

The wide range of the coverage ratios reflects the heterogeneous nature of the reinsurance sector. In addition to undertakings with regional and international operations, the sector also includes captive insurers, run-off platforms and some reinsurance undertakings that also perform the function of a holding company for an insurance group or a financial conglomerate. In such cases, the reinsurance activities are frequently subordinated to the holding company function and this is reflected, among other things, in more than adequate capital resources from the point of view of the reinsurance activities. Even though reinsurance undertakings represent only 8.5% of all insurers in terms of numbers, they nevertheless accounted for around 44.2% of the own funds of the entire insurance industry.

The own funds of the reinsurance undertakings fell slightly to an overall total of €211.8 billion as at the 31 December 2018 reporting date according to the quarterly reports submitted, while the solvency capital requirement increased slightly to €63.2 billion. The coverage ratio amounted to around 335%.

## 2.6.5 *Pensionskassen*

### Business trends

According to the projection as at the 2018 reporting date, premium income for the *Pensionskassen* recorded an overall decline in 2018 compared with the previous year. Premiums earned amounted in total to approximately €7.2 billion in the year under review, a small year-on-year decrease of around 0.8%. In 2017, they had risen by 6.1%.

Premium income for the stock corporations newly formed since 2002, which offer their benefits to all employers, fell by around 3.2% compared with the prior year to €2.5 billion.

In the case of the mutual insurance associations funded largely by employers, premium income rose by around 0.5% to approximately €4.8 billion.

### Investments

The aggregate investment portfolio of the *Pensionskassen* supervised by BaFin grew by 5.1% in 2018 to approximately €170.4 billion (previous year: €162.2 billion). The dominant investment types are still investment units, bearer bonds and other fixed-income securities, as well as registered bonds, notes receivable and loans.

The sector's hidden reserves declined to around €19.7 billion (previous year: €23.6 billion) according to preliminary figures. This corresponds to roughly 11.6% of the aggregate investments (previous year: 14.5%). The hidden liabilities are relatively insignificant at 0.8% overall.

### Projections and impact of the low interest rate environment

BaFin also prepared a projection for the *Pensionskassen* at the 30 September 2018 reporting date. It asked the undertakings to estimate their results for the financial year under four equity and interest rate scenarios. In view of the continuing low interest rate environment, the projection also covered the following four financial years, as in previous years. For those *Pensionskassen* with premium rates to which the German Premium Reserve Regulation (*Deckungsrückstellungsverordnung*) applies and which are required to build up a *Zinszusatzreserve*, the projection was further extended to cover the following 14 financial years.

As the analysis of the projections showed, the coverage ratio for the solvency capital requirement for the 2018 financial year was slightly below the prior-year level. As a general rule, the undertakings were therefore able to meet the solvency requirements, which are not based on Solvency II but on the provisions of the IORP II directive<sup>61</sup>. In BaFin's opinion, therefore, the sector's short-term risk-bearing capacity seems to be assured as before. Based on the projections, the overall net return on investment for the *Pensionskassen* was approximately 3.4% in 2018 (previous year: 4.1%).

The persistently low interest rates are also posing exceptional challenges for the *Pensionskassen*. The projections clearly show that the current return on investments is falling more rapidly than the average technical interest rate for the premium reserve. If it should be necessary for individual *Pensionskassen* to tighten their biometric actuarial assumptions or reduce the technical interest rate, it will become increasingly difficult for those

<sup>61</sup> Directive (EU) 2016/2341, OJ EU L 354/37.

*Pensionskassen* to finance the necessary increases in reserves from surpluses.

The *Pensionskassen* took action at an early stage to maintain their risk-bearing capacity. This can also be seen from the results of the 2018 projection: In many cases, the *Pensionskassen* have already recognised additional provisions.

BaFin therefore continues to monitor and support the *Pensionskassen* closely so that they can maintain and strengthen their risk-bearing capacity as far as possible even in the event of persistent low interest rates. *Pensionskassen* that have been hit particularly hard by the low interest rate environment receive more intensive supervision. This requires them to comply with additional regular reporting obligations. In some cases, the intensified supervision has already resulted in more active involvement by the employers and/or shareholders.

However, it is becoming clear that if the low interest rate environment persists, certain *Pensionskassen* will require additional funds. For *Pensionskassen* in the form of mutual insurance associations, it would be appropriate for their sponsoring undertakings to make funds available. *Pensionskassen* in the form of stock corporations would turn to their shareholders.

If an employer appoints a *Pensionskasse* to be responsible for occupational retirement provision for its employees, the employer is obliged to pay the benefits to the employees itself in the worst case, in accordance with its subsidiary liability under the German Occupational Pensions Act (*Betriebsrentengesetz*). This gives the beneficiaries and pensioners additional security. In addition, *Pensionskassen* with the legal form of stock corporations generally belong to the guarantee scheme for the life insurers.

### **Solvency**

According to the projection as at the 2018 reporting date, the solvency margin ratio in accordance with the German Capital Resources Regulation (*Kapitalausstattungs-Verordnung*) applicable to the *Pensionskassen* was an average of 132%, slightly below the level in the previous year. According to the estimates, four *Pensionskassen* were unable to comply with the solvency requirements as at 31 December 2018. In these circumstances, the undertakings are required to submit a recovery and/or financing plan under the provisions of the Insurance Supervision Act.

## **2.6.6 Pensionsfonds**

### **Business trends**

The *Pensionsfonds* recorded gross premium income totalling €10.2 billion in 2018, compared with €2.4 billion in the previous year. The fluctuations in premium income are attributable in particular to the fact that, in the case of *Pensionsfonds*, the premiums are often paid as a single premium, depending on the type of commitment agreed.

The total number of beneficiaries rose in the year under review to 1,058,215 persons compared with 942,782 persons in the previous year. Of those, 626,094 were vested employees who were members of defined contribution pension plans, while 60,525 vested employees were members of defined benefit pension plans. The benefit payouts of €1,907 million (previous year: €1,877 million) related to 373,134 persons drawing benefits.

### **Investments**

Investments for the account and at the risk of *Pensionsfonds* grew from €2,690 million to €2,917 million in the year under review. This corresponds to an increase in investments of 8.4% (previous year: 10%). The largest share of the portfolio amounting to 52% consisted of contracts with life insurance undertakings.

As at 31 December 2018, net unrealised gains in the investments made by *Pensionsfonds* amounted in total to €131.9 million (previous year: €139.5 million).

Assets administered for the account and at the risk of employees and employers grew only slightly in the year under review, from €34.2 billion in the previous year to €40.8 billion. Roughly 91% of these investments, which are measured in accordance with section 341 (4) of the German Commercial Code (*Handelsgesetzbuch*) at current market value, consisted of investment units.

### **Projections and impact of the low interest rate environment**

BaFin prepared projections in 2018 for 31 *Pensionsfonds* (see info box on page 125). The particular focus of the projections was the expected profit for the year, the expected solvency and the expected valuation reserves at the end of the current financial year.

The assessment of the projections indicated that the 31 *Pensionsfonds* included would be able to withstand the four defined scenarios financially. The technical provisions for the account and at the risk of employees and employers are generally recognised retrospectively

in accordance with the assets administered for the account and at the risk of employees and employers. If this process indicates that the amount of the investments falls short of a minimum premium reserve which may be calculated on a prospective basis, the difference must be made up by supplementary contributions from the employer. This means that balance-sheet cover for these technical provisions is guaranteed at all times. The projections showed that with no change in the capital market situation supplementary contributions would have become due as at 31 December 2018 for one *Pensionsfonds*. The obligations recognised by the *Pensionsfonds* in their financial statements are to a large extent not guaranteed by the *Pensionsfonds*, and the guarantees are covered by congruent reinsurance in some cases.

#### At a glance

### Projections for *Pensionsfonds*

The scenarios defined by BaFin for the projections for the *Pensionsfonds* were the capital market situation at the 30 September 2018 reference date and a negative equity scenario with a 27% drop in prices. In addition, BaFin required scenarios to be calculated that combined each of the two above-mentioned scenarios with a 100 basis point increase in the yield curve.

Nevertheless, BaFin also considers it necessary to address the potential medium- and long-term ramifications for the *Pensionsfonds* of a low interest rate phase that persists even longer. As part of the projection exercise, the *Pensionsfonds* were therefore once again also asked to estimate the expenses for the *Zinszusatzreserve* for the current financial year and for the following four financial years. In addition, they had to indicate whether they expected to be able to cover these expenses with corresponding income, and whether they would be able to comply with the solvency requirements under the German Regulation on the Supervision of *Pensionsfonds* (*Pensionsfonds-Aufsichtsverordnung*) in the future as well. Of the 21 *Pensionsfonds* which operate insurance-based business, 18 have so far been required to establish a *Zinszusatzreserve*. These 18 *Pensionsfonds* are currently financed through congruent reinsurance cover, or through current income or surpluses.

### Solvency

According to the preliminary figures, all of the *Pensionsfonds* had sufficient own funds. They therefore complied with BaFin's solvency requirements. For around two-thirds of the *Pensionsfonds*, the level of own funds required by supervisory law was equal to the minimum capital requirement of €3 million for stock corporations and €2.25 million for mutual *Pensionsfonds*. The individual solvency capital requirement for these *Pensionsfonds* is below the minimum capital requirement. This is due either to the relatively low volume of business or the type of business concerned.

# VI

## Supervision of securities trading and the investment business



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# 1 Bases of supervision

## 1.1 MiFID II and MiFIR – one year on

The national competent authorities in the European Union (EU) and the European Securities and Markets Authority (ESMA) have made great strides in implementing transparency in the secondary markets since the second Markets in Financial Instruments Directive (MiFID II)<sup>1</sup> and the Markets in Financial Instruments Regulation (MiFIR)<sup>2</sup> entered into force on 3 January 2018.<sup>3</sup> The trading venues have also contributed to this development.

Tighter regulation of trading systems and greater trading transparency are two key measures that European legislators introduced in response to the developments that followed after the first Markets in Financial Instruments Directive of 2004. The many different ways of trading are no longer limited to regulated markets and multilateral trading facilities. Instruments that were previously traded over the counter are now also traded via organised trading facilities and proprietary traders.

The fact that these execute considerable OTC trading volumes with their clients turns them into systematic internalisers (SIs).

Pre- and post-trade transparency requirements apply to all existing and new trading venues. In pre-trading, all trading venues have to publish bid and offer prices as well as the depth of trading interests. The European Supervisory Authorities waived these requirements in certain cases, for example for orders that are large in scale (LIS) compared with normal market size and in cases where the trading system determines the price of the financial instrument by reference to another market. In the latter case, however, trading in the financial instrument under this waiver at the specific trading venue must not exceed 4% of the total volume of trading in that financial instrument on all trading venues across the European Union, and trading under waivers in the EU must not be above 8% of the trading volume (double volume cap mechanism). Most recently, waivers for 342 financial instruments were suspended in the EU on this basis.<sup>4</sup>

1 Markets in Financial Instruments Directive. Directive 2014/65/EU, OJ EU L 173/349.

2 Markets in Financial Instruments Regulation. Regulation (EU) No 600/2014, OJ EU L 173/84.

3 For information on MiFID II, see also chapter II 2.1.

4 The respective lists are prepared by ESMA. The national competent stock exchange supervisory authorities then determine whether a relevant waiver has been granted and whether any instruments are covered by it. Since the expiry of the XETRA BEST waiver at the end of 2018, this has no longer applied to Germany.

### Robust data

The necessary calculations can only be performed on the basis of robust data. The Financial Instruments Reference Data System (FIRDS) contains all the key information on financial instruments traded at EU trading venues. The supervisory authorities are continuously improving the data basis, for example in relation to the Legal Entity Identifier (LEI). FIRDS is the underlying basis for other databases, which are required for calculating the double volume cap mechanism and the liquidity status of financial instruments as a basis for determining the SIs' quoting obligations. The data completeness indicators that ESMA has published for contributing trading venues are another sign of the progress made with data quality.

It is not yet possible to assess these regulations and their impact in any comprehensive way, because there is no consolidated tape provider (CTP) yet, and this makes it difficult to keep an overview of the data. Also, the first SI threshold calculation was only performed a few months ago and only covered some of the relevant asset classes.

### Supervisory measures implemented

ESMA and the national competent authorities made some urgent corrections immediately after 3 January 2018. They included removing serious drawbacks of the EU tick size regime for EU trading venues, which affected financial instruments from third countries and SIs. The tick size is the minimum price change that has to be taken into account when submitting orders or quotes in trading shares, certificates representing shares and exchange-traded funds (ETFs). The tick size depends on the order price and – except for ETFs – on the liquidity. The introduction of MiFID II/MiFIR led to considerable liquidity outflows from EU trading venues to trading venues in third countries and SIs.

In an effort to overcome the problem of SIs, BaFin communicated with stock exchanges, associations and financial services providers and shared its insights with ESMA. The outcome is a proposal to amend the Delegated Regulation<sup>5</sup> concerned. Although the European Commission has accepted the proposal, the legislative process has not yet been concluded. The amendment will have the effect of giving SIs virtually full equivalence with trading venues.

The disadvantages of trading in third-country financial instruments have been remedied on the basis of

individual measures adopted by the German stock exchange supervisory authorities – coordinated by BaFin throughout the EU as well as with ESMA – and by amending the Delegated Regulation<sup>6</sup> concerned. However, the amended version has not yet entered into effect. In future, the stock exchange supervisory authority responsible for a third-country financial instrument will be able to include the liquidity in that instrument's home market in the calculation of the liquidity band appropriate for the tick size.

### Problems identified and action taken

BaFin responds to and analyses complaints<sup>7</sup> it receives from the market on an ongoing basis and, if necessary, coordinates its response with ESMA and other supervisory authorities in the EU. Currently, BaFin, together with ESMA, is examining periodic auction models (frequent batch auctions) and market data costs. ESMA is conducting market surveys on these issues.

With regard to complaints about sharp rises in market data costs, which the trading venues primarily blame on the need to implement the requirements of MiFID II, it is not yet clear what measures, if any, the supervisory authorities in the respective countries can take. The different EU trading venues have very disparate pricing models, which means that the potential for comparison is limited. What is more, the definition of indefinite legal concepts, such as that of a "reasonable commercial basis", which market participants are calling for, has a direct impact on pricing. Any supervisory measures to be taken must therefore be carefully weighed from a legal and economic perspective and agreed on an EU-wide basis.

New periodic auction models (frequent batch auctions) are also being examined to determine whether they are compatible with the transparency requirements of MiFID II. ESMA has launched a call for evidence to establish current market practice in this area. Using this measure, ESMA is planning to analyse the different systems in use in the market and develop a robust distinction between the models used as standard in the market and new models, which may not be permissible.

## 1.2 Initial experience with the Market Abuse Regulation

Since the MAR entered into force, transparency requirements, such as for ad hoc disclosures and

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5 Delegated Regulation (EU) 2017/587, OJ EU L 87/387.

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6 Delegated Regulation (EU) 2017/588, OJ EU L 87/411.

7 See chapter II 2.4.



managers' transactions, apply not only to issuers whose financial instruments are admitted to trading on a regulated market, but also to issuers whose financial instruments are traded on multilateral trading facilities (MTFs) and organised trading facilities (OTFs). For managers' transactions, the transparency requirements of the MAR apply not only to an expanded group of issuers affected, but also to an enlarged catalogue of transaction types and financial instruments to be notified. As a result, notification requirements apply not only to sales and purchases, but also to donations, for example. The expanded transparency requirements led to a significant increase in the number of corresponding notifications in 2018 (3,260) compared with 1,809 notifications in 2015 – the last year before the MAR entered into force.

#### Definition

### Market Abuse Regulation

As from July 2016, the main provisions on market integrity and transparency are no longer contained in the German Securities Trading Act (*Wertpapierhandelsgesetz – WpHG*). In its place, the Market Abuse Regulation (MAR)<sup>8</sup>, which is directly applicable, determines which activities fall within the scope of illegal insider trading and market manipulation. At the same time, the MAR contains provisions on accompanying transparency requirements, such as ad hoc disclosures, insider lists and managers' transactions.

However, the new legal situation also gave rise to uncertainty in the capital market, as is demonstrated by the large number of queries about interpretive issues received by BaFin. For this reason, BaFin organised workshops with the issuers affected and published questions and answers (Q&As) on ad hoc disclosures, insider lists and managers' transactions.

In addition, another update of BaFin's Issuer Guideline is planned for 2019. The guideline is intended for domestic and foreign issuers whose securities are admitted to trading on a domestic stock exchange or that have consented to trading on an MTF. It is to provide practical guidance and explain BaFin's administrative practice. Through this wide range of information on offer,

BaFin aims to contribute to preventing the new laws from being a hurdle for issuers and to counteract any problems of comprehension. However, BaFin continues to be available for queries.

As a result of the MAR entering into force, the obligation on market participants to prevent and uncover market abuse, i.e. insider trading and market manipulation, has also increased considerably. All market participants brokering or executing transactions on a commercial basis are required to investigate trading activities using effective systems. Moreover, they are required to scrutinise transactions for irregularities that may indicate market abuse offences and to report any orders or transactions they have identified as suspicious. The same rules apply to market operators as well as investment firms operating a trading venue.

### Sharp increase in the number of suspicious transaction reports

These changes were the reason for a significant increase in the number of suspicious transaction reports, from 547 reports in 2015, before the MAR entered into force, to 3,104 in 2018. BaFin pursues a risk-based approach in investigating these reports, focusing on incidents that, for example, indicate systematic violations of prohibitions or violations with a pronounced impact on market integrity.

The MAR and the provisions of the Market Abuse Directive (MAD)<sup>9</sup>, which was transposed into national law alongside it, have added to the range of options for sanctioning prohibited activities that constitute de facto market abuse. For example, attempted market manipulation can now also be pursued as a criminal offence. At the same time, the maximum fines that can be imposed for acts of market abuse constituting an administrative offence have increased significantly. BaFin can also base the amounts of administrative fines imposed on legal persons on their revenue. BaFin provides details of how it makes use of the sanctions available and how it calculates administrative fines in its WpHG Administrative Fine Guidelines II<sup>10</sup>. BaFin publishes on its website decisions on any measures and sanctions it imposes in response to violations of market abuse regulations (naming and shaming) in compliance with the requirements of the MAR.

<sup>8</sup> Regulation (EU) No 596/2014, OJ EU L 173/1.

<sup>9</sup> Directive 2014/57/EU, OJ EU 2014 L 173/179.

<sup>10</sup> For information on sanctions, see also chapter II 4.

## 1.3 Central counterparties

The Committee on Payments and Market Infrastructures (CPMI) and the International Organization of Securities Commissions (IOSCO) re-assessed their report on central counterparties (CCPs) in 2018. The original 2016 report had identified gaps and implementation errors in the recovery planning, credit risk management and liquidity risk management of 10 CCPs included in the survey. In addition to the 10 CCPs from the initial assessment, the follow-up looked into 9 other CCPs. The results of the assessment were published in May 2018.

### Problems persist

As far as the participants in the 2016 survey are concerned, the report concludes that, although they have made significant progress in closing the gaps identified, some participants still seem to have problems in introducing and implementing specific rules and standards set out in the Principles for Financial Market Infrastructures (PFMI)<sup>11</sup>.

CPMI and IOSCO therefore called on the national competent authorities (NCAs) to closely investigate these concerns. The NCAs are also expected to encourage the CCPs under their supervision to take the steps required to comply with the Principles to the full extent. In this context, CPMI and IOSCO pointed specifically to the guide published in July 2017<sup>12</sup> on resilience of central counterparties and their revised recovery report<sup>13</sup>. The standards described there should be applied by the relevant CCPs and adequately taken into account in optimising their practices. BaFin has initiated a review to verify whether the CPMI and IOSCO Principles are being complied with.

## 1.4 Supervisory convergence

Since 2016, the practical work undertaken by the three European Supervisory Authorities (ESAs) has focused on promoting supervisory convergence as much as possible. The aim is to get the national competent authorities to interpret and apply the law uniformly. To this end, ESMA, the European Banking Authority (EBA), the European Insurance and Occupational Pensions Authority (EIOPA) and the NCAs have jointly been working on the development of convergence tools.

Guidelines and Q&As are the most familiar convergence tools. BaFin applies almost all the guidelines and Q&As, thus meeting the expectations of ESMA, the EBA and EIOPA. The convergence measures that BaFin does not apply or applies only in part are listed on its website<sup>14</sup>.

Supervisory convergence has a number of advantages: for example, it lowers the risk of supervisory arbitrage and promotes a level playing field in Europe and thus consistent supervision in the European market. Initially, convergence tools are not generally legally binding on market participants, but they become indirectly applicable as soon as BaFin adopts them into its supervisory practice.

To help market participants, BaFin provides non-binding translations of selected Q&As and organises regular workshops. In addition, it welcomes queries from the industry at any time.

# 2 Supervision in practice

## 2.1 Monitoring of market transparency and market integrity

### 2.1.1 Market abuse analysis

In the year under review, BaFin concluded 353 analyses into market abuse (previous year: 811 market abuse analyses; see Figure 8 “Market abuse analyses” on page 131). BaFin found indications of market abuse in 65 cases, of which 32 related to market manipulation and 33 to insider trading. In the previous year, a total of 241 cases related to market abuse.

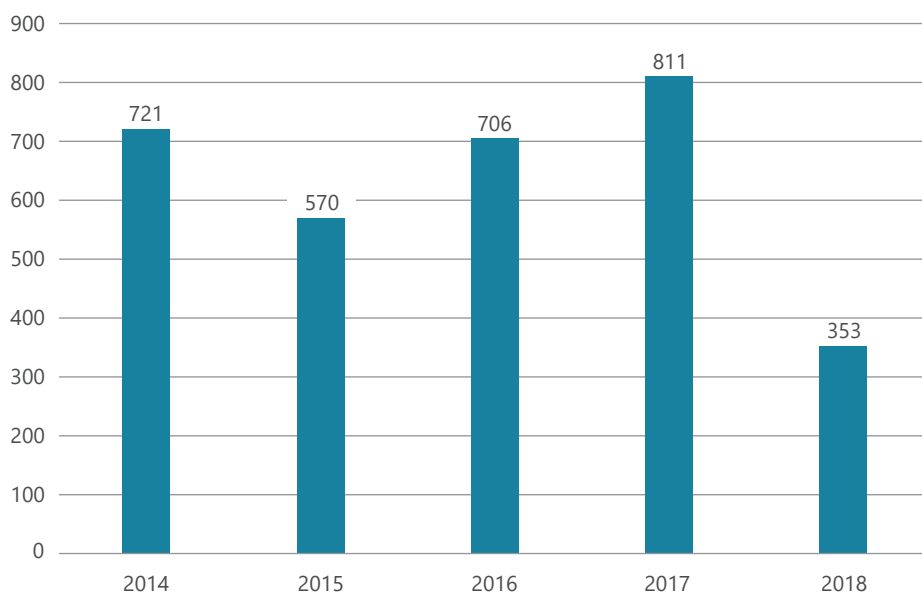
Thus, both the total number of analyses concluded and the number of cases where BaFin found indications of market abuse declined significantly. This is attributable to the fact that BaFin revised its risk-based approach for investigating possible incidents of market abuse. Thanks to these improvements, it can resolve cases faster if there is clear evidence of market abuse or if they are relevant to the functioning, stability and integrity of the financial market and – if necessary – hand them over promptly to the prosecuting authorities. BaFin processes such cases with utmost priority.

<sup>11</sup> See BaFinJournal September 2016, [www.bafin.de/dok/8346586](http://www.bafin.de/dok/8346586).

<sup>12</sup> BIS, 2017, Resilience of Central Counterparties (CCPs): further guidance on the PFMI.

<sup>13</sup> BIS, 2014, Recovery of financial market infrastructures.

<sup>14</sup> [www.bafin.de/dok/10691024](http://www.bafin.de/dok/10691024).

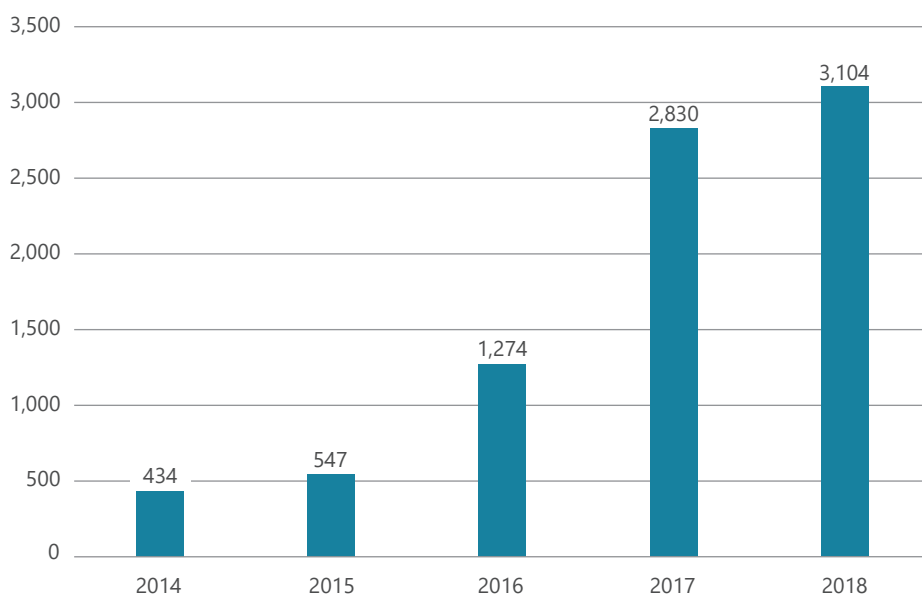
**Figure 8: Market abuse analyses**

However, since many of the non-urgent cases had thus far to be processed faster and therefore in larger numbers, the change in the approach has resulted in a significant drop in the number of analyses conducted in 2018. But this decline is offset by the fact that the new risk-based approach makes it possible to focus with greater intensity on pursuing significant cases of market abuse.

Most of the analyses were again triggered by suspicious transaction and order reports. The rising trend in the

number of such reports, which has continued since the new provisions of the MAR entered into force, persisted in 2018 (see Figure 9 "Suspicious transaction and order reports"). BaFin received 3,104 reports (previous year: 2,830 reports) from a total of 228 different parties subject to reporting requirements.

A total of 2,404 reports related to alleged market manipulation. Most cases involved trade-based manipulation, including pre-arranged trades and wash sales, where the buyer and seller are the same person.

**Figure 9: Suspicious transaction and order reports**

In 688 cases, the report related to insider trading. BaFin received 11 reports about potential violations of both the prohibition on insider trading and of that on market manipulation.

68%, and thus the vast majority of reports, related to market abuse involving equities, 17% affected warrants and certificates, 8% were attributable to bonds and 4% to fund units. The reports related to a total of 1,459 different financial instruments (previous year: 1,786 financial instruments).

In the year under review, BaFin published 5 consumer warnings (previous year: 7 consumer warnings) on its website, warning private market participants of concerted market manipulation attempts – such as through calls and spam e-mails.

### 2.1.1.1 Market manipulation analyses

Most of the positive market manipulation analyses – 17 cases – related to information-based market manipulation (previous year: 24 cases; see Figure 10 “Subject matter of positive market manipulation analyses”). These include incorrect, misleading or withheld information as well as manipulation in the form

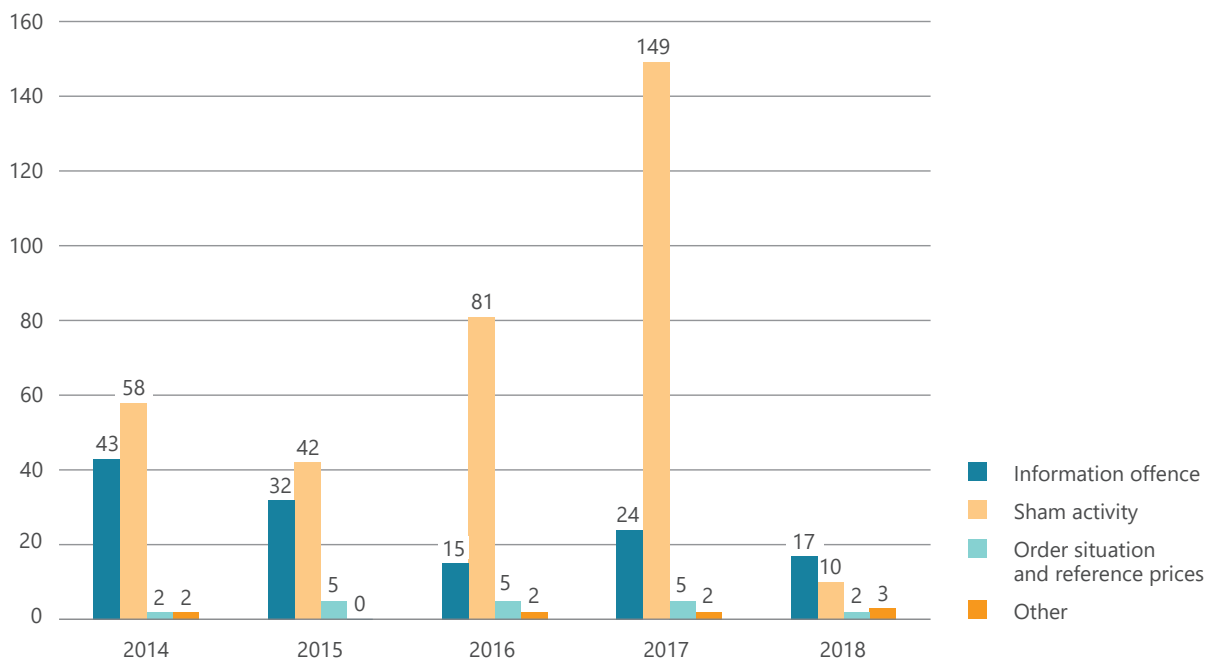
of scalping. The number of positive market manipulation analyses dealing with sham activities such as wash sales and pre-arranged trades fell sharply, from 149 cases in 2017 to 10 cases in 2018. BaFin attributes this decline to its adjusted risk-based approach in case handling.

Broken down by stock exchange segment, the proportion of cases of alleged market manipulation identified on the regulated unofficial market (*Freiverkehr*) was 72%, almost unchanged from the previous year (69%). Analyses relating to cases of market manipulation on the regulated market accounted for 28% (previous year: 31%).

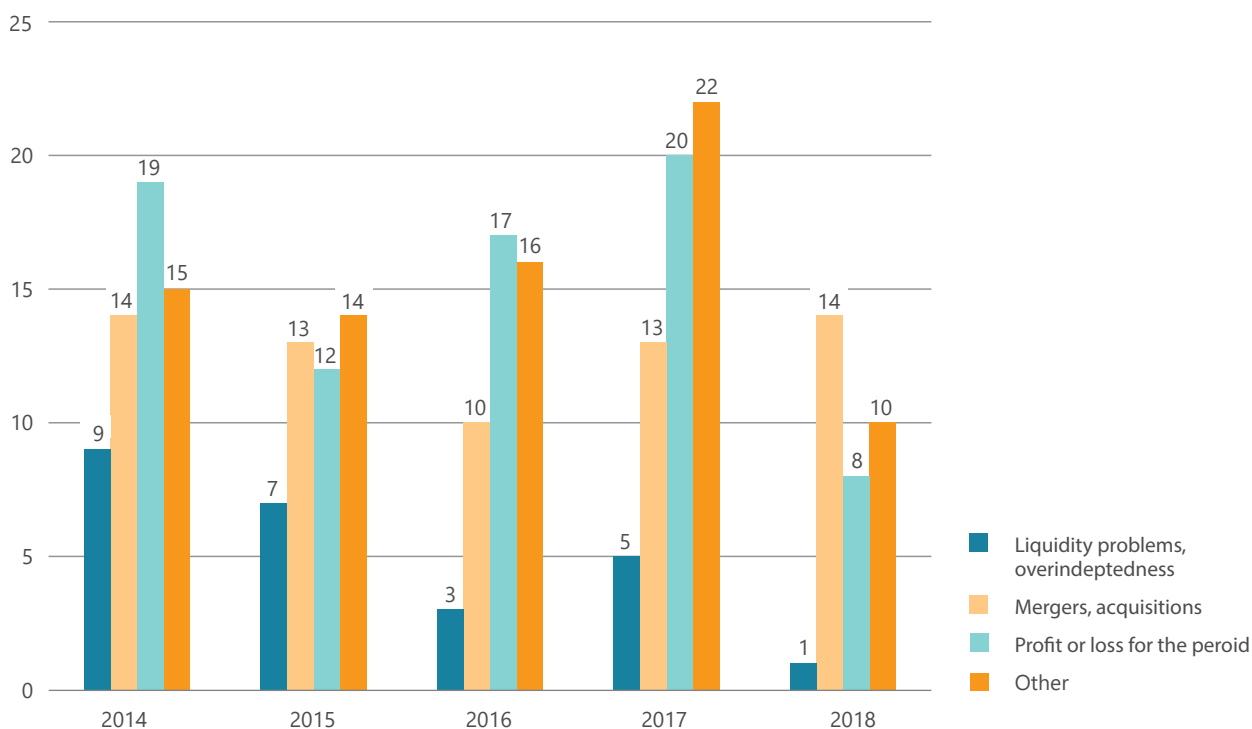
### 2.1.1.2 Insider trading analyses

The main focus of positive insider trading analyses – 14 cases – was on issues relating to mergers and acquisitions (previous year: 13 cases; see Figure 11 “Subject matter of positive insider trading analyses” on page 133). 8 cases were recorded in connection with companies’ earnings figures (previous year: 20 cases). As in previous years, most alleged insider trading took place on the regulated market (64%; previous year: 72%). The remaining cases (36%; previous year: 28%) related to the regulated unofficial market.

**Figure 10: Subject matter of positive market manipulation analyses**



**Figure 11: Subject matter of positive insider trading analyses**



## 2.1.2 Market manipulation

### Latest developments

The number of new investigations launched in 2018 decreased by 35% compared with the previous year. The reason for the decrease is not that BaFin received fewer suspicious transaction and order reports, but rather its processing using a risk-based approach. This enabled BaFin initially to postpone dealing with 400 individual reports, most of which related to the trading surveillance offices of stock exchanges, in

favour of cases with greater priority. Table 26 “Market manipulation investigations” shows the investigations launched at a glance. The number of proceedings completed in 2018 can be found in Table 27 “Completed market manipulation proceedings” on page 134.

### International cooperation

In 2018, BaFin again worked together with foreign supervisory authorities on many investigations. The exchange of information and administrative assistance between the supervisory authorities

**Table 26: Market manipulation investigations**

Period	New investigations	Investigations discontinued	Investigation results				Total (cases)	Ongoing investigations Total
			Investigations referred to public prosecutors’ offices or BaFin Administrative Fines Division					
			Public prosecutors’ offices		Administrative Fines Division*			
			Cases	Individuals	Cases	Individuals		
2016	272	40	106	275	7	9	<b>113</b>	<b>398</b>
2017	226	56	121	197	6	7	<b>127</b>	<b>441</b>
2018	149	84	77	124	4	4	<b>81</b>	<b>277</b>

\* The difference between the number of referrals to the BaFin Administrative Fines Division and the number of administrative fine proceedings initiated by BaFin (see 2.6.1) is attributable to the use of different processes.

**Table 27: Completed market manipulation proceedings**

Period	Total	Decisions by the public prosecutors' offices*					
		Investigations discontinued				Proceedings discontinued in accordance with section 153a of the Code of Criminal Procedure	Public main proceedings not commenced in accordance with section 204 of the Code of Criminal Procedure
		Proceedings discontinued in accordance with sections 152 (2) and 170 (2) of the Code of Criminal Procedure	Proceedings discontinued in accordance with section 153 of the Code of Criminal Procedure	Proceedings discontinued in accordance with sections 154, 154a of the Code of Criminal Procedure	Proceedings discontinued in accordance with section 154f of the Code of Criminal Procedure		
2016	345	166	49	28	17	50	0
2017	407	187	71	30	24	56	5
2018	268	138	31	16	14	43	5

Period	Final court judgements following criminal proceedings*				Rulings following administrative fine proceedings	
	Proceedings discontinued by the court in accordance with section 153a of the Code of Criminal Procedure	Convictions following summary proceedings without trial	Convictions following full trial	Acquittals	Investigations discontinued	Final administrative fines
2016	6	13	10	3	3	0
2017	5	15	4	0	3	7
2018	0	6	7	3	3	7

\* The figures relate to decisions from previous years, but BaFin only came to know about them in the years specified in the left table column.

of the EU member states was harmonised in 2018 by Implementing Regulation (EU) 2018/292 on market abuse, which governs the practical aspects of information exchange, using standardised forms, for example.

In a total of 75 cases (previous year: 95 cases), BaFin requested administrative assistance from supervisory authorities in 22 countries (previous year: 27 countries; see Table 28 "Requests for international administrative assistance"). In return, BaFin received 31 requests for administrative assistance from a total of 12 countries in the year under review. This compares with 44 requests for administrative assistance from 13 countries in 2017, which means that the number of requests for administrative assistance decreased by approximately 30% in 2018.

BaFin primarily exchanged information with supervisory authorities from other EU member states, such as France, the United Kingdom and Austria. Among non-EU countries, BaFin received support for its investigations into market manipulation from Canada and Switzerland.

**Table 28: Requests for international administrative assistance regarding market manipulation**

Period	Requests made	Requests received	Total
2017	95 (to 27 countries)	44 (from 13 countries)	139
2018	75 (to 22 countries)	31 (from 12 countries)	106

Information was often exchanged with other authorities in connection with the dissemination of recommendations or reports on the shares of smaller companies. Especially “pump and dump” schemes are often found to have originated in foreign countries. Since the cross-border exchange of information is essential in these cases, especially to ensure a thorough investigation, BaFin greatly values the cooperation with the supervisory authorities of other countries.

### Selected priority areas for the investigations

#### Short attacks

A phenomenon that the media often refer to as “short attacks” affected German stocks especially in 2016 and 2017 (see info box “Short attacks”). These kinds of attacks were the subject of a large number of investigations conducted by BaFin in 2018. BaFin had to determine whether these activities were violations of the prohibition on market manipulation.

#### At a glance

### Short attacks

A feature typical of short attacks is that individual investors benefit from falling share prices. As the name suggests, short attacks are associated with short selling: borrowed shares are sold and subsequently – as soon as the share price has fallen – bought back at a lower price. The fall in the price of the shares concerned is triggered by negative comments about the issuer, which are published around the time of the short sales. In many cases, these kinds of reports – even though most of them come from unknown individuals or analysis firms – create huge uncertainty among investors.

BaFin has provided information on the phenomenon of short attacks on several occasions in the past and advised investors to examine very carefully how trustworthy the disseminated reports really are before selling or acquiring financial instruments. Alternative reliable sources should always be consulted before making an investment decision. All the more reason for issuers to bear in mind that maximum transparency and good capital market communication – and the prompt correction of negative reports – reduce the risk of falling prey to such attacks. Overall, Germany saw a decline in the number of these types of short attacks in 2018.

#### Wirecard AG

As a result of a criminal complaint filed by BaFin because of information-based market manipulation, it is expected that, for the first time, a perpetrator of such short attacks will be punished. The competent public prosecutor’s office submitted an application to the Local Court of Munich to prosecute the individual responsible for a negative report on Wirecard AG, which had been published during such a short attack, and requested a fine of €36,000. The prosecutor’s office considered it proven that parts of the report had been incorrect and incomplete and therefore misleading. It held that the individual responsible had deliberately launched the dissemination of the misleading information as a way to make the share price crash. Publication of the report had led to a slump in the issuer’s share price by over 20%. A penalty order has not yet been issued.

#### Market manipulation and social networks

New channels of communication also bring new areas of work for BaFin: where in the past false or misleading information was mostly disseminated through channels such as the phone or e-mail, recently media such as Twitter, Facebook and other social networks have also been involved. Manipulators use social networks, for example to publish links to primary sources, or they disseminate false or misleading information directly. Information spread via social networks typically reaches a larger group of recipients than phone calls or e-mails. The reach may subsequently increase further, if the traditional media, such as news agencies, pick up on the false or misleading information and disseminate it further. BaFin is currently investigating the first cases of this new type of digital market manipulation.

### 2.1.3 Insider trading

#### Latest developments

BaFin launched 71 new insider trading investigations in 2018. This marks another slight increase in the number of these investigations compared with the previous year (62 investigations). This is mainly because the trading surveillance offices of stock exchanges involved BaFin more often in 2018, and BaFin responded each time by promptly launching an investigation. For a total of 32 of the new investigations launched, the trigger was (or included) such a referral by a trading surveillance office. In contrast, the number of investigations launched purely in response to a preceding insider trading analysis declined from 60 (2017) to 31 (2018). The remaining investigations were prompted by requests from prosecuting authorities and stock exchange supervisory authorities.

**Table 29: Insider trading investigations**

Period	New investigations	Investigations discontinued	Investigation results					Ongoing investigations
			Investigations referred to public prosecutors' offices or BaFin Administrative Fines Division					
			Public prosecutors' offices		Administrative Fines Division		Total (cases)	
Cases	Individuals	Cases	Individuals	Total				
2016	42	23	21	49			21	39
2017	62	11	18	40			18	72
2018	71	48	19	63	1	4	20	75

**Table 30: Completed insider trading proceedings**

Period	Total	Investigations discontinued	Investigations discontinued as part of out-of-court settlements	Final court judgements			
				Court judgements	Convictions following summary proceedings without trial	Convictions following full trial	Acquittals
2016	93	75	14	3	1	0	0
2017	41	27	5	5	4	0	0
2018	45	42	2	0	1	0	0

Table 29 „Insider trading investigations“ and Table 30 „Completed insider trading investigations“ show the results of investigations launched and proceedings completed in 2018.

#### International administrative assistance

International administrative assistance is also an indispensable tool in insider trading surveillance. In 2018, BaFin requested administrative assistance from supervisory authorities based in 16 different countries in a total of 38 cases (previous year: 79 cases; see Table 31 “Requests for international administrative assistance”). It cooperated most frequently with the United Kingdom, Switzerland and France. Administrative assistance was requested from BaFin in 18 cases, with most of the requests coming from Austria. In the previous year, there were 28 requests for administrative assistance.

**Table 31: Requests for international administrative assistance in insider trading surveillance**

Period	Requests made	Requests received	Total
2017	79 (to 22 countries)	28 (from 15 countries)	107
2018	38 (to 16 countries)	18 (from 10 countries)	57

#### 2.1.4 Ad hoc disclosures and managers' transactions

##### 2.1.4.1 Ad hoc disclosures

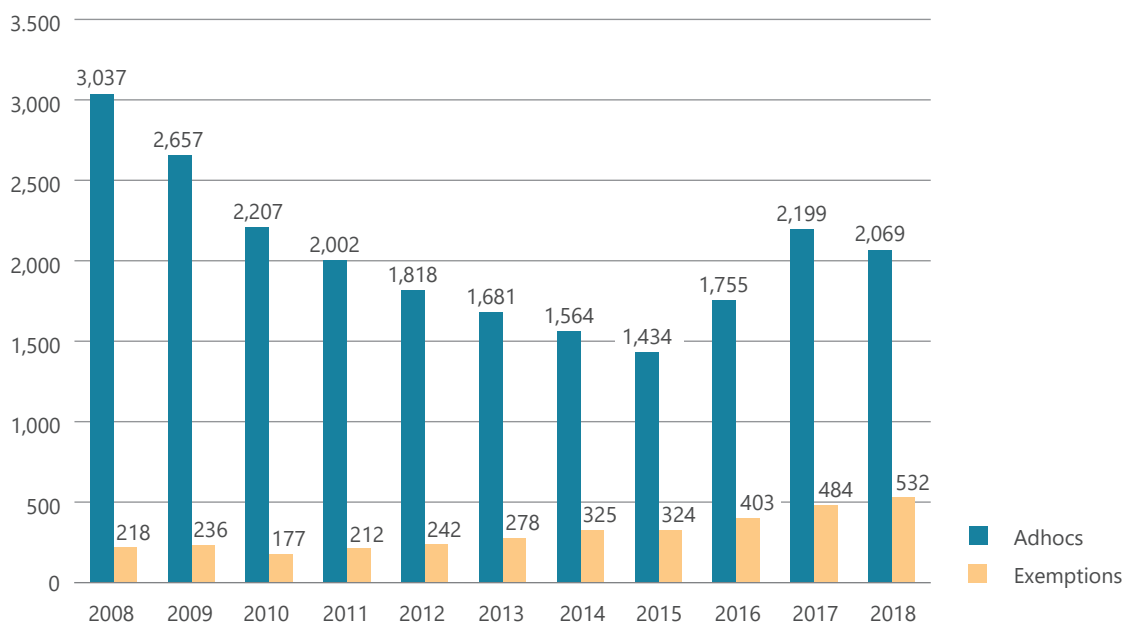
In the year under review, issuers published a total of 2,069 ad hoc disclosures (previous year: 2,197 ad hoc disclosures; see Figure 12 “Ad hoc disclosures and exemptions” on page 137). In addition, BaFin received 532 self-exemption notifications (previous year: 484 self-exemption notifications). Although there was a moderate decline in the number of ad hoc disclosures compared with the previous year, the number of self-exemptions continued to increase. This is probably due to greater awareness of the significance of intermediate steps. This is because intermediate steps in a protracted process may also be deemed to be inside information, if by themselves they satisfy the criteria of inside information as set out in Article 7(3) of the Market Abuse Regulation (MAR).

#### New publication requirements as a result of the MAR

Since 3 January 2018, Article 17(1) of the MAR has also required issuers whose securities are listed, with their consent or approval, on an organised trading facility (OTF) to publish as soon as possible any inside information that directly concerns those issuers. Another



**Figure 12: Ad hoc disclosures and exemptions**



new requirement is that emission allowance market participants have to publish inside information. As specified in Article 17(2) of the MAR, they, too, have had to disclose information on emission allowances they hold in respect of their business since 3 January 2018. This relates primarily to relevant technical information, but also to investment decisions. With regard to installations, such disclosures may relate to information relevant to the capacity or utilisation of installations, such as planned or unplanned unavailability of such installations, partial decommissioning or even the permanent closure of the operation. But decisions that may affect for example the construction of new installations and changes in energy efficiency in major installations must also be disclosed. However, this obligation only applies if the installations or aviation activities have emissions that exceed specific thresholds. In addition, Recital 51 of the MAR explains that the information to be disclosed should concern the physical operations of the disclosing party and not its own plans or strategies for trading emission allowances, auctioned products based on them, or derivative financial instruments relating to them.

Emission allowance market participants that are already subject to notification obligations pursuant to Article 4 of the Regulation on Wholesale Energy Market Integrity and Transparency (REMIT)<sup>15</sup> can use the technical tools specified there for disclosures pursuant to Article 17 of

the MAR. This is possible if the inside information to be disclosed essentially has the same content and there is an assurance that the inside information is in fact transmitted to the relevant media. Separate disclosure pursuant to the MAR is not required in these cases: for emission allowances, Recital 51 of the MAR stipulates that duplication of mandatory disclosures pursuant to the MAR and REMIT should be avoided.

#### Areas in BaFin's focus

Many investigations conducted in 2018 were triggered by submissions received by BaFin. This shows that the capital market now examines ad hoc and other disclosures published by issuers much more critically. At the same time, the share of ad hoc disclosures that triggered further investigation remained at a high level.

In 2018, BaFin also expanded further on its interpretive practice on how to disclose inside information. On many issues, BaFin is in close consultation with other national competent authorities in the European Union and with ESMA. There are plans to collate BaFin's interpretive practice in its Issuer Guideline in 2019.

#### 2.1.4.2 Managers' transactions

Executives (e.g. members of management boards or supervisory boards) of issuers admitted to a regulated market or an MTF as well as persons closely related to such individuals reported a total of 3,260 securities transactions in 2018. In the previous year, BaFin had received 2,789 reports (see Figure 13 "Reports of

<sup>15</sup> Regulation (EU) No 1227/2011. OJ EU L 326/1.

managers' transactions"). After recording a significant rise in the number of transactions reported in 2016, the number of reports BaFin received in 2018 was similar to that of previous years.

## 2.1.5 Monitoring of short selling

### 2.1.5.1 Prohibitions

The EU Short Selling Regulation<sup>16</sup> prohibits uncovered short selling of shares and certain sovereign debt instruments. This also applies to the creation of, or entry into, sovereign credit default swaps (CDSs) other than for hedging purposes. BaFin followed up on suspicious transaction reports and its own evidence in 2018, investigating potential uncovered short selling in 71 cases (previous year: 100 cases). The suspicious transaction reports related to both companies and private individuals.

BaFin discontinued 49 investigations (previous year: 79 investigations discontinued). Most of the investigations discontinued in 2018 related to voluntary self-reports due to minor infringements, caused by human error, such as a misunderstanding when the customer placed an order. As at 31 December 2018, BaFin's investigation of 18 cases had not yet been completed (31 December 2017: 19 cases). BaFin referred

another 44 cases to other authorities within the EU for reasons of competence (previous year: 6 cases). BaFin pursued 6 cases further in administrative fine proceedings; it had completed 13 administrative fine proceedings in the previous year.

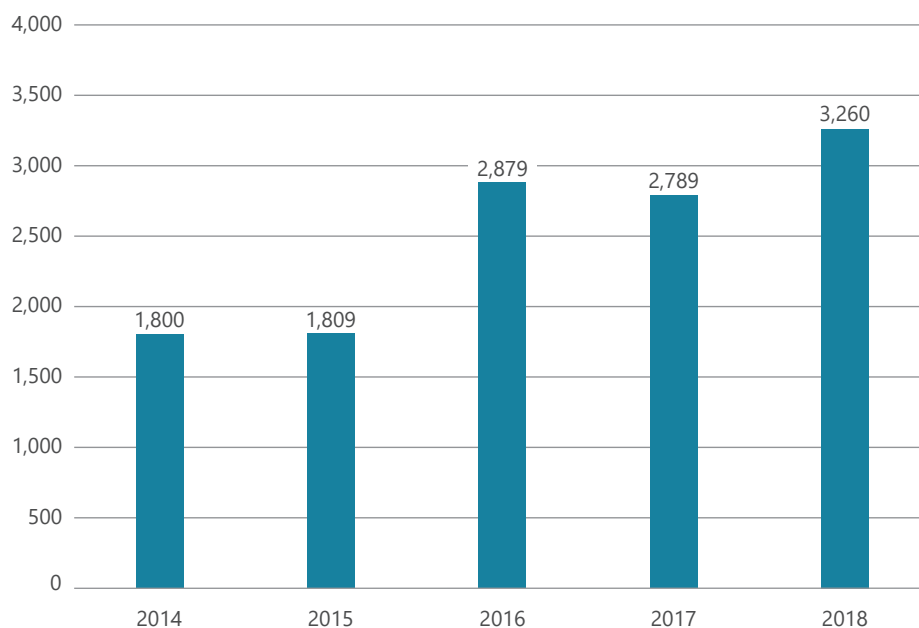
### 2.1.5.2 Transparency requirements and notifications by market makers

BaFin investigated 23 violations of the transparency requirements for net short positions in 2018 (previous year: 38 violations). A total of 17 investigations were discontinued, compared with 26 discontinued investigations in the previous year. As at 31 December 2018, the investigation of 7 cases had not yet been completed, compared with 12 cases on 31 December 2017.

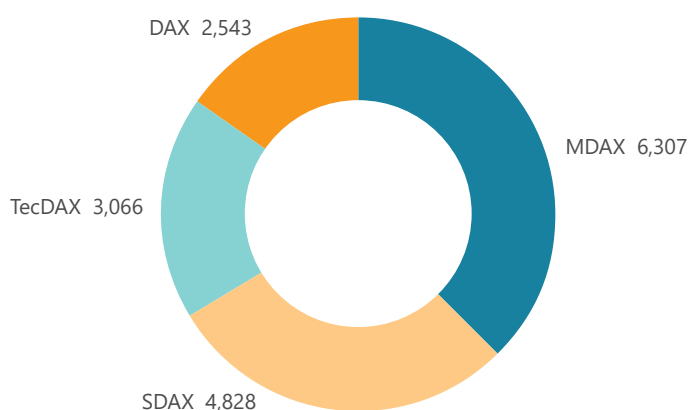
Net short positions are reported using BaFin's reporting and publishing platform. At the end of 2018, 444 undertakings and 2 private individuals were registered for the reporting system. As in previous years, most of the parties subject to the notification requirement came from the United States and the United Kingdom. In 2018, 279 parties subject to the notification requirement notified BaFin of a total of 16,417 net short positions (previous year: 12,861 net short positions) in 489 different shares (previous year: 281 shares) admitted to trading on a regulated market or multilateral trading facility. This corresponds to an average of 65 notifications per trading day. Of this total,

<sup>16</sup> Regulation (EU) 236/2012, OJ EU L 86/1.

**Figure 13: Reports of managers' transactions**



**Figure 14: Notifications broken down by index\***



\* The individual figures add up to more than the total number of notifications, because some issuers are represented in two indices.

4,764 notifications had to be published in the Federal Gazette (*Bundesanzeiger*) in 2018, because the threshold of 0.5% of the share capital in issue had been crossed or reached. A total of 4,001 notifications were published in the Federal Gazette in 2017. In addition, BaFin received 124 notifications for federal government debt securities (initial threshold: 0.5%; previous year: 135 notifications). By contrast, as in the previous year, there were no notifications for debt securities of the federal states (initial threshold: 0.1%). Most of the net short positions were built in shares by issuers on the regulated market (see Figure 14 “Notifications broken down by index”).

In 2018, 48 market makers (previous year: 44 market makers) and 31 primary dealers (previous year: 30 primary dealers) notified BaFin of their activities.

**Table 32: Notifications by market makers and primary dealers in 2018**

	Market makers	Primary dealers
Total number of companies	48	31
of which based in Germany	45	9
of which based abroad	3*	22**
Total number of notifications in 2018	1,628	1
Total number of notifications since September 2012	8,057	39

\* Non-EU third country.

\*\* Domiciled outside Germany.

In this process, they made use of the exemptions from the prohibitions on short selling and from the transparency requirements laid down in Article 17 of the EU Short Selling Regulation (see Table 32 “Notifications by market makers and primary dealers in 2018”).

## 2.1.6 Supervision of financial market infrastructures: central counterparties and central securities depositories

### 2.1.6.1 Brexit

Eurex Clearing AG plays a central role in the clearing of derivative contracts in Europe. Especially as far as the clearing of interest rate swaps is concerned, Brexit<sup>17</sup> could result in the relocation of the clearing business from the United Kingdom to the EU-27.

Eurex Clearing AG had created a new offering for clearing interest rate swaps back in 2017, which means that such an offering is now also available in the EU-27. In October 2018, the company expanded its offering to include the repurchase operations (repo) segment. Further expansion is planned for the OTC FX segment, where foreign exchange instruments are traded over the counter (OTC).

BaFin is in close consultation with Eurex Clearing AG on all matters relevant to Brexit. In 2018, the supervisory focus was on increasing the technical and organisational capacity required to deal with Brexit and the new clearing offering. BaFin will continue to give the institution intensive supervisory support in 2019.

<sup>17</sup> See chapter II 1.

### 2.1.6.2 Non-discriminatory access to CCPs – transitional period approved

Pursuant to Article 35 of the MiFIR, a trading venue has the right to non-discriminatory access to a central counterparty (CCP), if it meets certain conditions. These arrangements have been in force since 3 January 2018.

However, if requested by a CCP, Article 54(2) of the MiFIR allows the competent authority to exclude the application of Article 35 of the MiFIR as regards exchange-traded derivatives for a transitional period until 3 July 2020.

After a thorough review of the conditions, BaFin approved a request in this regard from Eurex Clearing AG with effect from 3 January 2018. This means that the company will only have to apply Article 35 of the MiFIR to exchange-traded derivatives from 3 July 2020.

### 2.1.6.3 Authorisation procedure for central securities depositories

On 10 March 2017, the European Union published the regulatory technical standard on the Central Securities Depositories Regulation<sup>18</sup>. In response, all European central securities depositories (CSDs) applied for their authorisations by the deadline of the end of September 2017. The application normally covers the core services provided by CSDs and, for selected central securities depositories, also banking-type ancillary services.

So far, only a small number of CSDs have been authorised, although most of them are in the midst of the authorisation procedure. This means that the completeness of the documentation has not yet been determined or that the supervisory authorities are still conducting the six-month review proceedings. The German central securities depository, Clearstream Banking Frankfurt, has not yet been authorised.

In 2018, the European Commission published the regulatory technical standards on settlement discipline<sup>19</sup>, which will enter into force after two years, i.e. on 13 September 2020. They deal with, among other things, the timing and substance of the communication between investment firms and their clients about the

transactions cleared by a CSD. Other key elements of the regulatory standards are a penalty mechanism and a buy-in process if securities are not delivered within certain settlement periods.

### 2.1.7 Supervision of OTC derivative transactions and compliance with position limits

Pursuant to the EU Regulation on OTC derivatives, central counterparties and trade repositories (European Market Infrastructure Regulation – EMIR)<sup>20</sup>, financial and certain non-financial counterparties must clear standardised OTC derivatives through a CCP. Alternative risk mitigation techniques, such as collateralisation, must be applied to OTC derivative transactions that do not have to be cleared through a CCP.

However, under EMIR, the companies concerned may opt not to collateralise transactions conducted within a consolidated or supervisory group. BaFin received a total of 66 requests to this effect in 2018. Details are listed in Table 33 “Notifications and requests”.

**Table 33: Notifications and requests**

	<b>Notifications/ requests 2017</b>	<b>Notifications/ requests 2018</b>
Total number of notifications/requests	<b>172</b>	<b>66</b>
One counterparty domiciled in other EU member state (notification)	102	39
One counterparty domiciled in third country (request)	70	27

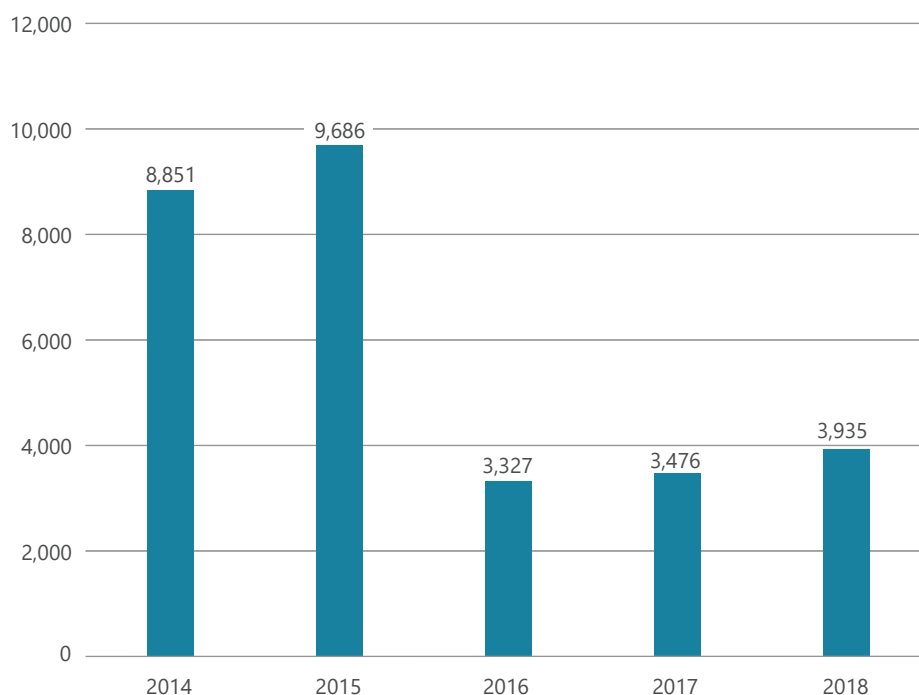
In parallel, companies that have been subject to the clearing obligation for OTC derivatives since 2016 have the option to request an exemption from this obligation for intragroup transactions. 11 requests to this effect were submitted in 2018, compared with 20 requests in the previous year.

The clearing and collateralisation requirements for OTC derivatives are subject to market surveillance by BaFin, which pursues a risk-based approach for financial counterparties, such as insurance undertakings, investment firms, banks and funds. If the volume of

<sup>18</sup> Regulation (EU) No 909/2014. OJ EU L 257/1.

<sup>19</sup> Delegated Regulation (EU) No 1229/2018. OJ EU L 230/1.

<sup>20</sup> Regulation (EU) No 648/2012. OJ EU L 201/1.

**Figure 15: Voting rights notifications**

derivatives exceeds a certain threshold, non-financial counterparties are required pursuant to section 32 of the Securities Trading Act (until 2 January 2018: section 20 of the Securities Trading Act) to comply with the key requirements of EMIR. Evidence of compliance is provided by producing an auditor-issued certificate.

#### **New requirements for position limits**

The requirements for position limits and position reporting for commodity derivatives laid down in MiFID II entered into force at the beginning of 2018. BaFin imposed 15 individual position limits in commodity derivatives by way of general administrative acts in 2018. Apart from one position limit on freight rates, they exclusively affected energy contracts. In parallel, the technical infrastructure was created, which allows parties subject to the notification requirement for positions in commodity derivatives to meet their obligations electronically by the set deadline.

#### **No sustained violations of notification requirements**

BaFin did not find evidence of sustained violations of the notification requirements in the period under review. To date, only a small number of requests for hedging exemptions have been received. However, based on reactions from the market, BaFin expects more requests for exemptions in 2019.

### **2.1.8 Voting rights and duties to provide information to securities holders**

3,935 changes in voting interests were reported to BaFin in 2018 (see Figure 15 “Voting rights notifications”, compared with 3,476 changes in 2017. Of these, 2,016 notifications (previous year: 2,214 notifications) were group notifications, in which the parent company reported changes in or levels of equity interests. A further 754 notifications (previous year: 455 notifications) were voluntary group notifications, where only subsidiaries had reporting obligations, but the ultimate parent (voluntarily) submits a group notification that exempts the subsidiaries from this obligation.

Submissions for the three notification criteria pursuant to the Securities Trading Act break down as follows:

- 2,654 notifications (previous year: 2,674 notifications) relating to changes in voting rights triggered by the number of voting rights reaching or crossing certain thresholds (sections 33 and 34 of the Securities Trading Act);
- 215 notifications (previous year: 204 notifications) relating to changes resulting from holdings of financial instruments reaching or crossing thresholds (section 38 of the Securities Trading Act);

- and 219 notifications (previous year: 219 notifications) relating to aggregated voting rights and holdings of financial instruments (section 39 of the Securities Trading Act)<sup>21</sup>.

839 notifications (previous year: 436 notifications) related to levels of equity interests: they did not report that thresholds had been crossed or reached, but merely that the level of equity interests had changed.

In the year under review, 517 companies were admitted to trading on the regulated market, compared with 602 companies in the previous year.<sup>22</sup> These companies published 305 notifications of changes in their voting share capital, as against 313 in 2017. At the end of 2018, 5 of these companies were real estate investment trusts (REITs).

Since the end of October 2018, parties subject to the reporting requirement have also been able to submit their voting rights notifications to BaFin and the issuer concerned electronically using the reporting and publishing platform (MVP Portal).

### 2.1.9 Recommendations of financial instruments

At the end of 2018, a total of 389 credit and financial institutions in Germany that provide their clients with in-house recommendations or recommendations developed by third parties within the meaning of Article 20 of the EU Market Abuse Regulation (MAR) were supervised by BaFin<sup>23</sup>. In the previous year, this affected 392 institutions. In addition, BaFin was notified of 138 independent natural or legal persons or associations of individuals that produced or disseminated recommendations, compared with 236 notifications in the previous year.

The Second Act Amending Financial Markets Regulations (*Zweites Finanzmarktnovellierungsgesetz*) allows the publication of a list of independent producers and/or disseminators of investment recommendations – provided they are not natural persons. In addition, the act imposes stricter requirements for proof of identity for activity notifications. Against this background, BaFin

launched an examination in the period under review of all activity notifications filed in the past.

The list of independent producers and/or disseminators of investment strategy and investment recommendations, which has been published at [www.bafin.de](http://www.bafin.de), only names those legal persons and associations of individuals that have duly notified their activities and submitted the requisite proof of identity. Their number amounted to 96 as at the end of the year under review. Natural persons are not included in the list because, as mentioned earlier, there is currently no legal basis for doing so.

Inclusion in the list of independent producers and/or disseminators of investment strategy and investment recommendations is not a reflection on the quality of the analyses they have published. BaFin updates the list as soon as it receives new information, such as new notifications and notifications of changes.

## 2.2 Prospectuses

### 2.2.1 Prospectus examination under the German Capital Investment Act (*Vermögensanlagegesetz*)

#### **Prospectus scrutiny under the Capital Investment Act**

In Germany, capital investments cannot be offered to the public without a prospectus approved by BaFin in advance. There are some exemptions from the prospectus requirement, for example for crowdfunding. Prospectuses for capital investments must be prepared in accordance with the Capital Investment Act. Their content and structure are governed by the German Investment Prospectus Regulation (*Vermögensanlagen-Prospektverordnung*).

Prospectuses play a crucial role in investor protection. Firstly, the prospectus is a key transparency and information document, which allows investors to make appropriate investment decisions. For this reason, it contains comprehensive information on the issuer and the capital investment. In addition, the prospectus constitutes the main basis for determining liability in disputes if it fails to contain all the material information required for the investment decision or the information provided does not correspond to the facts.

BaFin examines prospectuses under its legal mandate to establish whether they are complete, comprehensible and coherent (see info box “Scope of examination” on page 143). If the prospectus submitted fails to meet the legal requirements, BaFin normally discusses the deficiencies with the offeror. Alternatively, it may

<sup>21</sup> A single notification may relate to thresholds based on several notification criteria. As a result, the aggregate number of notifications attributable to the notification criteria is not the same as the total number of notifications submitted in the year under review.

<sup>22</sup> The decline is mainly due to adjustments to the counting method.

<sup>23</sup> Securities Supervision/Asset Management Sector.

## Scope of examination

The examination standard that BaFin applies in the approval process for investment prospectuses is prescribed by law and based on the provisions of EU securities prospectus law. They require prospectuses to be examined for completeness, comprehensibility and coherence. BaFin does not, however, examine the content or quality of the prospectus according to the legally defined standard for prospectus examination.

Coherence means that the information provided in the prospectus must be intrinsically consistent. BaFin checks whether individual details provided in the prospectus are consistent with each other, i.e. whether the prospectus itself is free from internal contradictions.

The coherence check does not mean that BaFin compares the prospectus with other information or documents or with other prospectuses. The

examination can in each case only relate to the prospectus submitted, which only contains information and figures as at the date of preparing the prospectus concerned. The prospectus examination conducted by BaFin does not involve responsibility for checking or comparing prospectuses from earlier issues to establish whether timings or contents have changed.

Nor does the scope of the coherence check include an assessment of whether the product presented is appropriate or plausible. The legal framework does not require a review of whether the information in the prospectus is correct. This means that neither the issuer's creditworthiness nor its integrity or the proper functioning and economic viability of its business model are assessed. Likewise, BaFin's prospectus examination does not involve an assessment of a product's chance of success.

withhold approval. But as soon as the prospectus meets the legal requirements, the offeror has a legal right to approval by BaFin.

To ensure that prospectuses are up to date, every prospectus is only valid for offers to the public for a period of 12 months. If the capital investment is to continue to be offered to the public after that, a new prospectus must be prepared and submitted to BaFin for approval.

### 2.2.2 Securities prospectuses/database

BaFin approved 21 prospectuses for initial public offerings (IPOs) in 2018, three times as many as in 2017 (7 prospectuses approved, see Table 34 "Number of approvals in 2018 and 2017"). Since the examination of IPO prospectuses is very complex, it dominated the supervisory work of the divisions responsible for examining securities prospectuses. The issue volumes of these IPOs ranged from €1.7 million to €4.2 billion.

The total number of final terms for base prospectuses filed indicates that the banks engaged in lively issuance activity: this number increased from 3,491,583 in 2017 to 4,450,367 in the year under review, thus continuing a multi-year trend.

Since the relevant act entered into force on 21 July 2018, BaFin has approved 14 securities information sheets (see info box "Securities information sheet" on page 144). 9 of them related to share issues and 4 to bond issues. In most cases, the issue volume was below €1 million.

**Table 34: Number of approvals in 2018 and 2017**

Product	2018	2017
Prospectuses (of which IPOs)	303 (21)	301 (7)
Registration documents	35	38
Supplements	836	1,066
Notifications transmitted	2,819	3,143
Notifications received	756	692

## Securities information sheet

The EU Prospectus Regulation<sup>24</sup> sets the threshold for the prospectus requirement of offers to the public at a total consideration of €1 million. Below this threshold, EU member states may impose other proportionate disclosure requirements at national level, but they may not demand a prospectus. In addition, the regulation allows member states to exempt offers to the public not exceeding €8 million from the prospectus requirement altogether.

In particular, an amendment to the German Securities Prospectus Act (*Wertpapierprospektgesetz*) makes it possible to take advantage of this EU provision in Germany: issuers offering securities with a total consideration of between €100,000 and less than €8 million – calculated over a 12-month period – to the public may prepare, file and publish a securities information sheet instead of a prospectus. This document is intended to serve as a source of

information for investors; it may only be published if authorised by BaFin. In no more than three pages, the securities information sheet has to provide in a clear and easily understandable way the key information on the securities, the offeror, the issuer and any guarantors. The details to be included and the order in which they are presented are prescribed. For the duration of the offer to the public, the securities information sheet has to be updated or corrected if necessary.

For offers between (and including) €1 million and less than €8 million addressed to non-qualified investors, the securities information sheet may only be used if an investment services enterprise brokers the securities exclusively by way of investment advice or broking, taking the wealth- and income-related individual investment thresholds into account.<sup>25</sup>

### 2.2.3 Non-securities investment prospectuses

In 2018, BaFin received a total of 93 investment prospectuses for checking. This represents another market-related decline compared with the previous year (121 prospectuses; see Figure 16 “Prospectuses received, approved, withdrawn and rejected” on page 145). BaFin approved 84 prospectuses (previous year: 93 prospectuses). 20 processes were discontinued because the offerors in question had withdrawn their application. In 1 other case, BaFin prohibited publication. The breakdown of prospectuses received by type of participation is shown in Figure 17 “Prospectuses by type of participation” on page 145. Figure 18 “Prospectuses by target investment” on page 145 shows the figures broken down by target investment.

#### Supplements to investment prospectuses

In 2018, BaFin received a total of 32 applications for the approval of supplements under the Capital Investment Act (previous year: 41 applications received). BaFin approved 31 of the supplements in total (previous year: 36 supplements).

### Capital investment information sheets without prospectus

Offerors have been required to undergo the approval process for capital investment information sheets since August 2017. In 2018, BaFin received 491 capital investment information sheets in crowdfunding processes for approval or updating (previous year: 452 documents received). BaFin approved their publication in 405 cases. 33 applications for approval of capital investment information sheets were withdrawn in the year under review.

### 2.2.4 Market supervision of offers of securities and capital investments to the public

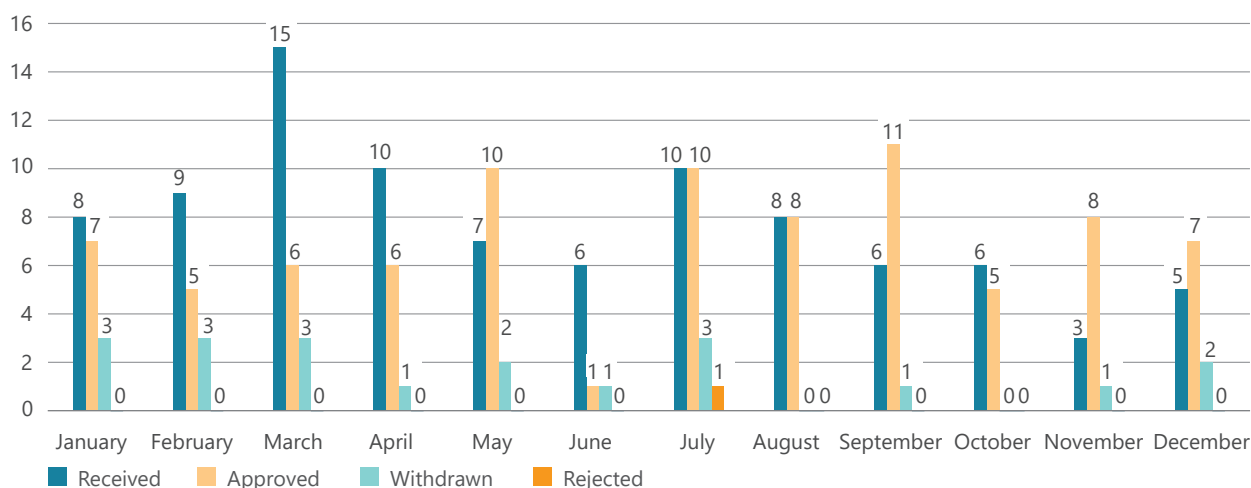
In 2018, BaFin conducted 142 market surveillance proceedings for possible violations of the Capital Investment Act and the Securities Prospectus Act (previous year: 150 proceedings). As part of this process, BaFin firstly investigated tip-offs it had received, and secondly it conducted its own checks of offers and the way they were marketed. In over 80% of these

<sup>24</sup> Regulation (EU) 2017/1129, OJ EU L 168/12.

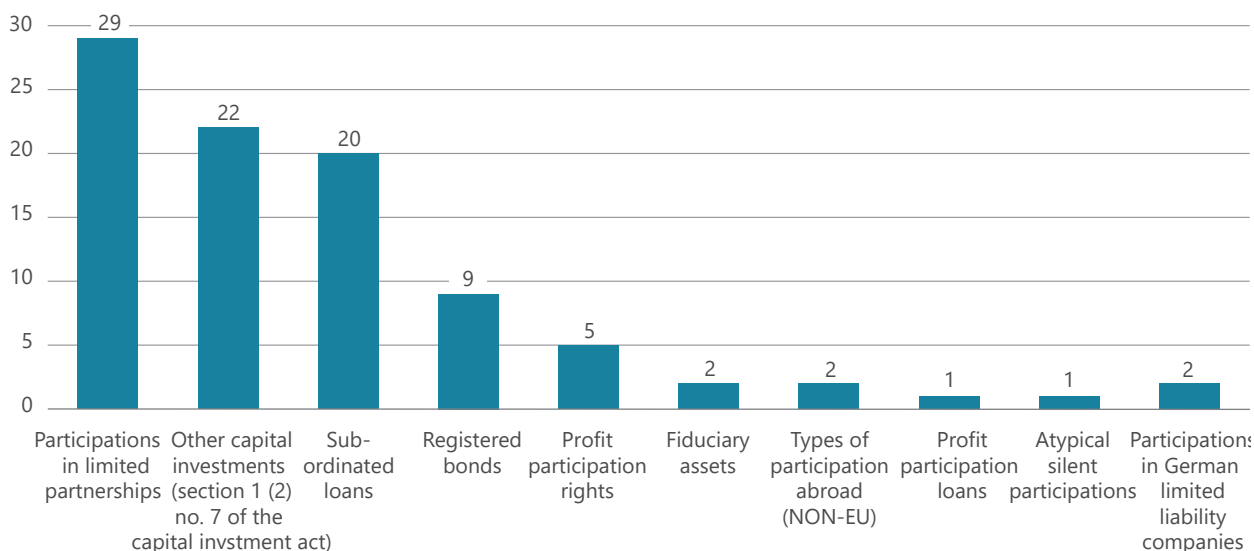
<sup>25</sup> [www.bafin.de/dok/11301580](http://www.bafin.de/dok/11301580).



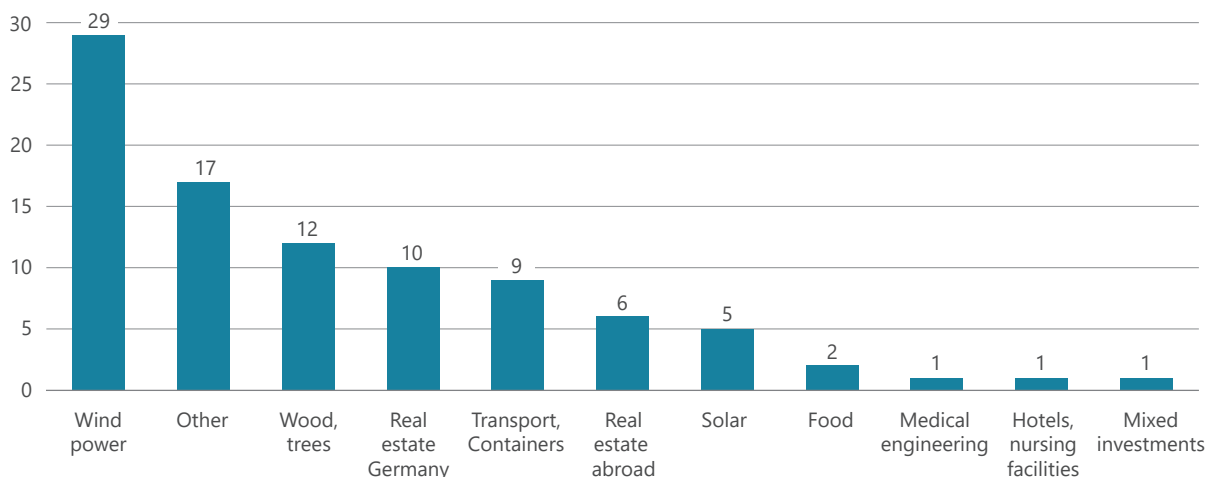
**Figure 16: Prospectuses received, approved, withdrawn and rejected**



**Figure 17: Prospectuses by type of participation**



**Figure 18: Prospectuses by target investment**



142 proceedings, it investigated whether capital investments or securities were offered to the public without publishing a prospectus in violation of the obligation to do so. BaFin completed 58 of the investigations in 2018. Where BaFin identified violations while the offer was still ongoing, it formally prohibited the offer or made the irregularity public. 14 of the investigations completed related to offers of shares to the public. In 9 cases, they involved a public offer of bonds, and another 24 proceedings dealt with direct investments, i.e. other types of investments.

BaFin found 5 violations of the prospectus requirement by providers of subordinated loans, significantly fewer than in the previous year (17 violations). The decline is attributable to the fact that BaFin regularly informs the providers concerned of violations and also rigorously prosecutes such violations.

There was also a slight decline, to 12, in the number of investigations due to suspected public offers of shares within the meaning of section 1 (2) no. 1 of the Capital Investment Act (previous year: 15 investigations). Examples include shares in partnerships (in particular OHG and KG) or shares in German limited liability companies (GmbH).

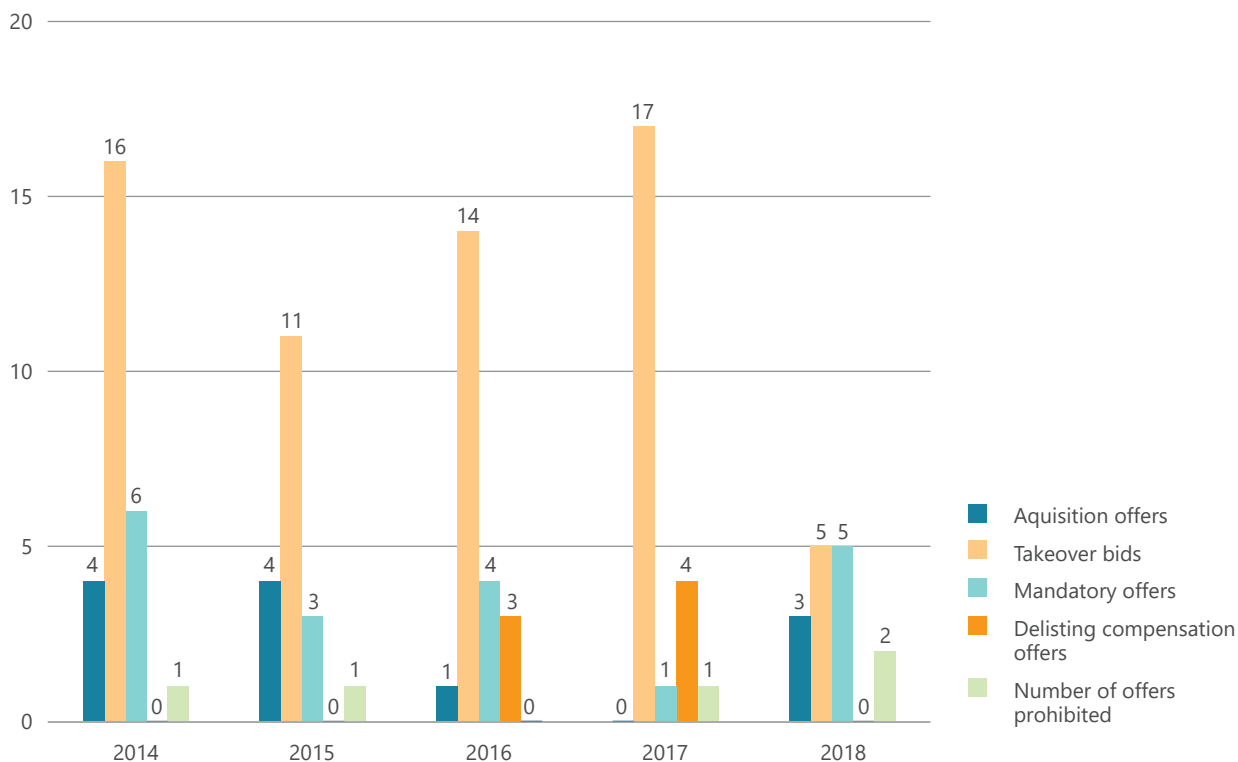
Marketing violations represented 16% of market surveillance proceedings in the year under review. BaFin completed 17 of the total 27 investigations. Most cases, 15 in total, related to violations of the notification requirements laid down in section 12 (2) of the Capital Investment Act. Here, BaFin found fault not so much with the fact that there was no warning as with the fact that it was not clearly enough highlighted in many cases. In 6 cases, BaFin criticised that there was no warning relating to the promised return in the marketing material for investments offered to the public (section 12 (3) of the Capital Investment Act). In 3 cases, BaFin objected to a reference in the marketing material for investments offered to the public, which is unlawful pursuant to section 12 (4) of the Capital Investment Act. A further 3 cases related to a marketing violation under the Securities Prospectus Act.

### 2.3 Company takeovers

#### Offer procedures

BaFin checked a total of 15 offer documents (previous year: 23 offer documents) in 2018. It approved their publication in 13 cases and prohibited the publication of 2 offer documents (see Figure 19 “Offer procedures from 2014 to 2018”).

**Figure 19: Offer procedures 2014 to 2018**



### **Takeover bid to the shareholders of innogy SE**

BaFin paid special attention in 2018 to the takeover bid that E.ON Verwaltungs SE submitted to the shareholders of innogy SE. The bid was embedded in an overall package that also included a share purchase agreement and asset swap with the RWE Group. If the takeover is successful, E.ON and RWE will in future focus on different segments. Whether the transaction, including the takeover bid, can be completed is, however, still dependent on antitrust approvals, since the offer document for the takeover bid contained two amendments to the offer conditions pursuant to section 18 of the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz*).

Firstly, as for the antitrust approvals, BaFin had for the first time allowed a long-dated offer condition of more than 12 months from the end of the acceptance period. This had been triggered by expectations of extensive antitrust investigations in a highly regulated sector. Another factor was the uncertainty brought about by Brexit in this context. However, according to BaFin's existing administrative practice, the respective offeror had to offer certain compensation payments in favour of the shareholders of the target company for all offer conditions that, by way of exception, extended beyond the end of the acceptance period. In addition to establishing liquid exchange trading, this case involved the notarisation, by a notary in the offer document, of the extension of the statutory period for subsequent acquisition pursuant to section 31 (5) sentence 1 of the Securities Acquisition and Takeover Act to the end of the long-dated period and of the publication of all subsequent acquisition transactions during this period.

Secondly, BaFin allowed for the first time that the offeror could protect itself from the prohibition of individual parts of the transaction by using a long-dated offer condition on the basis of the Holz Müller/Gelatine case law of the Federal Court of Justice (*Bundesgerichtshof*) on approval requirements by the general shareholders' meeting.

### **Atypical exchange offer to the shareholders of Biofrontera AG**

On 16 March 2018, Deutsche Balaton AG announced publicly that it intended to acquire up to 6.25 million shares of Biofrontera AG. For this, it intended to offer a consideration mix, consisting of €1 and a warrant. Each warrant was to allow its holders to acquire back one Biofrontera share at a later date. There was, however, no securities prospectus approved by BaFin for the warrants to be offered, nor did Deutsche

Balaton AG submit within four weeks an offer document containing all the disclosures about the warrants required under prospectus law. BaFin therefore had no choice but to prohibit the partial acquisition offer on 25 April 2018.

On the same day, Deutsche Balaton Biotech AG, a wholly owned subsidiary of Deutsche Balaton AG, declared that it would submit a partial acquisition offer that was substantially the same. On 28 May 2018, it published the corresponding offer document with all the mandatory disclosures required under prospectus law about the warrants being offered. The transaction was a first in that never before had a mere (partial) acquisition offer been designed as an exchange offer under the regime of the Securities Acquisition and Takeover Act. It was also the first time that the consideration offered initially included only securities other than the offeror's own shares plus a cash component. However, on 20 July 2018, Deutsche Balaton Biotech AG made a supplemental alternative offer of pure cash compensation of €6 for each share of Biofrontera AG.

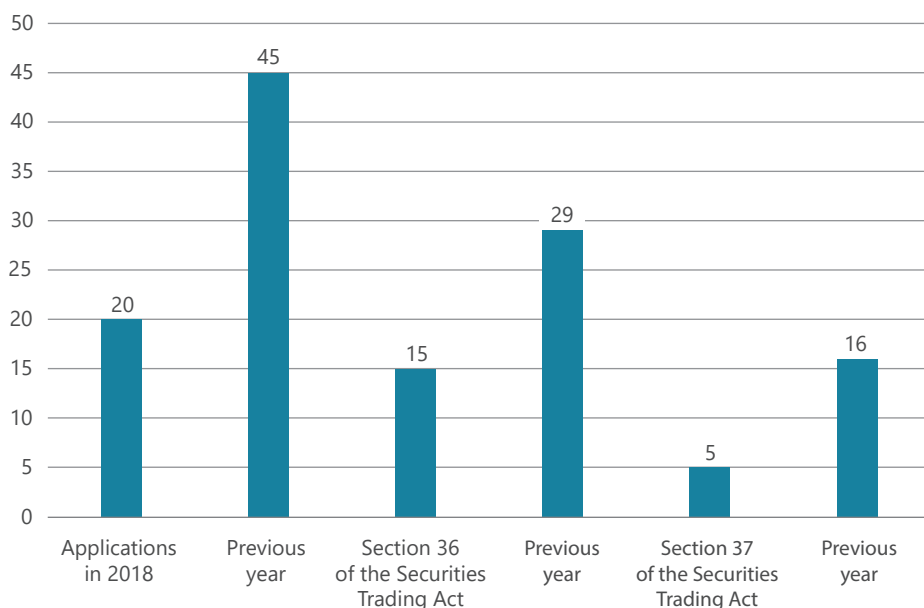
### **Prohibition of mandatory offers**

By way of a notice issued on 5 September 2018, BaFin prohibited the mandatory offer of the offerors, Triton Liegenschaften GmbH, Bergisch Gladbach, and Jochen Schwarz, to the shareholders of Pinguin Haustechnik AG, Hamburg, pursuant to section 15 (1) no. 3 of the Securities Acquisition and Takeover Act. In a statement published on 27 July 2018, the offerors had declared that they had obtained control of Pinguin Haustechnik AG, Hamburg. But they had failed to submit an offer document for examination by BaFin within a four-week period, as required pursuant to section 14 (1) sentence 1 of the Securities Acquisition and Takeover Act. Despite the prohibition, Triton Liegenschaften GmbH and Jochen Schwarz have to proceed with the mandatory offer procedure. A prohibition pursuant to section 15 of the Securities Acquisition and Takeover Act that relates to a mandatory offer does not generally affect the essential obligation to submit to BaFin an offer document that meets the legal requirements and to make a mandatory offer. The effect of the prohibition in such cases is mainly that the obligation to pay interest (section 38 no. 3 of the Securities Acquisition and Takeover Act) and the loss of rights (section 59 of the Securities Acquisition and Takeover Act) are put beyond dispute.

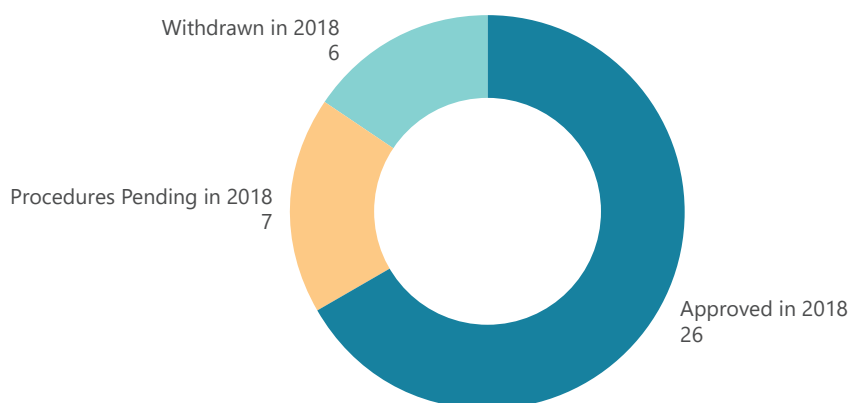
### **Exemption procedures**

BaFin received a total of 20 applications for exemption or non-consideration in 2018 (previous year: 45 applications), see Figure 20 "Exemption procedures" on page 148.

**Figure 20: Exemption procedures**



**Figure 21: Processing status of exemption procedures under the Securities Acquisition and Takeover Act**



26 applications for exemption or non-consideration were approved in the course of 2018; 6 applications were withdrawn (see Figure 21 “Processing status of exemption procedures under the Securities Acquisition and Takeover Act”).

## 2.4 Financial reporting enforcement

### Monitoring of financial reporting

The number of companies subject to the two-tier enforcement procedure by BaFin and the German Financial Reporting Enforcement Panel (*Deutsche Prüfstelle für Rechnungslegung – FREP*) declined by 9 in 2018 as against the previous year. As at 1 July 2018, a total of 552 companies (previous year: 561 companies) from 8 countries, as in 2017, were affected.

The FREP completed a total of 84 examinations in 2018 (previous year: 99 examinations), of which 80 were sampling examinations. The error findings by BaFin, where the undertaking had not accepted the FREP’s finding or refused to cooperate with the FREP at the first stage of the enforcement proceedings (see Table 35 “Enforcement procedures completed” on page 149), related to various accounting issues, such as the recognition of compensation claims, the measurement of a subsidiary and various notes disclosures. At the end of 2018, 10 cases were still pending at BaFin; in 7 of these, BaFin performs its own error identification procedures.

### Publication of financial reports

In 2018, BaFin examined in approximately 920 cases (previous year: 930 examinations) whether the issuers

**Table 35: Enforcement procedures completed**

	Error finding: yes	Error finding: no	Error publication: yes	Error publication: no
Companies accept FREP's findings	12	n/a	12	0
Companies do not accept FREP's findings	1	2	1	0
Companies refuse to cooperate with FREP	3	0	3	0
BaFin has material doubts as to the accuracy of the FREP's findings/procedure	0	0	0	0
Examination taken over by BaFin (banks, insurance undertakings)	0	0	0	0
<b>Total</b>	<b>16</b>	<b>2</b>	<b>16</b>	<b>0</b>

had published their online annual and half-yearly financial reports on time. In 19 cases (previous year: 16 cases) it found indications of violations, which it pursued further in administrative fine proceedings.<sup>26</sup>

As in the previous year, BaFin continued to monitor the publication of notifications in 2018, which are intended to provide information on when and where issuers publish their financial reports on the internet. In 19 cases (previous year: 31 cases), issuers whose registered office is in Germany failed to publish these notifications. 18 of these cases related to annual financial reports and 1 case to a half-yearly financial report. In 16 cases, the issuers had not only neglected to publish the notifications on annual financial reports, but also failed to publish the financial reports themselves. The Federal Office of Justice (*Bundesamt für Justiz*) monitors the publication of annual reports by issuers whose registered office is in Germany. BaFin initiated administrative offence proceedings in cases where the notification had not been published.<sup>27</sup>

An annual check is also required to verify whether the published half-yearly financial reports contain the minimum components required by law. In 15 cases, BaFin found that there was no responsibility statement, which prompted it to pursue these 15 cases further in administrative fine proceedings.

BaFin launched 13 administrative procedures to enforce the financial reporting requirements, compared with 8 such procedures in the previous year. A total of 17 proceedings were still pending from previous years, and 7 proceedings were concluded by BaFin in 2018. Most of the pending proceedings are at the enforcement

stage. BaFin threatened coercive fines in a total of 11 cases. It imposed coercive fines of up to €565,000 and initiated enforcement measures in 9 cases.

In 2018, BaFin published information on 16 companies, detailing the measures taken and the associated comments pursuant to section 124 of the Securities Trading Act. In the previous year, it published this kind of information on 11 companies.

## 2.5 Supervision of the investment business

### 2.5.1 Asset management companies and depositaries

In 2018, 12 (previous year: 11) German asset management companies (*Kapitalverwaltungsgesellschaft*) were authorised to manage investment funds or their existing authorisation was extended. 2 companies surrendered their authorisation, compared with 6 in the previous year. This brought to 146 the number of companies in Germany with an authorisation in accordance with the German Investment Code (*Kapitalanlagengesetzbuch*) at the end of 2018, as against 136 companies in the previous year. In addition, 71 asset management companies registered in accordance with section 44 of the Investment Code; 52 companies had requested registration in 2017. 6 asset management companies surrendered their registration, 1 of which applied for authorisation in accordance with the Investment Code. The total number of asset management companies registered at the end of 2018 therefore stood at 379 (previous year: 314 asset management companies).

In 13 cases, asset management companies established a branch in another EU member state or offered cross-border services (previous year: 22 cases). Conversely,

<sup>26</sup> See also 2.6.1.

<sup>27</sup> See also chapter II 4.

57 asset management companies from other EU countries notified BaFin that they had established a branch or started providing cross-border services in Germany (previous year: 53 companies).

### **Risk-based supervision**

During the year under review, BaFin performed 99 supervisory visits and annual interviews on site, compared with 116 in 2017. In addition, it accompanied 18 audits and special audits at asset management companies as well as at depositaries and trustees (previous year: 5 audits accompanied).

The supervisory and annual interviews conducted in 2018 focused in particular on how to deal with negative interest rates and issues related to Brexit, such as investments in the United Kingdom. Other central topics included, among others, sustainable investments, issues of IT security, fund costs and the cost structure of ETFs. Other issues on which the supervisory and annual interviews focused included the response to current and future new supervisory regulations, such as the General Data Protection Regulation (GDPR), MiFID II, the Supervisory Requirements for IT in Asset Management Companies (KAIT)<sup>28</sup> and depositary circulars.

## **2.5.2 Investment funds**

The German investment market continued to grow in 2018, with both special and retail funds recording cash inflows.

At the end of 2018, asset management companies in Germany managed a total of 6,679 open-ended investment funds (previous year: 6,370 funds) with assets totalling €2,057 billion (previous year: €2,055 billion). Of these funds, 2,576 were retail funds with assets totalling €468 billion and 4,103 were special AIFs<sup>29</sup> with assets of €1,589 billion. In the previous year, assets totalling €491 billion were attributable to 2,341 retail funds and assets of €1,564 billion to 4,029 special AIFs.

Aggregate (net) cash inflows into domestic retail and special funds amounted to €103.3 billion in the year under review (previous year: €107 billion). (Gross) cash inflows amounted to €355.9 billion (previous year: €330.7 billion). Of this total, €113.3 billion was attributable to retail investment funds (previous year: €113.7 billion) and €242.6 billion to special AIFs (previous

year: €217 billion). This was set against cash outflows totalling €253 billion (previous year: €223.7 billion).

In 2018, BaFin approved exactly 152 new retail investment funds in accordance with the Investment Code, including 114 undertakings for collective investment in transferable securities (UCITS), 5 open-ended retail AIFs and 33 closed-ended retail AIFs. In the previous year, BaFin had authorised 138 retail investment funds in accordance with the Investment Code, including 107 UCITS, 7 open-ended retail AIFs and 24 closed-ended retail AIFs.

### **2.5.2.1 Open-ended real estate funds and hedge funds**

As at the end of 2018, 61 asset management companies had an authorisation to manage open-ended real estate funds (previous year: 58 companies). In 2018, 4 companies received their authorisations from BaFin and 1 surrendered its authorisation.

While 21 asset management companies also established open-ended real estate funds for retail investors (previous year: 21 asset management companies), 40 companies limited their activities to the management of open-ended real estate special funds (previous year: 37 asset management companies). Of this number, 7 companies have to date not established any open-ended real estate funds.

1 open-ended real estate fund for retail investors was issued in the course of 2018, increasing the number of these funds to 54 (previous year: 53 funds). The fund volume of this market segment amounted to €99.01 billion as at the end of the year (previous year: €92.33 billion).

In 2018, gross cash inflows into open-ended real estate funds for retail investors amounted to €8.0 billion. Gross cash inflows into open-ended real estate special funds declined slightly to €15.5 billion (previous year: €16.2 billion). The fund assets of open-ended real estate special funds amounted to €103.7 billion at the end of 2018 (previous year: €88.2 billion).

22 open-ended real estate funds for retail investors were in liquidation at the end of 2018 (previous year: 21 funds). Their fund volume amounted to €3.17 billion (previous year: €3.92 billion). The management rights for 20 of these funds have already been transferred to the depositary (previous year: 19 funds).

There were 13 hedge funds in Germany at the end of 2018 (previous year: 14 hedge funds). The total

<sup>28</sup> For information on KAIT, see also chapter II 6.1.

<sup>29</sup> Alternative investment funds.

volume under their management was €3.36 billion (previous year: approximately €3.43 billion). As in 2017, there were no German funds of hedge funds in Germany.

### 2.5.2.2 Foreign investment funds

In 2018, there were 10,511 EU UCITS<sup>30</sup> authorised for marketing (previous year: 10,183 funds). BaFin processed a total of 1,158 new notifications by companies wanting to market EU UCITS in Germany, compared with 1,006 new notifications in 2017. As in previous years, most of the notifications – 650 in total – came from Luxembourg. In addition, BaFin received 361 notifications from Ireland, 41 from France and 31 notifications from Austria. Marketing was discontinued for 830 EU UCITS.

In addition, 2,095 EU AIFs and 321 foreign AIFs from third countries were authorised to conduct marketing in Germany (previous year: 1,591 EU AIFs and 285 foreign AIFs from third countries). Of the total number, 1,343 originated in Luxembourg, 232 in the United Kingdom, 264 in Ireland, 115 in the Cayman Islands, 110 in the United States, 91 in France, 47 in the Netherlands and 2 in Switzerland. In 2018, marketing for 771 AIFs (previous year: 553 AIFs) started in Germany, including 477 from Luxembourg, 40 from the United Kingdom, 52 from Ireland, 30 from the Cayman Islands and 16 from the United States. 231 EU AIFs and foreign AIFs ceased marketing, including 110 from Luxembourg, 51 from the United Kingdom and 28 from Ireland.

## 2.6 Administrative fine proceedings

### 2.6.1 Administrative fines<sup>31</sup>

Due to violations of provisions of securities law, BaFin initiated a total of 135 new administrative fine proceedings in 2018 (previous year: 188 proceedings; see Table 36 “Administrative fine proceedings” on page 153). A total of 869 cases from previous years were still pending at the beginning of 2018.

<sup>30</sup> UCITS are funds that meet the requirements of Directive 2009/65/EC of the European Parliament and of the Council of 13 July 2009 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities.

<sup>31</sup> For administrative fine proceedings due to violations by investment firms of the conduct of business rules as well as organisational and transparency requirements under the German Securities Trading Act (*Wertpapierhandelsgesetz*) and violations of the German Banking Act (*Kreditwesengesetz*), see chapters II 2.5.2 and II 4.

The penalty rate was 39.8% in 2018. BaFin completed 126 of the investigations by imposing fines totalling approximately €7.8 million.<sup>32</sup> BaFin discontinued a total of 193 proceedings, 160 for discretionary reasons. This means that 322 proceedings were completed in total. Only 682 proceedings were still pending at the end of 2018.

### 2.6.2 Proceedings completed by imposing revenue-based administrative fines

Since the German Act Implementing the Transparency Directive Amending Directive (*Gesetz zur Umsetzung der Transparenzrichtlinie-Änderungsrichtlinie*)<sup>33</sup> entered into force, BaFin has been able to impose fines that are based on a legal person’s revenue generated in the preceding financial year. To do so requires that the maximum revenue-based fine provided for in the act exceeds the absolute maximum fine. For example, under the provisions implementing the Transparency Directive, BaFin can impose an administrative fine of up to €10 million or an administrative fine amounting to 5% of the previous year’s total revenue. The decisive criterion is which total is higher. In 2018, BaFin imposed fines determined on the basis of revenue in 5 multiple-case proceedings<sup>34</sup>.

The highest revenue-based administrative fine imposed on a company in 2018 was ordered by BaFin because of a breach of that company’s duty of oversight within the meaning of section 130 (1) sentence 1 of the Act on Breaches of Administrative Regulations (*Ordnungswidrigkeitengesetz*). This fine amounted to €1.34 million.<sup>35</sup> Another case, which involved the failure to publish a notification on an annual financial report in a timely manner, was completed by BaFin by imposing a revenue-based administrative fine of €94,000.

### 2.6.3 Information published

Since the Act Implementing the Transparency Directive Amending Directive entered into force, BaFin has published on its website information on its own measures and sanctions as well as on disciplinary fine decisions of the Federal Office of Justice. In the past 3 years, it published information on 46 administrative

<sup>32</sup> The total amount of administrative fines imposed also includes the administrative fine proceedings presented in chapter II 4.

<sup>33</sup> Act Implementing the Transparency Directive Amending Directive of 20 November 2015, Federal Law Gazette I 2015, page 2029.

<sup>34</sup> 7 proceedings (as at 18 December 2018, not yet final).

<sup>35</sup> See 2.6.4.

actions and 21 administrative fines of BaFin and 71 disciplinary fine decisions of the Federal Office of Justice. This approach is intended to reinforce the general preventive effect of measures and sanctions and to encourage market participants to act in accordance with the law.

The intention of legislators is, as a rule, that the information is not anonymised and published without undue delay. There are, however, circumstances that require in individual cases that publication is delayed or anonymised, or that the information is not published at all. Within the scope of section 124 of the Securities Trading Act, the information can only be anonymised in the case of natural persons.

#### 2.6.4 Selected cases

In 2018, BaFin imposed a fine of €42,000 on an individual who had violated the prohibition on market manipulation under section 20a of the Securities Trading Act, old version. In six cases, he had used sham buy and sell orders in certain financial instruments to give misleading indications of supply and demand.

In proceedings against a credit institution due to a negligent breach of its duty of oversight, BaFin imposed an administrative fine of €1.34 million. The institution had failed to establish suitable oversight and organisational measures to meet its own voting rights notification requirements and those of its group subsidiaries as prescribed.

In another case, BaFin imposed an administrative fine of €57,500 on an undertaking. This institution had negligently breached its duties of oversight, and this resulted in violations of the prohibition on naked short selling. The management board had failed over an extended period to take adequate oversight and organisational measures to ensure that market maker notifications were submitted to BaFin. When the financial services institution was made aware of this by BaFin, it rectified the organisational deficiencies.

Furthermore, BaFin imposed an aggregate administrative fine of €2.4 million on a company due to two violations, committed by multiple acts, of voting rights notification requirements under sections 33 and 34 of the Securities Trading Act. The company concerned had failed to issue voting rights notifications within the prescribed period.

In another case, BaFin punished a domestic issuer by imposing an administrative fine of €192,000. The issuer had published an ad hoc disclosure on the successful conclusion of an agreement to acquire another company in contravention of section 15 (1) sentence 1 of the Securities Trading Act, old version. The background to this violation was that the issuer had given itself an invalid self-exemption from the obligation to publish inside information relating to the transaction without undue delay.



**Table 36: Summary of administrative fine proceedings<sup>36</sup> in 2018**

	Proceedings pending at the beginning of 2018	New proceedings initiated in 2018	Proceedings completed by imposing an administrative fine	Highest individual administrative fine imposed (€)	Proceedings discontinued for		Proceedings pending at the end of 2018
					factual or legal reasons	discretionary reasons	
Reporting requirements	9	0	1	20,000	0	3	5
Ad hoc disclosures	83	16	6	192,000	1	7	85
Managers' transactions	6	1	2*	5,325	0	1	4
Market manipulation	32	6	10*	42,000	6	6	16
Notification and publication requirements	445	51	79	1,340,000	16	95	306
Duties to provide information to securities holders	26	0	1	11,300**	6	12	7
Short selling	16	0	4	57,500	0	2	10
Financial reporting requirements	168	46	10	148,500	3	22	179
Prospectuses (Securities Prospectus Act/ Capital Investment Act)	30	2	0	0	0	3	29
Company takeovers (Securities Acquisition and Takeover Act)	10	5	2	9,000	0	2	11
Other	10	5	3	9,750	0	2	10

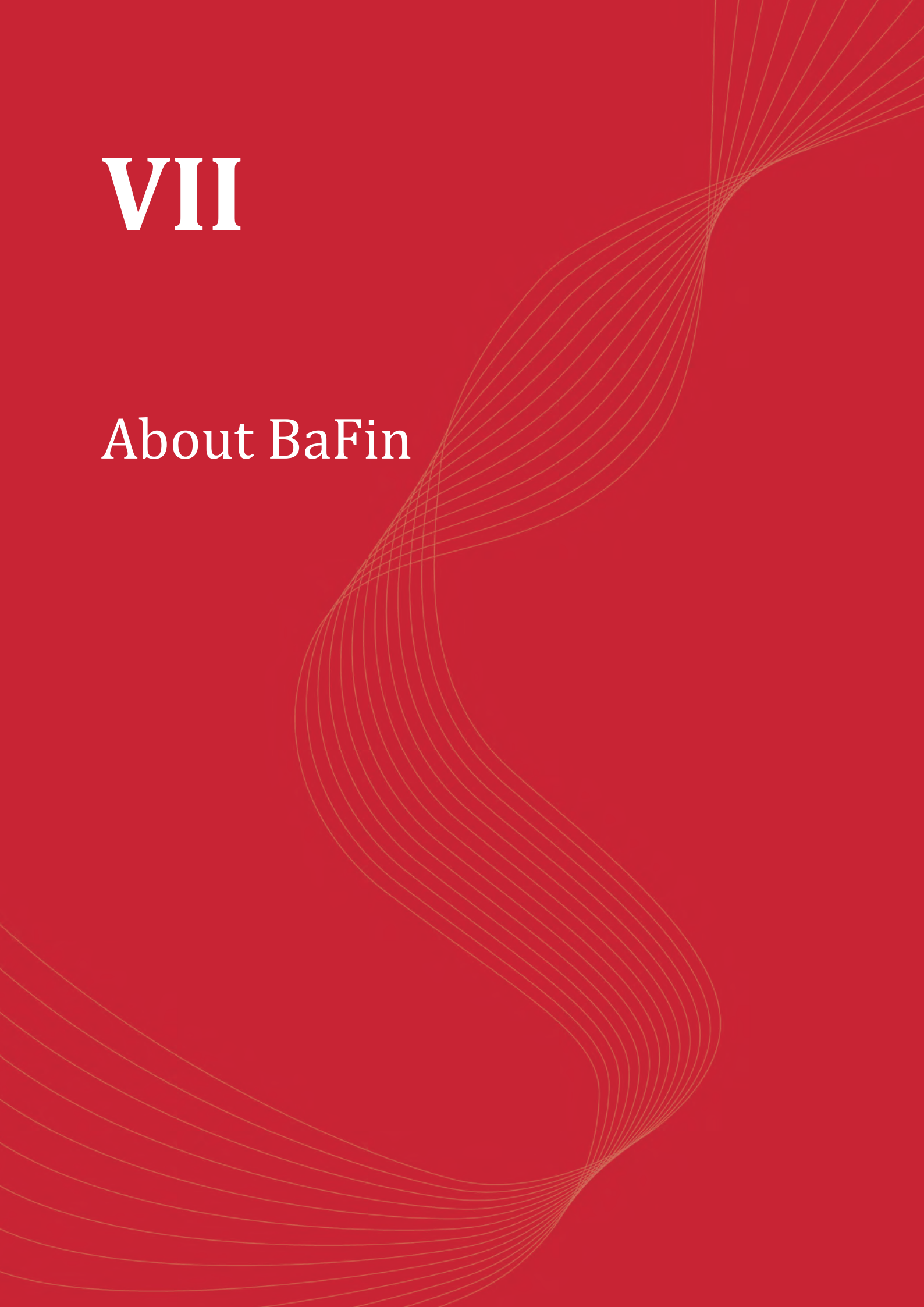
\* Includes 1 case that led to the conviction of the individual concerned in criminal proceedings. Also includes an assessment of life circumstances in the determination of the administrative fine.

\*\* The administrative fine was imposed due to a breach of the duty of oversight for this and other violations.

<sup>36</sup> The figures quoted refer to the aggregate of all administrative fine proceedings pursued in Securities Supervision.

# VII

## About BaFin



# 1 Human resources

As at 31 December 2018, a total of 2,713 employees (previous year: 2,602 employees) worked at BaFin's offices in Bonn (1,895 employees) and Frankfurt am Main (818 employees). Approximately 75% (2,026 employees) were civil servants (*Beamte*) and approximately 25% (687 persons) were public service employees covered by collective wage agreements (*Tarifbeschäftigte*) and others not covered by collective wage agreements (see Table 38 "Personnel").

Women represented just under half of BaFin's employees, accounting for 47% (1,282 women). As at 31 December, 75 employees were on long-term assignment to international institutions and supervisory authorities, of whom 39 were working temporarily as delegates to the European Central Bank (ECB).

## A total of 122 new staff recruited

In 2018, BaFin recruited a total of 122 new members of staff, 4 more than in the previous year (see Table 37 "Recruitment in 2018"); this does not include vocational trainees and candidates for entry to the higher intermediate civil service. The majority of the new recruits were economists and fully qualified lawyers, but they also comprised mathematicians and graduates in other disciplines from higher education institutions and universities of applied sciences. BaFin also recruited candidates for entry to the higher intermediate civil service and vocational trainees for the intermediate civil service. A further 82 employees were added to these figures, as BaFin took over the resolution functions of the Federal Agency for Financial Market Stabilisation (FMSA) in 2018.<sup>1</sup>

**Table 37: Recruitment in 2018**

Career level	Total	Female	Male
<b>Higher civil service</b>	67	31	36
Qualifications:			
Fully qualified lawyers	17		
Economists	38		
Mathematicians/ statisticians	7		
Other	5		
<b>Higher intermediate civil service</b>	24	6	18
Qualifications:			
Business lawyers	3		
Economists	19		
Career training	1		
Other	1		
<b>Intermediate/ basic civil service</b>	31	20	11
<b>Candidates for entry to the higher intermediate civil service/ vocational trainees</b>	11	7	4
<b>Total</b>	<b>122*</b>	<b>57*</b>	<b>65*</b>

\* Excluding candidates for entry to the higher intermediate civil service/ vocational trainees.

## Career entry at BaFin

Those starting their careers at BaFin may undergo preparation for the higher intermediate civil service and complete vocational training in the intermediate civil service, among other options. At the end of 2018,

**Table 38: Personnel**

As at 31 December 2018

Career level	Employees			of which	of which public
	Total	Female	Male	civil servants	service employees
<b>Higher civil service</b>	1,344	554	790	1,186	158*
<b>Higher intermediate civil service</b>	819	358	461	686	133
<b>Intermediate/basic civil service</b>	550	370	180	154	396
<b>Total</b>	<b>2,713</b>	<b>1,282</b>	<b>1,431</b>	<b>2,026</b>	<b>687*</b>

\* Including those employees not covered by collective wage agreements.

<sup>1</sup> See 2017 Annual Report, page 164.

BaFin employed a total of 35 candidates for entry to the higher intermediate civil service and vocational trainees, compared with 43 in the previous year.

As at 31 December, 14 of the candidates for entry to the higher intermediate civil service (previous year: 18) were enrolled as students on the “Central Banking” degree programme offered by the Deutsche Bundesbank University, and two more on the information technology for public administration degree programme at the Federal University of Applied Administrative Sciences. As in the previous year, five students out of this group began their studies during the year under review.

Five trainees began their vocational training in 2018 (previous year: nine trainees). At the end of 2018, BaFin had completed training for a total of 19 vocational trainees (previous year: 24 trainees) in the following four career profiles: administration specialists, IT specialists for system integration, business administration specialists for office management and media and information services specialists, specialising in librarianship.

### **Expertise through CPD**

BaFin attaches great importance to broadening and further developing its employees’ knowledge and skills and keeping them up-to-date on an ongoing basis. In 2018, BaFin employees took part in 693 continuing professional development (CPD) events (previous year: 656 events). The total number of attendances at such events in 2018 was 4,602 (previous year: 4,029 attendances). On average, each BaFin employee therefore attended a CPD session on 2.8 days (previous year: 3.0 days).

Whether for beginners, more advanced participants or experts: BaFin provides CPD sessions for its employees in a wide range of specialist areas to strengthen their expertise and soft skills. Joint training initiatives, in particular with the Deutsche Bundesbank, the ECB and the European Supervisory Authorities (ESAs), promote closer collaboration and more effective international networking.

## **2 Budget**

BaFin’s Administrative Council approved a budget of €345 million for 2018. The budget was therefore around €60 million higher than in 2017 (€285.5 million).

The increase was mostly caused by the integration of functions and personnel of the FMSA into BaFin as at 1 January 2018.<sup>2</sup>

Personnel expenses accounted for 67.7% of the projected expenditure (€233.3 million; previous year: €209.3 million) and non-staff costs for 26.3% (€90.7 million; previous year: €63.5 million). Capital expenditure represented 3.6% of the budget (previous year: 2.2%). Cost reimbursements and grants were virtually unchanged from the previous year’s level at 2.4% of the budget (see Figure 22 “2018 budget expenditure” on page 157).

### **Financing through cost allocations and fees**

BaFin is independent of the federal budget and is fully self-financed from its own income. The largest proportion of this in the 2018 budget was attributable to cost allocations levied on the supervised undertakings, a special levy with a financing function. The projected figure for cost allocations in 2018 amounted to €310.3 million (previous year: €260.6 million). BaFin also generates administrative income such as fees and interest. The projected figure for these items in 2018 amounted to €34.7 million (previous year: €24.9 million) (see Figure 23 “2018 budget income” on page 157).

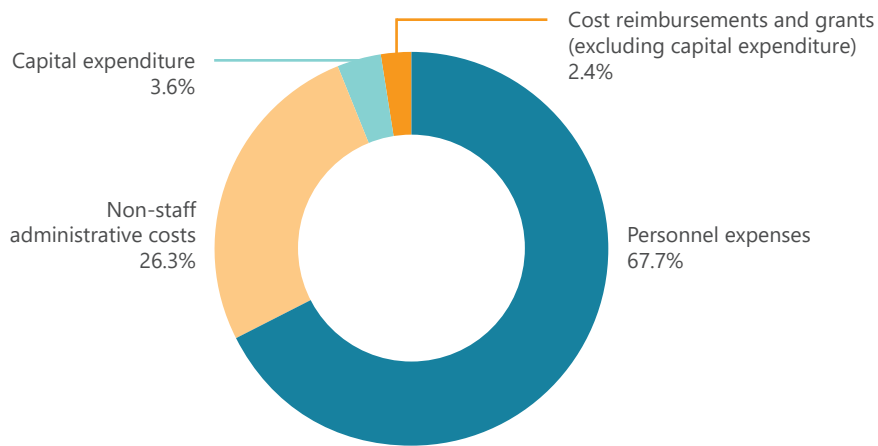
The final cost allocation for 2017 was performed in 2018. It showed that the banking industry accounted for 45.3% of the total income from cost allocations in 2017. The insurance sector contributed 27.0% and securities trading 27.7% (see Figure 24 “Cost allocations by supervisory area in 2017” on page 157). BaFin accounted for the 2017 cost allocation for the national resolution authority separately in 2018, since in 2017 this area formed part of the FMSA. For this purpose, it included the advance payments made to the FMSA. The final cost allocation for 2018 will take place during 2019.

### **Actual expenditure and income**

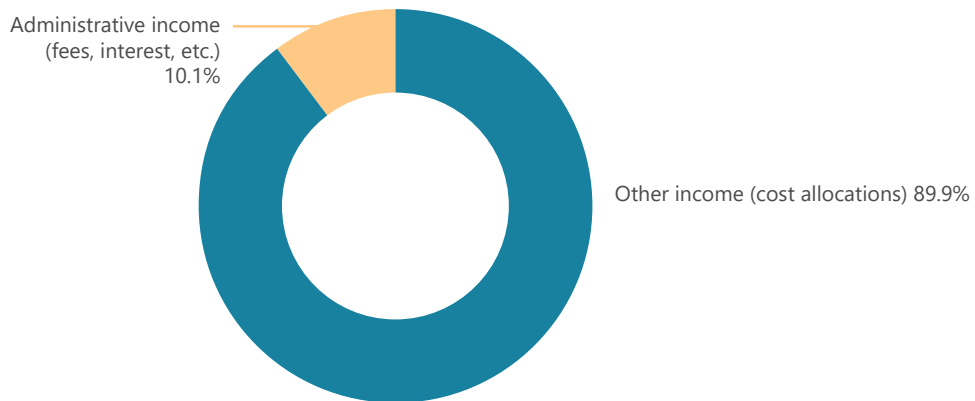
BaFin’s actual expenditure in 2018 was approximately €320.5 million (previous year: €279 million). This is around €24.5 million less than the figure reported in the budget. It was set against income of around €331.3 million (previous year: €282.5 million). BaFin’s Administrative Council had not yet approved the 2018 annual financial statements at the time this report went to press.

<sup>2</sup> See the German Act for the Reorganisation of the Functions of the Financial Market Stabilisation Agency (*Gesetz zur Neuordnung der Aufgaben der Bundesanstalt für Finanzmarktstabilisierung*).

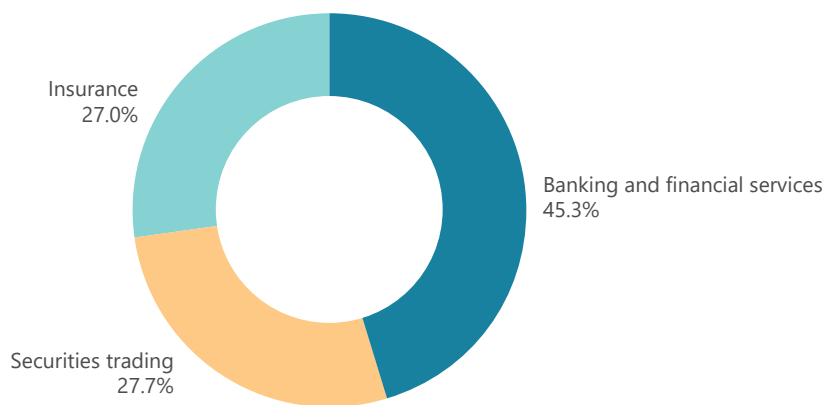
**Figure 22: 2018 budget expenditure**



**Figure 23: 2018 budget income**



**Figure 24: Cost allocations by supervisory area in 2017**



### Separate enforcement budget

BaFin drew up a separate enforcement budget totalling €8.3 million in 2018, roughly equal to the prior-year figure of €8.2 million. This included a planned cost reimbursement to the German Financial Reporting Enforcement Panel (*Deutsche Prüfstelle für Rechnungslegung*) amounting to €6 million (previous year: €6 million). Actual expenditure on enforcement amounted to around €8 million (previous year: €7.9 million), while income – including advance cost allocation payments for 2019 – amounted in total to approximately €14.7 million (previous year: €16.5 million).

## 3 E-government: BaFin's digitalisation strategy

The digital transformation poses new challenges for financial supervision, since it is important to shape these far-reaching changes and establish regulations for digital financial supervision that are fit for the future. In 2018, BaFin therefore drew up a digitalisation strategy covering all sectors which is directed towards the specific responsibilities and requirements of supervisors.

However, in many areas financial supervisors have already been thinking and working in digital terms to a large extent for quite some time. The strategy therefore firstly documents the current status of projects that have already been implemented. But it also highlights crucial decisions for the future. BaFin has identified three fields of action in its digitalisation strategy: "Supervision and regulation", "IT supervision and security" and "Transformation of BaFin", which refers to internal digitalisation. The strategy establishes primary objectives for each of the three fields of action and defines the proposed next steps.

### Basic issues for the fields of action

In the first field of action, BaFin is confronting the following basic issue: What should the supervisory and regulatory response be to the market changes triggered by digitalisation? The basic issue for the second field of action is how BaFin can ensure that the innovative technologies, IT systems and data used by the supervised undertakings are secure. The third field of action addresses the issue of how BaFin should continue to develop – both internally and at the interfaces with the market – in the light of the ongoing digitalisation process.

### Particular challenge for BaFin

The third field of action, the digital transformation of BaFin, presents a particular challenge for the Supervisory Authority: Public-sector administrative authorities are less able to respond flexibly to technical innovations such as digitalisation than private-sector organisations. This is an inevitable consequence of the nature of their organisation and method of functioning as well as the legal framework to which they are subject.

This makes it all the more important, in BaFin's view, to plan and support the process of digital transformation centrally, and to manage the resulting additional responsibilities and projects in an effective and efficient manner. It created the position of a Chief Digital Officer (CDO) in 2018 for this purpose. The CDO will be assisted by a Digital Office. The internal digitalisation of BaFin, and therefore the CDO as the implementing officer, will contribute to making BaFin's supervisory and support processes largely paperless and more efficient across all sectors. These innovations will also enable BaFin to develop appropriate new supervisory instruments and solutions.<sup>3</sup>

## 4 Communications

### 4.1 Press enquiries

In 2018, BaFin again received several thousand enquiries from journalists relating to the different areas of responsibility of the Supervisory Authority.

### Money laundering prevention

For example, a number of international cases of money laundering involving banks – including Danske Bank and ING – resulted in a sharp increase in interest on the part of the media in the topic of money laundering prevention. Journalists wanted to know, for example, what BaFin's responsibilities and powers were in this area and the specific nature of the detailed regulations. They also obtained explanations of BaFin's position on the possible Europeanisation of anti-money-laundering supervision. There was also considerable interest in the fact that BaFin had ordered preventive measures against money laundering and terrorist financing to be taken at Deutsche Bank and appointed a special representative<sup>4</sup>.

<sup>3</sup> On the "Supervision and regulation" and "IT supervision and security" fields of action, see also chapter II .6

<sup>4</sup> See chapter II 5.2.

### Initial coin offerings (ICOs)

The media were again concerned with the topic of initial coin offerings (ICOs) in 2018. The main question was the extent to which the issue or public offering of crypto tokens triggered authorisation or prospectus requirements.

### Brexit

Many journalists sought information on the exit of the United Kingdom from the European Union. Among other things, they asked which financial institutions were intending to relocate to Germany so that they could then use their passporting rights from here. The supervisory requirements for the institutions were also a subject of interest.

### Digitalisation

Many enquiries related to the ways in which digitalisation is affecting the supervisory authorities and the business activities of the banks in particular. The questions focused firstly on competition from technology groups which also offer banking services, and secondly on the IT capabilities of the banks and the security of their IT systems. In many cases, journalists also sought information on the supervisory requirements for outsourcing to cloud service providers and on the responsibilities of a chief information officer.

### Run-off

External run-off returned as a central topic of interest for the media as a result of the planned sale of Generali Lebensversicherung AG to the Viridium Group. Journalists were particularly interested in the length, content and applicable standards of BaFin's examination of the sale. BaFin's press release<sup>5</sup> made it clear that the sale of an insurance undertaking is subject to strict requirements which are aimed at safeguarding the interests of the policyholders. After all, the sale of an undertaking is not allowed to leave the policyholders in a worse position.

### Pensionskassen

Following BaFin's warning that without additional capital a number of *Pensionskassen* might no longer be able to meet their benefit commitments in full<sup>6</sup>, the media increasingly focused on their situation. They were particularly interested in the financial position of the funds and the question of what supervisory measures BaFin was planning or had already taken – especially in relation to more intensive supervision. At

the start of December, the situation of the *Pensionskasse* of Caritas VVaG was the subject of numerous press enquiries. BaFin had previously published its order to the fund forbidding it to take on new business.<sup>7</sup>

### Cap on commissions and ban on sharing commissions

Another important topic in the media consisted of the implementation and interpretation of the EU Insurance Distribution Directive (IDD). BaFin confirmed in the spring that it was considering introducing guideline standard commissions in the life insurance sector to avoid inappropriate incentives in commission-based distribution. Since then, the Federal Ministry of Finance has announced a statutory cap on commissions. Journalists were also interested in compliance with the ban on the sharing of commissions. The case of gonetto GmbH and the anniversary promotion by Check24 also attracted particular attention.

### Validity of premium adjustments

A number of press enquiries centred on the ongoing judicial proceedings on the legal validity of premium adjustments in private health insurance where there is a lack of economic independence on the part of the trustees. An oral hearing was held on this issue before the Federal Court of Justice (*Bundesgerichtshof* – BGH) on 19 December 2018. On 19 December 2018, the BGH confirmed BaFin's interpretation of the law. The fact that trustees frequently work closely together with insurers over long periods of time, and receive payment from them, did not of itself constitute grounds for declaring premium increases to be invalid.

### Insolvency of P&R

BaFin received numerous enquiries on the insolvency of the P&R group of companies. The group had been offering direct investments in containers. Journalists were primarily interested in the obligation to publish a prospectus and BaFin's responsibilities, as well as in direct investment as an investment model. Many questions also related to the authorisation requirements and the competencies and powers of the Supervisory Authority. None of the companies in the P&R Group were subject to ongoing supervision by BaFin, however.

### MiFID II

The provisions of the second Markets in Financial Instruments Directive (MiFID II) were the focus of media attention again in 2018. The main subjects of interest were the suitability assessment and the new record-keeping obligations. In contrast to the

<sup>5</sup> [www.bafin.de/dok/11121600](http://www.bafin.de/dok/11121600).

<sup>6</sup> See [www.bafin.de/dok/11116514](http://www.bafin.de/dok/11116514).

<sup>7</sup> [www.bafin.de/dok/11766868](http://www.bafin.de/dok/11766868) (only available in German).

investment advice minutes required in the past which had to record all matters discussed in the investment consultation, the statement on suitability is restricted to the reasons for the suitability of the recommendations made in the consultation. But the record-keeping requirements of investment firms cover more than the statement on suitability. If clients give an order to their adviser subsequent to receiving advice, the time and place of the meeting, the individuals in attendance, the initiator of the meeting and information on the order itself have to be documented. Customers can ask for the documentation to be provided to them. The undertakings can also combine the information with the contents of the statement on suitability.

## 4.2 Events and trade fairs

### **Fintech conference “BaFin-Tech”**

On 10 April 2018, BaFin held its second Fintech conference “BaFin-Tech”. Both new and established undertakings from the financial services industry were invited. Developments in financial technology and discussions with guests from the business world, academia and politics took centre stage at the event. Participants also had the opportunity to join workshops on the topics of cloud computing, big data, artificial intelligence and platformification.

### **Forum on “White-collar Crime and the Capital Market”**

On 19 and 20 September 2018, BaFin hosted its annual forum on “White-Collar Crime and the Capital Market” for the 15th time. Around 350 representatives of the police and the public prosecutor’s office, as well as of the Deutsche Bundesbank, stock exchange supervisory authorities, trading surveillance offices of stock exchanges and foreign supervisory authorities were invited as guests. The participants also had the opportunity to attend seminars, such as those on national risk analysis and the compliance function.

### **Workshop on “IT Supervision in the Banking Sector”**

On 27 September 2018, representatives of the finance industry and IT security experts gathered at BaFin’s invitation for its fifth workshop on “IT Supervision in the Banking Sector”. Around 400 participants brought themselves up-to-date on current issues affecting the digital financial world. Central topics were the Supervisory Requirements for IT in Financial Institutions (*Bankaufsichtliche Anforderungen an die IT – BAIT*) and the supervision of security in payment transactions under the German Payment Services Supervision Act (*Zahlungsdienststeuergesetz*).

### **Resolution conference**

On 30 October 2018, BaFin held its first resolution conference for representatives of credit institutions and their industry associations. The speakers provided the approximately 180 participants with information about resolution planning, resolution strategies for specific institutions and current developments relating to the bank levy, among other topics. A panel discussion with representatives from business, administration and academia addressed the topic “The resolvable bank – utopia or reality?”

### **Information for investors at trade fairs and events**

In April 2018, BaFin took part in the “Invest” trade fair in Stuttgart, providing information covering a wide range of subjects. Representatives of the Supervisory Authority gave a number of talks informing investors about the most important changes resulting from MiFID II, among other things, and explained the most frequent misconceptions relating to price determination and market-making for certificates and warrants.

BaFin was also represented at the investor fairs in Berlin, Dresden, Düsseldorf, Munich and Hamburg in 2018, as well as at the Federal Ministry of Finance’s open house in Berlin and the German Senior Citizens’ Day organised by the German National Association of Senior Citizens Organisations in Dortmund. Many attendees at these events took the opportunity to ask questions of BaFin’s employees directly.

## 4.3 Publications

BaFin again issued a number of publications on supervisory and consumer topics at [www.bafin.de](http://www.bafin.de) in 2018. A few examples are described in the following.

### **BaFinPerspectives**

In August, BaFin published the first issue of its BaFinPerspectives series. The issue deals with a variety of perspectives relating to the ongoing digitalisation process, as well as the related topics of big data and artificial intelligence and their implications for the financial markets, supervision and regulation (see info box “BaFin study on Big Data and Artificial Intelligence” on page 161). The second issue of BaFinPerspectives appeared on 28 February 2019. It is also dedicated to the topic of digitalisation. The next issue is scheduled for 9 May. It will address the subject of sustainable finance. The BaFinPerspectives series contains contributions from internal and external authors and interviews. The series is published in German and English on BaFin’s homepage.<sup>8</sup>

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<sup>8</sup> [www.bafin.de/dok/11506544](http://www.bafin.de/dok/11506544).



### Brochures and ABCs in simple language

Numerous brochures on topics relevant to consumers can be found on BaFin's home page.<sup>9</sup> At the start of October 2018, BaFin also published two new simple-language brochures which explain important concepts used in the banking<sup>10</sup> and insurance<sup>11</sup> sectors.

### Annual Report and statistics

In addition to its Annual Report<sup>13</sup>, BaFin also published its annual statistics on the status and development of German insurance undertakings<sup>14</sup> and its statistics on reinsurance undertakings<sup>15</sup>. The Annual Report and the reinsurance statistics are also available in English.

#### Note

### BaFin study on Big Data and Artificial Intelligence

What will be the effects of technological developments in data processing and analysis on the finance industry? What implications will emerge for financial stability, the supervision of markets and undertakings and for collective consumer protection? BaFin's report "Big data meets artificial intelligence – Challenges and implications for the supervision and regulation of financial services"<sup>12</sup>, published in mid-June 2018, makes a contribution to answering these questions.

The report contains the findings of a study on which experts from Partnerschaft Deutschland, the Boston Consulting Group (BCG) and the Fraunhofer Institute for Intelligent Analysis and Information Systems (IAIS) also collaborated.

The objective was to obtain a comprehensive picture to enable BaFin to identify strategic trends, market developments and newly emerging risks at an early stage and to respond appropriately. The report highlights the implications of technology-driven market developments from different regulatory and supervisory perspectives. "The findings clearly show how important it is for us to address these issues from a supervisory and regulatory point of view", commented BaFin President Felix Hufeld.

BaFin submitted the report and the key questions it contains for public consultation. Information on the results of the consultation and an initial analysis by Hufeld can be found in BaFinPerspectives<sup>16</sup> which was published at the end of February 2019 at [www.bafin.de](http://www.bafin.de).

9 [www.bafin.de/dok/8228504](http://www.bafin.de/dok/8228504).

10 [www.bafin.de/dok/11529872](http://www.bafin.de/dok/11529872).

11 [www.bafin.de/dok/11529884](http://www.bafin.de/dok/11529884) (only available in German).

12 [www.bafin.de/dok/11250046](http://www.bafin.de/dok/11250046) (only available in German).

13 [www.bafin.de/dok/8249058](http://www.bafin.de/dok/8249058) (only available in German).

14 [www.bafin.de/dok/7867196](http://www.bafin.de/dok/7867196).

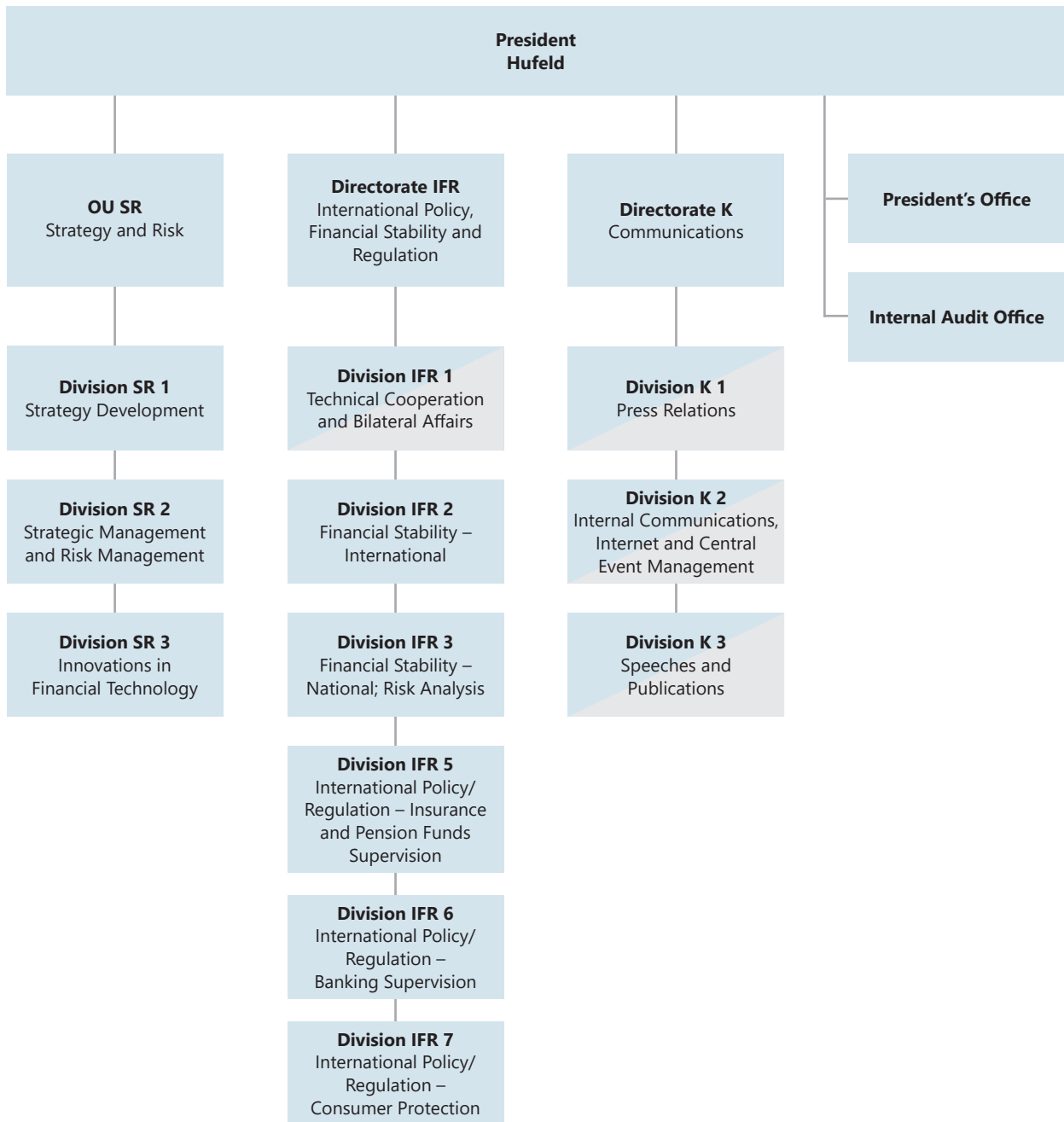
15 [www.bafin.de/dok/8814286](http://www.bafin.de/dok/8814286) (only available in German).

16 [www.bafin.de/dok/12221420](http://www.bafin.de/dok/12221420).



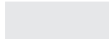

# Appendix



# 1 Organisation chart\*

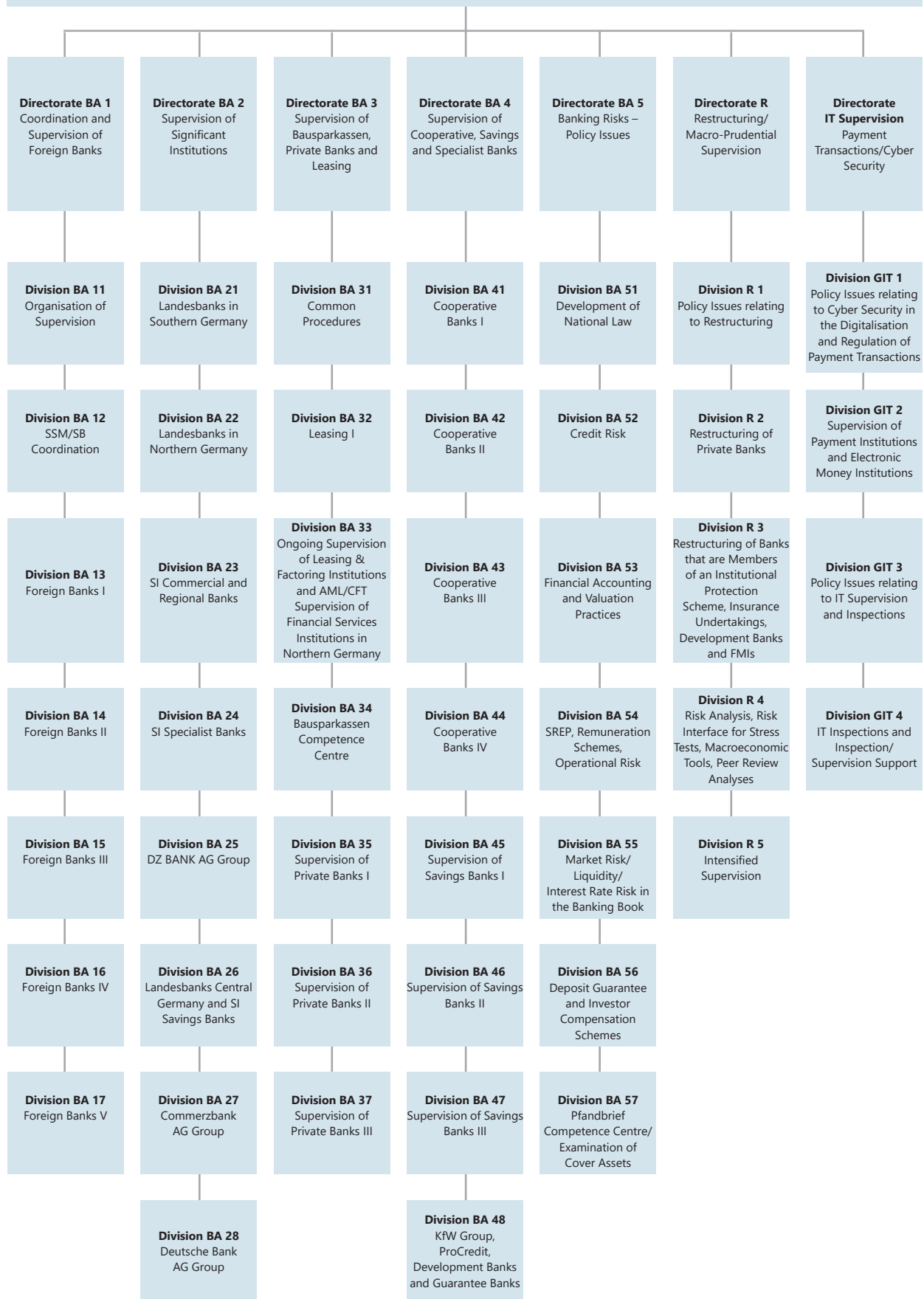


## Notes

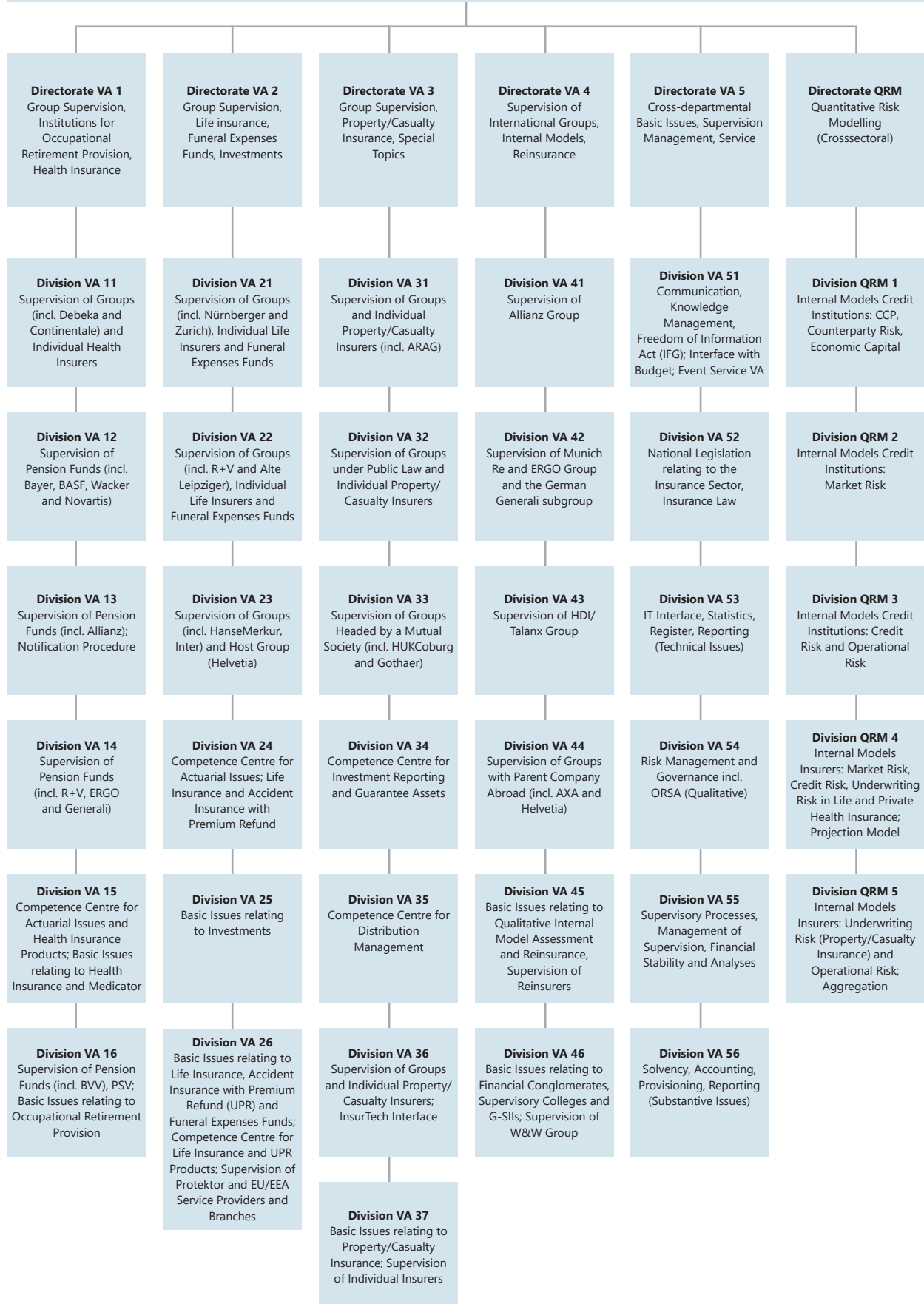
-  Executive Board
-  Bonn office
-  Frankfurt office
-  Offices in Bonn and Frankfurt

\* As at: February 2019

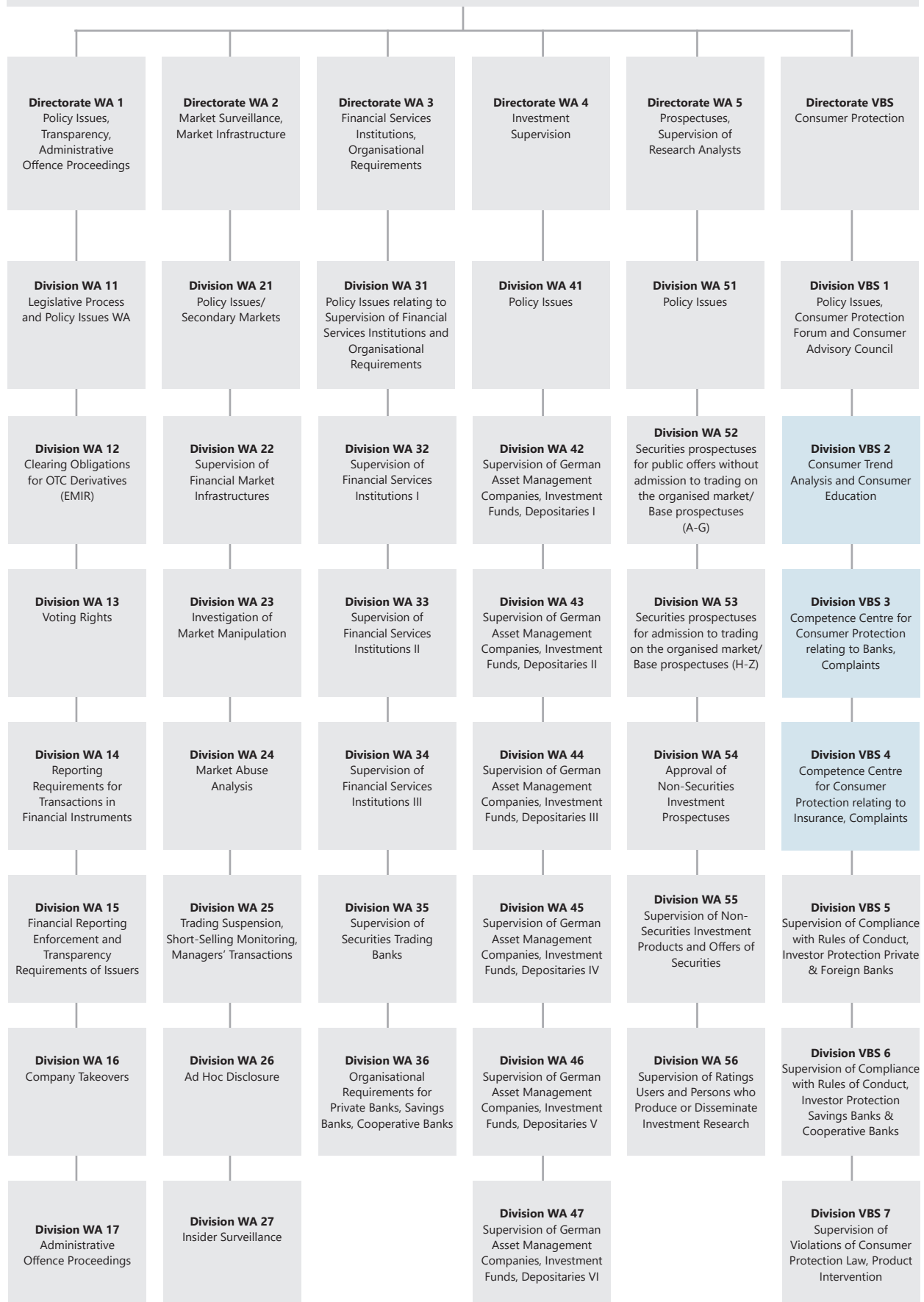
**Banking Supervision**  
Chief Executive Director Röseler



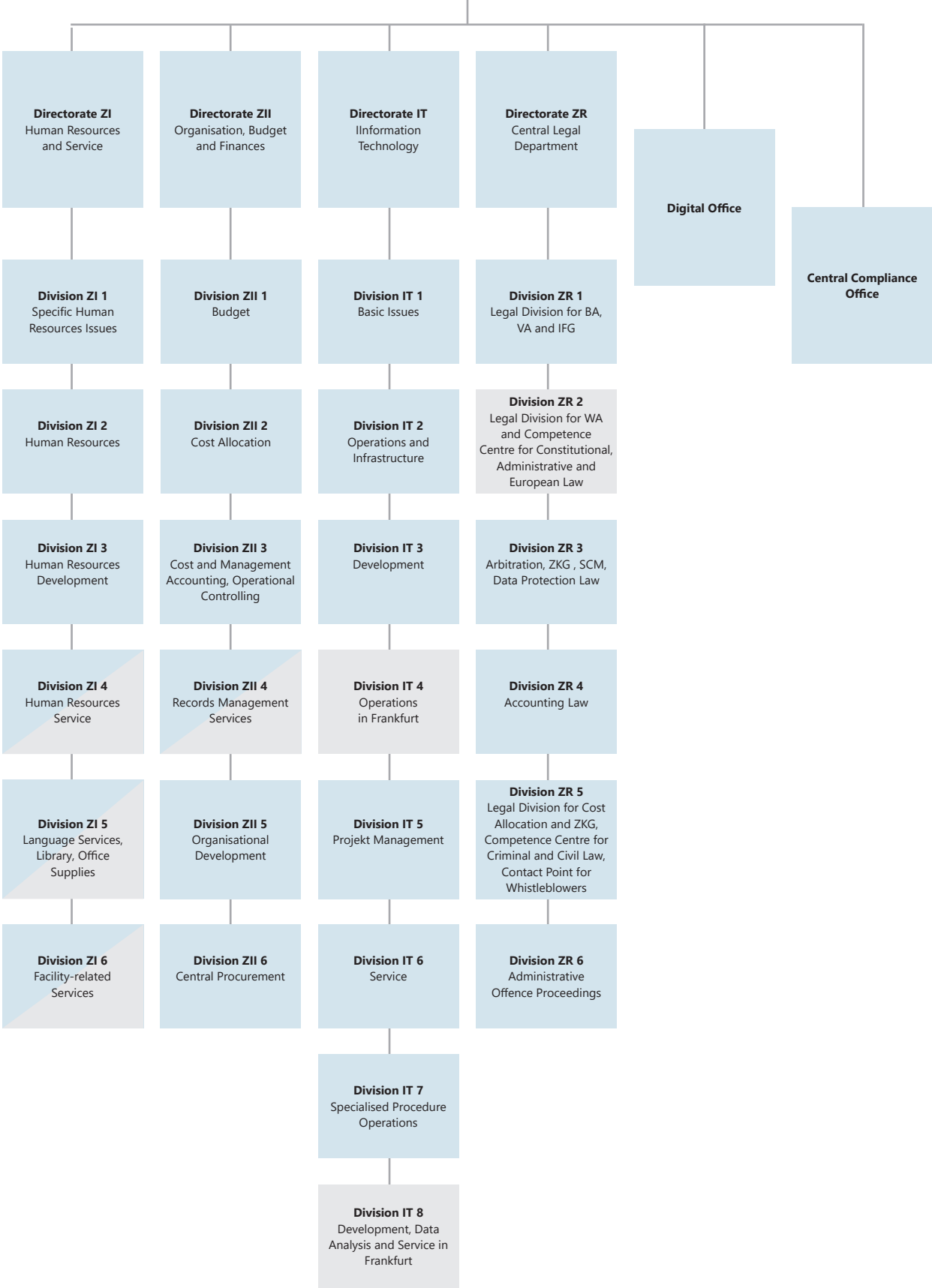
**Insurance and Pension Funds Supervision  
Chief Executive Director Dr Grund**



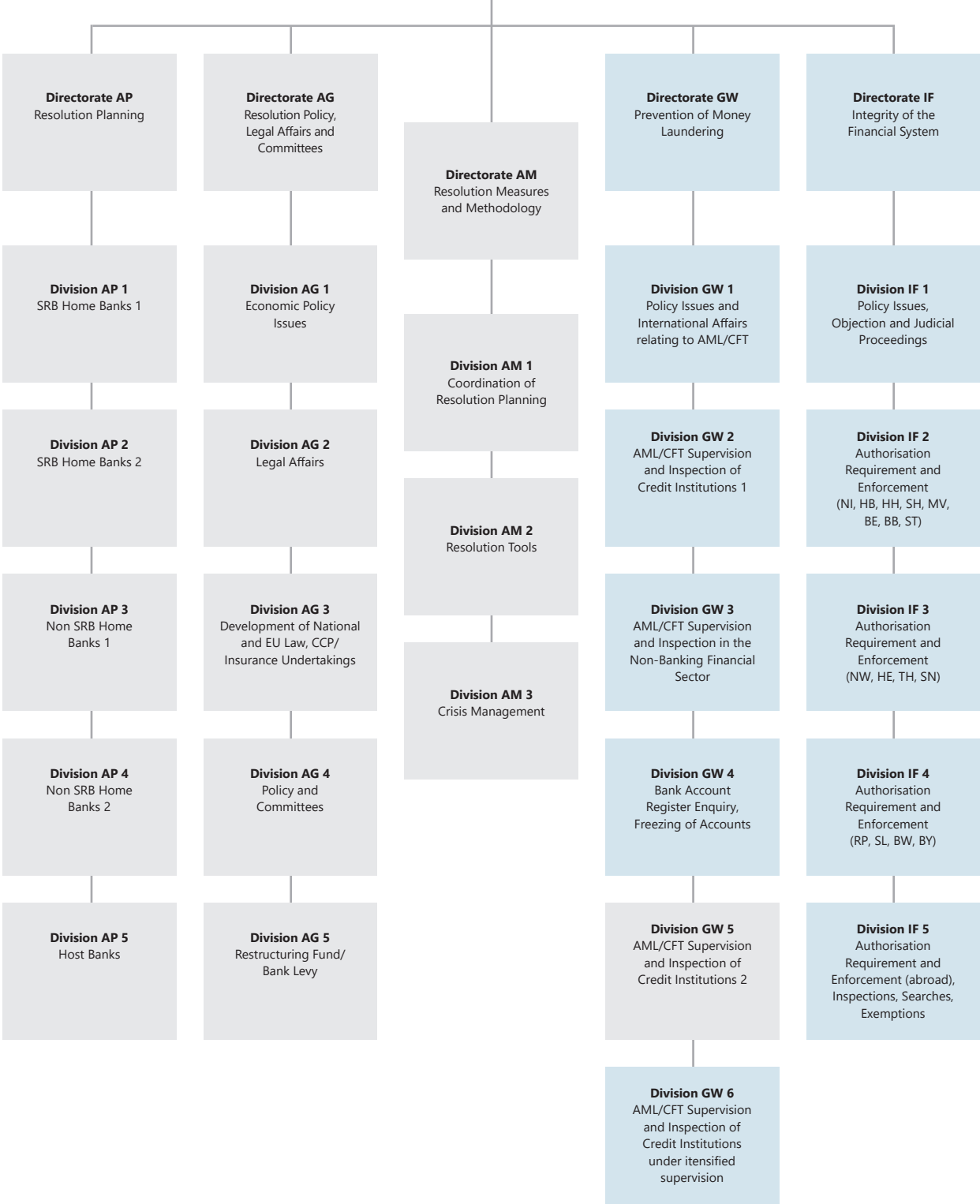
**Securities Supervision/Asset Management  
Chief Executive Director Roegele**



**Internal Administration and Legal Affairs**  
**Chief Executive Director Freiwald**



**Resolution Directorate**  
Chief Executive Director Dr Pötzsch





## 2 BaFin bodies

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Dr Jörg Kukies (Chair – Federal Ministry of Finance)  
Dr Levin Holle (Deputy Chair – Federal Ministry of Finance)  
Dr Eva Wimmer (Federal Ministry of Finance)  
Dr Raphael L’Hoest (Federal Ministry for Economic Affairs and Energy)  
Erich Schaefer (Federal Ministry of Justice and Consumer Protection)  
Helga Springeneer (Federal Ministry of Justice and Consumer Protection)

#### **Representing the Bundestag**

MdB Matthias Hauer  
MdB Alexander Radwan  
MdB Dr Jens Zimmermann  
MdB Prof. Harald Weyel  
MdB Frank Schäffler

#### **Representing the private sector and the academic community**

Dr Christian Ossig (proposed by the credit institutions)  
Dr Jörg von Fürstenwerth (proposed by the insurance undertakings)  
Thomas Richter (proposed by the asset management companies)  
Prof. Isabel Schnabel (representing the academic community)  
Prof. Fred Wagner (representing the academic community)

As at: March 2019

### 2.2 Members of the Advisory Board

#### **Representing credit institutions**

Dr Christian Ossig  
Dr Karl-Peter Schackmann-Fallis  
Gerhard Hofmann  
Dr Oliver Wagner  
Jens Tolckmitt  
Iris Bethge

#### **Representing insurance undertakings**

Dr Wolfgang Weiler (Deputy Chair)  
Dr Jörg Freiherr Frank von Fürstenwerth  
Dr Markus Faulhaber  
Dr Immo Querner

#### **Representing asset management companies**

Rudolf Siebel

#### **Representing the Bundesbank**

Erich Loeper

#### **Representing the Association of Private Health Insurers**

Uwe Laue

#### **Representing the academic community**

Prof. Andreas Hackethal  
Prof. Andreas Richter  
Prof. Isabel Schnabel (Chair)

#### **Representing the Working Group on Occupational Retirement Provision**

– aba –  
Heribert Karch

#### **Representing consumer protection organisations**

Stephan Kühnlenz  
Prof. Günter Hirsch  
Dr h.c. Hans-Joachim Bauer

#### **Representing the liberal professions**

Frank Rottenbacher

#### **Representing associations for SMEs**

Ralf Frank

#### **Representing the trade unions**

Leonhard Regneri

#### **Representing industry**

Ralf Brunkow

As at: March 2018

## 2.3 Members of the Insurance Advisory Council

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Dr Karin Becker

Dr Frank Ellenbürger

Christian J. Fuchs

Prof. Nadine Gatzert

Prof. Helmut Gründl

Martina Grundler

Prof. Maria Heep-Altiner

Jörg F. Henne

Burkhard Keese

Dr Mathias Kleuker

Sandra Klug

Uwe Laue

Katharina Lawrence

Hubertus Münster

Ute Pesch

Dr Michael Pickel

Dr Claudia Picker

Prof. Petra Pohlmann

Dr Markus Rieß

Holger R. Rohde

Prof. Heinrich R. Schradin

Hermann-Josef Tenhagen

Prof. Manfred Wandt

As at: 31 December 2018

## 2.4 Members of the Securities Council

Baden-Württemberg Ministry of Economic Affairs,  
Labour and Housing

Bavarian Ministry of Economic Affairs, Regional  
Development and Energy

Berlin Senate Department for Economics, Energy  
and Public Enterprise

The Ministry for Economic Affairs and Energy  
of the State of Brandenburg

Free Hanseatic City of Bremen, Senator for Economic  
Affairs, Labour and Ports

Free and Hanseatic City of Hamburg, Ministry of Finance

Ministry of Economics, Energy, Transport and Regional  
Development of the State of Hesse

Ministry of Economics, Employment and Health of the  
State of Mecklenburg-Western Pomerania

Ministry of Economic Affairs, Employment, Transport  
and Digitalisation of the State of Lower Saxony

Ministry of Finance of the State of  
North Rhine-Westphalia

Ministry for Economics, Transport, Agriculture and  
Viculture of the State of Rhineland-Palatinate

Ministry of Finance of the State of Rhineland-Palatinate

Ministry for Economic Affairs, Labour, Energy and  
Transport of the State of Saarland

Ministry for Economic Affairs, Labour and Transport  
of the State of Saxony

Ministry of Economy, Science and Digitalisation  
of the State of Saxony-Anhalt

Ministry of Finance of the State of Schleswig-Holstein

Ministry of Finance of the State of Thuringia

As at: April 2018

## 2.5 Members of the Consumer Advisory Council

### **Representing the academic community**

Prof. Christoph Brömmelmeyer  
Prof. Petra Buck-Heeb  
Prof. Peter Rott

### **Representing consumer and investor protection organisations**

Jella Benner-Heinacher  
Andrea Heyer  
Stephan Kühnlitz  
Dorothea Mohn (Chair)

### **Representing out-of-court dispute settlement systems**

Dr Peter Frellesen  
Prof. Günter Hirsch (successor from 1 April 2019: Dr h.c. Wilhelm Schluckebier)  
Gabriele Meister

### **Representing the Federal Ministry of Justice and Consumer Protection**

Dr Erich Paetz

### **Representing the trade unions**

Maximilian Fuhrmann

As at: March 2018

### 3 Authorised credit institutions, insurers and *Pensionsfonds*

#### 3.1 Credit institutions supervised by BaFin or the ECB

##### 3.1.1 Authorised institutions

In 2018 BaFin was responsible for supervising a total of 1,533 German credit institutions (previous year: 1,577) and 47 housing enterprises with savings schemes (previous year: 47, see Table 39).

Of the total of 1,533 credit institutions, 1,470 were CRR credit institutions (previous year: 1,522). Of these 1,470 CRR credit institutions, 1,409 (previous year: 1,457) were subject to direct supervision by BaFin as less significant institutions (LSIs) under the Single Supervisory Mechanism (SSM) (see info box “Definition Credit institution or not?”). The 33 securities trading banks, 30 other credit institutions and 47 housing enterprises with savings schemes also referred to in Table 39 are supervised exclusively by BaFin.

##### 3.1.2 German institutions directly supervised by the ECB under the SSM

59 of the German CRR credit institutions referred to in Table 39 (previous year: 63) were directly supervised by the European Central Bank (ECB) in 2018 as significant institutions (SIs) under the SSM (see Table 32). BaFin is involved in their supervision as part of the SSM.

**Table 39: German institutions**

As at 31 December 2018

	1,470
CRR credit institutions*	of which SIs** 59
	of which LSIs*** 1,409
Securities trading banks	33
Other credit institutions	30
<b>Total credit institutions</b>	<b>1,533</b>
<b>Housing enterprises with savings schemes</b>	<b>47</b>

\* Two of these CRR credit institutions are neither SIs nor LSIs.

\*\* The SIs are supervised directly by the ECB.

\*\*\* Two of these credit institutions provide financial market infrastructures and are therefore supervised by BaFin’s Securities Supervision Sector.

#### Definition

#### Credit institution or not?

A **credit institution** is an undertaking which conducts at least one of the types of banking businesses described in detail in section 1 (1) of the German Banking Act (*Kreditwesengesetz*) commercially or on a scale which requires commercially organised business operations. Banking business includes the deposit business and credit business, but also specific securities-related activities such as principal broking services and the safe custody business.

Pursuant to section 1 (3d) of the Banking Act, a **CRR credit institution** is a credit institution that also meets the narrower definition of a credit institution in accordance with Article 4 (1) no. 1 of the EU Capital Requirements Regulation (CRR) and is engaged in the deposit and credit businesses. CRR credit institutions are supervised in the context of the Single Supervisory Mechanism (SSM) either

directly by the ECB as significant institutions (SIs) or by BaFin together with the Deutsche Bundesbank as less significant institutions (LSIs).

While the **securities trading banks** and the other credit institutions are not CRR institutions, they nevertheless fall within the German definition of a credit institution.

In accordance with section 1 (29) of the Banking Act, **housing enterprises with savings schemes** are undertakings with the legal form of a registered cooperative society, whose business object is principally the management of their own housing portfolios and which also conduct banking business solely in the form of deposit business, in a manner restricted by law. They have not been included in the credit institutions in this table.

**Table 40: German institutions supervised by the ECB under the SSM**

As at 31 December 2018

Aareal Bank AG	Hanseatic Bank GmbH & Co KG
Bausparkasse Schwäbisch Hall Aktiengesellschaft, Bausparkasse der Volksbanken und Raiffeisenbanken	ING-DiBa AG
Bayerische Landesbank	Landesbank Baden-Württemberg
Berlin Hyp AG	Landesbank Berlin AG
Bethmann Bank AG	Landesbank Hessen-Thüringen Girozentrale
BHW Bausparkasse Aktiengesellschaft	Landeskreditbank Baden-Württemberg – Förderbank –
comdirect bank Aktiengesellschaft	Landwirtschaftliche Rentenbank
COMMERZBANK Aktiengesellschaft	Merck Finck Privatbankiers AG
CreditPlus Bank Aktiengesellschaft	MKB Mittelrheinische Bank Gesellschaft mit beschränkter Haftung
DB Investment Services GmbH	Münchener Hypothekenbank eG
DB Privat- und Firmenkundenbank AG	NATIXIS Pfandbriefbank AG
DekaBank Deutsche Girozentrale	Norddeutsche Landesbank – Girozentrale –
DEUTSCHE APOTHEKER- UND ÄRZTEBANK EG	norisbank GmbH
DEUTSCHE BANK AKTIENGESELLSCHAFT	NRW.BANK
Deutsche Bank Bauspar-Aktiengesellschaft	Opel Bank GmbH
Deutsche Bank Europe GmbH	PSA Bank Deutschland GmbH
Deutsche Hypothekenbank (Actien-Gesellschaft)	S Broker AG & Co. KG
Deutsche Kreditbank Aktiengesellschaft	Sal. Oppenheim jr. & Cie. AG & Co. Kommanditgesellschaft auf Aktien
Deutsche Pfandbriefbank AG	Santander Consumer Bank Aktiengesellschaft
Dexia Kommunalbank Deutschland GmbH	Sparkasse Mittelholstein Aktiengesellschaft
DSK Hyp AG*	Start:bausparkasse AG***
DVB Bank SE	State Street Bank International GmbH
DZ BANK AG Deutsche Zentral-Genossenschaftsbank, Frankfurt am Main	TARGOBANK AG
DZ HYP AG	TeamBann.a.Nürnberg
European Bank for Financial Services GmbH (ebase)	UniCredit Bank AG
FIDOR Bank AG	Volkswagen Bank Gesellschaft mit beschränkter Haftung
Frankfurter Bankgesellschaft (Deutschland) AG	VON ESSEN Bank GmbH
Frankfurter Sparkasse	VR DISKONTBANK GmbH
GEFA BANK GmbH	Previous name:
Hamburg Commercial Bank AG**	* SEB AG
Hamburger Sparkasse AG	** HSH Nordbank AG
	*** Deutscher Ring Bausparkasse Aktiengesellschaft

### 3.1.3 Calculation of the capital requirements

#### Use of IRB Approaches

As at the 31 December 2018 reporting date, a total of 12 less significant institutions and groups of institutions and 1 development bank were using internal ratings-based (IRB) approaches to calculate their capital requirements for credit risk. These institutions and groups of institutions and the development bank under supervision did not apply the internal assessment approach (IAA) for securitisation positions, however.

The IRB approach makes a distinction between whether, beyond its retail business, an institution estimates only the probability of default (foundation IRB approach) itself or whether it also estimates the loss given default and the conversion factor (advanced IRB approach). A total of 4 of these 12 institutions and groups of institutions and the development bank used the advanced IRB approach on a group or individual basis, and 3 institutions applied the IRB approach on an individual basis exclusively for the risk positions arising from their retail business.

#### Operational risk approaches

The German institutions or groups of institutions in Germany employ all four available approaches to calculate their capital requirements for operational risk. The basic indicator approach (BIA) and the standardised approach (STA) are determined using the specified indicator, which is based on income statement figures.

At the 2018 year-end, more than 1,400 institutions and groups of institutions – almost exclusively LSIs – were using the basic indicator approach. Another 46 institutions or groups of institutions, of which 23 are supervised by the ECB and 23 directly by BaFin, were applying the standardised approach. Two institutions or groups of institutions were working with the alternative standardised approach (ASA), which uses a standardised earnings indicator instead of the specified indicator. BaFin is responsible for these institutions.

The advanced measurement approach (AMA) does not make use of indicators, but uses the institution's own actual loss experience, external data, scenarios as well as business environment and internal control factors.

The capital requirement for the operational risk of an institution or a group of institutions is calculated on the basis of this information with the help of a complex model. At the close of 2018, a total of 13 institutions and groups of institutions with operations in Germany, of which 6 were German and 7 foreign institutions, were applying the AMA. Of the German institutions, four are supervised by the ECB and 2 by BaFin. Of the foreign institutions, 6 are supervised by the ECB and 1 by BaFin.

Following the publication of the revised framework for determining operational risk by the Basel Committee in December 2017, it will probably no longer be possible to use a model-based approach for Pillar I purposes from 2022 onwards. However, BaFin expects that model-based approaches will continue to be important for determining economic capital, especially for significant institutions, beyond 2022. Moreover, the AMA will be the legal reality for at least another three years. For those reasons, BaFin once again insisted on necessary model improvements and modifications under the AMA in 2018.

As in previous years, BaFin focused on the procedures for measuring, controlling and monitoring legal risks and IT risks. IT risks in particular have grown in significance and will become increasingly significant over the next few years.

## 3.2 Insurance undertakings and *Pensionsfonds* under BaFin's supervision

### 3.2.1 Authorised insurance undertakings and *Pensionsfonds*

The number of insurance undertakings supervised by BaFin declined slightly in 2018, while the number of *Pensionsfonds* rose slightly. At the end of the year under review, BaFin supervised a total of 550 insurance undertakings (previous year: 552) and 33 *Pensionsfonds* (previous year: 31). Out of the total number of insurers, 528 were engaged in business activities and 22 were not. In order to give as full a picture as possible of the insurance market in Germany, all of the information in this chapter also includes 8 public-law insurance undertakings supervised by the federal states. The breakdown of the undertakings by insurance class is therefore as follows (see Table 41 on page 175):

**Table 41: Number of supervised insurance undertakings and *Pensionsfonds*\***

As at 31 December 2018

	Insurance undertakings with business activities			Insurance undertakings without business activities		
	BaFin supervision	Federal states supervision	Total	BaFin supervision	Federal states supervision	Total
Life insurers	85	2	87	9	0	9
<i>Pensionskassen</i>	136	0	136	3	0	3
Funeral expenses funds	33	0	33	1	0	1
Health insurers	46	0	46	0	0	0
Property/casualty insurers	199	6	205	7	0	7
Reinsurers	29	0	29	2	0	2
<b>Total</b>	<b>528</b>	<b>8</b>	<b>536</b>	<b>22</b>	<b>0</b>	<b>22</b>
<i>Pensionsfonds</i>	33	0	33	0	0	0

\* These figures do not include the relatively small mutual insurance associations whose activities are mostly regionally based and which are supervised by the federal states (BaFin 2017 statistics – Primary insurers and *Pensionsfonds*, page 12, Table 5) as well as municipal and church supplementary benefit funds (*Zusatzversorgungskassen*) or occupational pension schemes.

**Life insurers**

In 2018, responsibility for the supervision of 1 life insurer transferred from the federal states to BaFin. 6 insurers from the European Economic Area (EEA) registered for the cross-border provision of services in Germany (see Table 42).

**Table 42: Registrations by EEA life insurers in 2018**

Country	CBS*	BO**
France	1	
United Kingdom	4	
Spain	1	

\* CBS = Cross-border provision of services within the meaning of section 61 (3) of the German Insurance Supervision Act (*Versicherungsaufsichtsgesetz*).

\*\* BO = Branch office business within the meaning of section 61 (2) of the Insurance Supervision Act.

**Health insurers**

The number of German health insurers supervised by BaFin remained unchanged in 2018 at 46 undertakings.

**Property and casualty insurers**

6 property and casualty insurers supervised by BaFin ceased operating in 2018. 4 undertakings received new

authorisations during the year under review. Responsibility for the supervision of 1 property and casualty insurer transferred from the federal states to BaFin. 12 property and casualty insurers from the EEA (2 each from Belgium and France and 8 from Luxembourg) established a branch office in Germany. 1 branch office from each of Liechtenstein, Luxembourg and Spain and 2 branch offices from the United Kingdom terminated their activities. 30 insurers from the EEA registered for the cross-border provision of services in Germany. Other insurers that had already registered for the cross-border provision of services in Germany reported an expansion in their business operations (see Table 43 on page 176).

**Reinsurers**

The number of active reinsurers under BaFin's supervision amounted to 29 at the close of the year under review. Another 2 reinsurers are no longer accepting new business. 1 reinsurer from the Czech Republic established a branch office in Germany in 2018. A total of 7 branches of undertakings from the EEA (Ireland, Luxembourg, Spain, the Czech Republic and 3 from France) were operating in Germany.

***Pensionskassen*, *Pensionsfonds* and funeral expenses funds**

One funeral expenses fund terminated its activities in 2018. 2 *Pensionsfonds* received new authorisations.

**Table 43: Registrations by EEA property and casualty insurers in 2018**

<b>Country</b>	<b>CBS*</b>	<b>BO**</b>
Belgium	3	2
France	4	2
United Kingdom	2	
Ireland	4	
Croatia	1	
Latvia	1	
Liechtenstein	1	
Luxembourg	7	8
Malta	4	
Netherlands	2	
Portugal	1	

\* CBS = Cross-border provision of services within the meaning of section 61 (3) of the Insurance Supervision Act (*Versicherungsaufsichtsgesetz*).

\*\* BO = Branch office business within the meaning of section 61 (2) of the Insurance Supervision Act.



## 4 Complaints statistics for individual undertakings

### 4.1 Explanatory notes on the statistics

For many years, BaFin has published complaints statistics in its annual report classified by insurance undertaking and class. The Higher Administrative Court in Berlin (*Oberverwaltungsgericht – OVG*) issued a ruling on 25 July 1995 (case ref.: OVG 8 B 16/94) ordering the Federal Insurance Supervisory Office (*Bundesaufsichtsamt für das Versicherungswesen – BAV*), one of BaFin's predecessors, to include this information.

The complaints statistics list how many complaints BaFin processed in full in 2018 for Insurance Supervision.

The statistics do not take into account whether the complaints processed are justified, and hence are not indicative of the quality of the insurance business.

In order to provide an indicator of the volume of insurance business, the number of complaints that BaFin processed in full in 2018 is compared with the number of contracts in the respective insurance class as at 31 December 2017. The figures for the volume of business are notified by the individual undertakings. The citation of these figures puts rapidly growing insurers, often newly established undertakings, at a disadvantage because new business written in the course of the year giving rise to the complaints is not reflected in the statistics.

In the life insurance class, the figure specified for collective insurance arrangements relates to the number of insurance contracts. The volume of health insurance business is based on the number of natural persons with health insurance contracts, rather than the number of insured persons under each premium scale, which is usually higher. As in the past, these figures are not yet entirely reliable.

The figures for property and casualty insurance represent the number of insured risks. The figure for the volume of insurance business increases if undertakings agree group policies with large numbers of insured persons. Due to the limited disclosure requirements (section 51 (4) no. 1 sentence 4 of the Regulation on German Insurance Accounting (*Verordnung über die Rechnungslegung von Versicherungsunternehmen*), volume of business figures can only be disclosed for insurers whose gross premiums earned in 2017 exceeded €10 million in the respective insurance classes or types. The tables give no information on the volume of business (n.a.) for undertakings below that limit in the individual insurance classes.

The statistics do not include insurance undertakings operating within one of the classes listed that have not been the subject of complaints in the year under review.

As undertakings domiciled in other countries in the European Economic Area (EEA) were not required to submit reports to BaFin, no data is given for the volume of business of these insurers. The number of complaints is shown for the sake of completeness.

## 4.2 Life insurance

Reg. no.	Name	Number of insured risks	Complaints
1001	AACHENMÜNCHENER LEB.	5,090,178	55
1006	ALLIANZ LEBEN	10,663,690	143
1007	ALTE LEIPZIGER LEBEN	1,464,647	47
1017	ATHORA LV AG	263,692	14
1020	AXA LEBEN	2,758,122	50
1011	BARMENIA LEBEN	243,080	7
1028	BASLER LEBEN	660,498	21
1013	BAYER. BEAMTEN LEBEN	182,682	2
1015	BAYERN-VERS.	1,843,446	11
1177	CONCORDIA OECO LEBEN	171,425	2
1021	CONDOR LEBEN	217,949	4
1335	CONTINENTALE LV AG	752,049	8
1022	COSMOS LEBEN	1,368,484	25
1115	CREDIT LIFE AG	n.a.	5
1023	DEBEKA LEBEN	3,358,472	43
1167	DELTA DIREKT LEBEN	79,464	1
1136	DEVK ALLG. LEBEN	791,595	11
1025	DEVK DT. EISENBahn LV	553,747	3
1180	DT. ÄRZTEVERSICHERUNG	223,054	3
1148	DT. LEBENSVERS.	662,462	6
1130	ERGO DIREKT LEBEN AG	978,300	15
1184	ERGO LEBEN AG	4,466,729	78
1151	ERGO VORSORGE LEBEN	162,817	1
1107	EUROPA LEBEN	489,709	5
1035	FRANKFURT MÜNCHENER	286,559	14
1152	FRANKFURTER LEBEN	98,501	4
1139	GENERALI LEBEN AG	4,064,272	104
1108	GOTHAER LEBEN AG	1,291,812	28
1312	HANNOVERSCHE LV AG	993,195	7
1114	HANSEMERKUR LEBEN	296,472	2
1033	HDI LEBEN AG	2,097,394	41
1158	HEIDELBERGER LV	371,880	21
1137	HELVETIA LEBEN	150,656	5
1055	HUK-COBURG-LEBEN	662,214	15
1047	IDEAL LEBEN	595,270	8
1330	INTER LEBENSVERS. AG	111,873	3
1119	INTERRISK LEBENSVERS.	92,559	1

1045	KARLSRUHER LV AG	81,201	5
1062	LEBENSVERS. VON 1871	644,453	9
1112	LVM LEBEN	787,598	8
1109	MECKLENBURG. LEBEN	163,600	2
1162	MYLIFE DEUTSCHLAND	n.a.	1
1164	NEUE LEBEN LEBENSVERS	892,938	14
1131	NÜRNBERGER BEAMTEN LV	46,167	1
1147	NÜRNBG. LEBEN	2,617,885	53
1194	PB LEBENSVERSICHERUNG	1,083,799	19
1123	PLUS LEBEN	58,553	2
1081	PROV. LEBEN HANNOVER	807,360	3
1083	PROV.NORDWEST LEBEN	1,672,195	16
1082	PROV.RHEINLAND LEBEN	1,198,271	11
1141	R+V LEBENSVERS. AG	4,167,674	23
1018	RHEINLAND LEBEN	83,405	2
1150	SAARLAND LEBEN	141,177	2
1048	SIGNAL IDUNA LV	1,637,024	36
1157	SKANDIA LEBEN	255,778	45
1153	SPARK.-VERS.SACHS.LEB	569,020	2
1104	STUTTGARTER LEBEN	510,839	10
1091	SV SPARKASSENVERS.	1,633,345	9
1090	SWISS LIFE AG (CH)	898,124	18
1132	TARGO LEBEN AG	1,970,356	11
1092	UNIVERSA LEBEN	174,634	3
1093	VER.POSTVERS.	22	2
1140	VICTORIA LEBEN	971,934	38
1099	VOLKSWOHL-BUND LEBEN	1,443,904	11
1160	VPV LEBEN	725,773	10
1005	WÜRTT. LEBEN	2,058,014	23
1103	WWK LEBEN	927,914	36
1138	ZURICH DTSCH. HEROLD	3,146,417	46

Please refer to the "Explanatory notes on the statistics" on page 177.

### 4.3 Health insurance

Reg. no.	Name	Number of insured risks	Complaints
4034	ALLIANZ PRIV.KV AG	2,633,787	212
4142	ALTE OLDENBURGER AG	161,594	7
4112	ARAG KRANKEN	618,834	32
4095	AXA KRANKEN	1,736,364	142
4042	BARMENIA KRANKEN	1,236,014	35
4134	BAYERISCHE BEAMTEN K	1,144,664	24
4104	BERUFSFEUERWEHR HANN.	1,298	1
4004	CENTRAL KRANKEN	1,711,333	61
4118	CONCORDIA KRANKEN	104,588	1
4001	CONTINENTALE KRANKEN	1,350,329	45
4028	DEBEKA KRANKEN	4,040,278	52
4131	DEVK KRANKENVERS.-AG	405,429	2
5129	DFV DEUTSCHE FAM.VERS	n.a.	4
4044	DKV AG	4,374,468	171
4121	ENVIVAS KRANKEN	410,083	6
4126	ERGO DIREKT KRANKEN	1,549,415	19
5508	EUROPA VERSICHERUNG	n.a.	1
4119	GOTHAER KV AG	591,523	20
4043	HALLESCHE KRANKEN	694,928	47
4144	HANSEMERKUR KV AG	1,491,463	32
4117	HUK-COBURG KRANKEN	1,081,280	41
4145	INTER KV AG	384,150	22
4011	LANDESKRANKENHILFE	359,250	51
4109	LVM KRANKEN	361,687	8
4037	MÜNCHEN.VEREIN KV	325,871	14
4125	NÜRNBG. KRANKEN	303,848	6
4143	PAX-FAMILIENF.KV AG	164,907	7
4116	R+V KRANKEN	973,768	11
4002	SIGNAL IDUNA KRANKEN	2,539,737	67
4039	SÜDDEUTSCHE KRANKEN	657,693	23
4108	UNION KRANKENVERS.	1,238,728	11
4045	UNIVERSA KRANKEN	361,219	13
4139	WÜRTT. KRANKEN	403,286	2

Please refer to the "Explanatory notes on the statistics" on page 177.

## 4.4 Motor vehicle insurance

Reg. no.	Name	Number of insured risks	Complaints
5342	AACHENMÜNCHENER VERS.	2,494,791	10
5135	ADAC AUTOVERSICHERUNG	1,108,711	13
5312	ALLIANZ VERS.	12,619,346	89
5441	ALLSECUR DEUTSCHLAND	1,306,343	88
5405	ALTE LEIPZIGER VERS.	473,236	7
5155	AXA EASY	272,074	15
5515	AXA VERS.	4,846,196	68
5317	BARMENIA ALLG. VERS.	320,778	10
5633	BASLER SACH AG	318,495	3
5318	BASLER VERSICHERUNG (CH)	n.a.	2
5310	BAYER. BEAMTEN VERS.	212,994	1
5324	BAYER.VERS.VERB.AG	1,889,118	5
5146	BGV-VERSICHERUNG AG	743,523	4
5098	BRUDERHILFE SACH.AG	430,084	2
5338	CONCORDIA VERS.	975,820	5
5339	CONDOR ALLG. VERS.	286,538	2
5340	CONTINENTALE SACHVERS	783,024	12
5552	COSMOS VERS.	1,156,551	23
5343	DA DEUTSCHE ALLG.VER.	1,146,577	45
5549	DEBEKA ALLGEMEINE	924,938	4
5513	DEVK ALLG. VERS.	4,104,623	35
5344	DEVK DT. EISENB. SACH	1,002,609	4
5562	ERGO DIREKT	n.a.	2
5472	ERGO VERSICHERUNG	2,243,696	19
5508	EUROPA VERSICHERUNG	717,370	5
5470	FAHRLEHRERVERS.	327,359	2
5024	FEUERSOZietät	152,892	3
5473	GENERALI VERSICHERUNG	2,084,258	14
5858	GOTHAER ALLGEMEINE AG	1,573,331	10
5372	GOTHAER VERS.BANK	n.a.	1
5469	GVV-KOMMUNALVERS.	157,427	1
5585	GVV-PRIVATVERSICH.	201,196	1
5131	HANNOVERSCHE DIREKT	n.a.	1
5096	HDI GLOBAL SE	986,555	11
5085	HDI VERSICHERUNG	2,556,702	59
5044	HDNA VVAG	n.a.	1
5448	HELVETIA	n.a.	1

5384	HELVETIA VERS. (CH)	352,748	5
5375	HUK-COBURG UNTER.	7,268,797	65
5521	HUK-COBURG-ALLG. VERS	9,351,754	60
5086	HUK24 AG	3,754,027	43
5401	ITZEHOER VERSICHERUNG	1,497,900	24
5078	JANITOS VERSICHERUNG	111,158	1
5058	KRAVAG-ALLGEMEINE	1,744,779	20
5080	KRAVAG-LOGISTIC	1,146,939	12
5402	LVM SACH	6,058,655	37
5061	MANNHEIMER VERS.	229,380	3
5412	MECKLENBURG. VERS.	879,872	5
5070	NEXIBLE VERS. AG	n.a.	3
5426	NÜRNBG. ALLG.	244,812	5
5198	ÖFF. FEUER SA	278,476	1
5787	OVAG - OSTDT. VERS.	411,038	24
5446	PROV.NORD BRANDKASSE	793,179	2
5095	PROV.RHEINLAND VERS.	1,472,098	7
5438	R+V ALLGEMEINE VERS.	4,264,845	22
5137	R+V DIREKTVERSICHER.	443,058	13
5798	RHEINLAND VERS. AG	242,667	1
5051	S DIREKTVERSICHERUNG	347,143	11
5690	SCHWARZMEER U. OSTSEE	n.a.	1
5125	SIGNAL IDUNA ALLG.	1,028,194	5
5781	SPARK.-VERS.SACHS.ALL	185,944	1
5036	SV SPARK.VERSICHER.	1,046,280	4
5767	THÜGA SCHADENAUSGL.	n.a.	1
5055	VERTI VERSICHERUNG	1,335,554	66
5400	VGH LAND.BRAND.HAN.	1,901,669	11
5862	VHV ALLGEMEINE VERS.	5,204,286	72
5169	VOLKSWAGEN AUTO AG	782,522	9
5093	WESTF.PROV.VERS.AG	1,504,776	3
5525	WGV-VERSICHERUNG	1,440,710	13
5479	WÜRTT. GEMEINDE-VERS.	1,048,498	2
5783	WÜRTT. VERS.	2,956,970	29
5476	WWK ALLGEMEINE VERS.	188,355	3

Please refer to the "Explanatory notes on the statistics" on page 177.

## 4.5 General liability insurance

Reg. no.	Name	Number of insured risks	Complaints
5342	AACHENMÜNCHENER VERS.	1,317,419	8
5498	ADAC VERSICHERUNG	n.a.	3
5581	ADLER VERSICHERUNG AG	n.a.	1
5312	ALLIANZ VERS.	4,360,254	37
5441	ALLSECUR DEUTSCHLAND	n.a.	1
5405	ALTE LEIPZIGER VERS.	193,152	6
5515	AXA VERS.	3,163,918	21
5316	BAD. GEMEINDE-VERS.	2,943	1
5792	BADEN-BADENER VERS.	n.a.	2
5317	BARMENIA ALLG. VERS.	263,454	1
5633	BASLER SACH AG	382,149	1
5310	BAYER. BEAMTEN VERS.	181,695	1
5319	BAYER. HAUSBESITZER	n.a.	1
5324	BAYER.VERS.VERB.AG	1,141,284	10
5146	BGV-VERSICHERUNG AG	160,014	2
5098	BRUDERHILFE SACH.AG	211,564	2
5338	CONCORDIA VERS.	368,713	2
5339	CONDOR ALLG. VERS.	n.a.	1
5340	CONTINENTALE SACHVERS	452,856	3
5549	DEBEKA ALLGEMEINE	1,389,039	2
5513	DEVK ALLG. VERS.	1,239,555	4
5344	DEVK DT. EISENB. SACH	571,441	1
5472	ERGO VERSICHERUNG	1,556,120	29
5024	FEUERSOZietät	170,990	2
5473	GENERALI VERSICHERUNG	1,487,534	9
5858	GOTHAER ALLGEMEINE AG	1,665,201	17
5485	GRUNDEIGENTÜMER-VERS.	n.a.	1
5365	GVO GEGENSEITIGKEIT	n.a.	2
5374	HAFTPFLICHTKASSE	1,351,309	11
5501	HANSEMERKUR ALLG.	374,463	5
5096	HDI GLOBAL SE	14,510	1
5085	HDI VERSICHERUNG	1,324,788	20
5384	HELVETIA VERS. (CH)	362,019	3
5375	HUK-COBURG UNTER.	2,022,510	13
5521	HUK-COBURG-ALLG. VERS	1,657,794	6
5546	INTER ALLG. VERS.	115,821	1
5057	INTERLLOYD VERS.AG	n.a.	1

5780	INTERRISK VERS.	n.a.	1
5078	JANITOS VERSICHERUNG	198,131	1
5080	KRAVAG-LOGISTIC	n.a.	1
5402	LVM SACH	1,396,458	6
5061	MANNHEIMER VERS.	175,611	2
5412	MECKLENBURG. VERS.	283,449	3
5334	MEDIENVERS. KARLSRUHE	n.a.	1
5426	NÜRNBG. ALLG.	319,184	5
5686	NÜRNBG. BEAMTEN ALLG.	n.a.	1
5015	NV-VERSICHERUNGEN	181,136	1
5198	ÖFF. FEUER SA	123,476	1
5787	OVAG - OSTDT. VERS.	n.a.	5
5446	PROV.NORD BRANDKASSE	371,361	1
5095	PROV.RHEINLAND VERS.	852,018	3
5438	R+V ALLGEMEINE VERS.	1,891,445	29
5798	RHEINLAND VERS. AG	119,039	3
5690	SCHWARZMEER U. OSTSEE	n.a.	1
5125	SIGNAL IDUNA ALLG.	710,084	6
5036	SV SPARK.VERSICHER.	1,074,737	7
5459	UELZENER ALLG. VERS.	225,678	1
5042	VERSICHERUNGSK.BAYERN	15,569	8
5400	VGH LAND.BRAND.HAN.	781,809	8
5862	VHV ALLGEMEINE VERS.	1,486,181	7
5484	VOLKSWOHL-BUND SACH	151,766	2
5082	WALDENBURGER VERS.	n.a.	1
5093	WESTF.PROV.VERS.AG	840,180	5
5525	WGV-VERSICHERUNG	366,068	4
5783	WÜRTT. VERS.	1,182,475	13
5476	WWK ALLGEMEINE VERS.	143,461	1

Please refer to the "Explanatory notes on the statistics" on page 177.



## 4.6 Accident insurance

Reg. no.	Name	Number of insured risks	Complaints
5342	AACHENMÜNCHENER VERS.	2,552,797	6
5498	ADAC VERSICHERUNG	3,370,825	9
5312	ALLIANZ VERS.	3,922,954	18
5515	AXA VERS.	835,853	6
5792	BADEN-BADENER VERS.	268,876	2
5633	BASLER SACH AG	386,637	4
5310	BAYER. BEAMTEN VERS.	106,011	1
5324	BAYER.VERS.VERB.AG	1,029,780	2
5338	CONCORDIA VERS.	366,298	1
5340	CONTINENTALE SACHVERS	588,602	5
5552	COSMOS VERS.	169,691	4
5549	DEBEKA ALLGEMEINE	1,956,171	4
5513	DEVK ALLG. VERS.	928,775	1
5344	DEVK DT. EISENB. SACH	264,271	2
5562	ERGO DIREKT	229,481	3
5472	ERGO VERSICHERUNG	1,899,629	18
5508	EUROPA VERSICHERUNG	n.a.	1
5473	GENERALI VERSICHERUNG	1,972,444	9
5858	GOTHAER ALLGEMEINE AG	710,524	3
5374	HAFTPFLICHTKASSE	191,135	1
5501	HANSEMERKUR ALLG.	101,702	1
5085	HDI VERSICHERUNG	458,334	6
5448	HELVETIA	n.a.	1
5384	HELVETIA VERS. (CH)	121,535	1
5375	HUK-COBURG UNTER.	992,743	2
5573	IDEAL VERS.	n.a.	1
5546	INTER ALLG. VERS.	78,436	1
5078	JANITOS VERSICHERUNG	169,190	6
5402	LVM SACH	956,902	5
5061	MANNHEIMER VERS.	63,017	1
5412	MECKLENBURG. VERS.	167,219	3
5414	MÜNCHEN. VEREIN ALLG.	n.a.	1
5426	NÜRNBG. ALLG.	468,939	5
5015	NV-VERSICHERUNGEN	n.a.	1
5095	PROV.RHEINLAND VERS.	2,380,929	1
5438	R+V ALLGEMEINE VERS.	1,410,272	6
5798	RHEINLAND VERS. AG	102,130	1

5125	SIGNAL IDUNA ALLG.	1,677,584	10
5781	SPARK.-VERS.SACHS.ALL	92,238	2
5586	STUTTGARTER VERS.	559,903	2
5036	SV SPARK.VERSICHER.	282,646	2
5790	TARGO VERSICHERUNG	108,051	5
5400	VGH LAND.BRAND.HAN.	5,013,594	4
5484	VOLKSWOHL-BUND SACH	170,133	1
5479	WÜRTT. GEMEINDE-VERS.	144,289	1
5783	WÜRTT. VERS.	720,370	3
5590	WÜRZBURGER VERSICHER.	n.a.	1
5476	WWK ALLGEMEINE VERS.	286,951	7

Please refer to the "Explanatory notes on the statistics" on page 177.

## 4.7 Household contents insurance

Reg. no.	Name	Number of insured risks	Complaints
5342	AACHENMÜNCHENER VERS.	967,207	4
5312	ALLIANZ VERS.	2,526,884	19
5405	ALTE LEIPZIGER VERS.	109,534	2
5068	AMMERLÄNDER VERS.	443,444	11
5515	AXA VERS.	1,242,153	9
5792	BADEN-BADENER VERS.	n.a.	1
5318	BASLER VERSICHERUNG (CH)	n.a.	1
5310	BAYER. BEAMTEN VERS.	n.a.	3
5043	BAYER.L-BRAND.VERS.AG	n.a.	1
5324	BAYER.VERS.VERB.AG	553,539	1
5338	CONCORDIA VERS.	250,686	2
5340	CONTINENTALE SACHVERS	218,404	2
5552	COSMOS VERS.	n.a.	1
5549	DEBEKA ALLGEMEINE	805,990	1
5513	DEVK ALLG. VERS.	940,305	2
5344	DEVK DT. EISENB. SACH	429,305	1
5472	ERGO VERSICHERUNG	983,502	16
5508	EUROPA VERSICHERUNG	n.a.	2
5024	FEURERSOZietät	118,439	1
5473	GENERALI VERSICHERUNG	1,138,785	1
5858	GOTHAER ALLGEMEINE AG	772,837	10
5365	GVO GEGENSEITIGKEIT	n.a.	4
5374	HAFTPFLICHTKASSE	275,827	1
5501	HANSEMERKUR ALLG.	n.a.	1
5085	HDI VERSICHERUNG	681,309	9
5375	HUK-COBURG UNTER.	1,448,900	10
5521	HUK-COBURG-ALLG. VERS	976,022	4
5086	HUK24 AG	271,057	2
5573	IDEAL VERS.	n.a.	1
5546	INTER ALLG. VERS.	n.a.	1
5780	INTERRISK VERS.	201,924	1
5078	JANITOS VERSICHERUNG	110,728	1
5404	LBN	109,109	2
5402	LVM SACH	847,946	8
5061	MANNHEIMER VERS.	73,606	1
5412	MECKLENBURG. VERS.	187,680	1
5426	NÜRNBG. ALLG.	152,874	1

5787	OVAG - OSTDT. VERS.	n.a.	2
5095	PROV.RHEINLAND VERS.	502,056	3
5438	R+V ALLGEMEINE VERS.	1,091,543	6
5121	RHION VERSICHERUNG	n.a.	1
5773	SAARLAND FEUERVERS.	n.a.	2
5125	SIGNAL IDUNA ALLG.	317,144	4
5781	SPARK.-VERS.SACHS.ALL	n.a.	1
5042	VERSICHERUNGSK.BAYERN	n.a.	2
5400	VGH LAND.BRAND.HAN.	471,670	4
5862	VHV ALLGEMEINE VERS.	409,935	1
5461	VPV ALLGEMEINE VERS.	153,323	1
5162	WERTGARANTIE AG	n.a.	1
5093	WESTF.PROV.VERS.AG	557,849	2
5783	WÜRTT. VERS.	730,340	9

Please refer to the "Explanatory notes on the statistics" on page 177.

## 4.8 Residential building insurance

Reg. no.	Name	Number of insured risks	Complaints
5342	AACHENMÜNCHENER VERS.	410,699	11
5312	ALLIANZ VERS.	2,512,990	52
5405	ALTE LEIPZIGER VERS.	115,198	9
5455	ARAG ALLG. VERS.	40,263	1
5515	AXA VERS.	871,356	19
5633	BASLER SACH AG	209,539	7
5318	BASLER VERSICHERUNG (CH)	n.a.	1
5310	BAYER. BEAMTEN VERS.	36,386	4
5319	BAYER. HAUSBESITZER	36,020	1
5043	BAYER.L-BRAND.VERS.AG	1,981,608	14
5324	BAYER.VERS.VERB.AG	855,432	7
5146	BGV-VERSICHERUNG AG	74,154	1
5098	BRUDERHILFE SACH.AG	53,538	1
5338	CONCORDIA VERS.	221,578	5
5339	CONDOR ALLG. VERS.	46,076	2
5340	CONTINENTALE SACHVERS	138,382	4
5552	COSMOS VERS.	n.a.	5
5549	DEBEKA ALLGEMEINE	269,517	3
5513	DEVK ALLG. VERS.	411,014	1
5344	DEVK DT. EISENB. SACH	269,567	1
5522	DOLLERUP.FREIE BRANDG	n.a.	2
5472	ERGO VERSICHERUNG	412,976	13
5024	FEURERSOZietät	85,671	6
5473	GENERALI VERSICHERUNG	532,576	14
5858	GOTHAER ALLGEMEINE AG	336,067	6
5485	GRUNDEIGENTÜMER-VERS.	83,139	2
5032	HAMB. FEUERKASSE	160,485	2
5085	HDI VERSICHERUNG	252,961	16
5384	HELVETIA VERS. (CH)	149,587	3
5126	HÜBENER VERSICHERUNG	n.a.	2
5375	HUK-COBURG UNTER.	689,891	11
5521	HUK-COBURG-ALLG. VERS	298,340	2
5086	HUK24 AG	94,500	2
5057	INTERLLOYD VERS.AG	51,923	1
5780	INTERRISK VERS.	123,542	1
5078	JANITOS VERSICHERUNG	n.a.	1
5362	LANDESSCHADENHILFE	n.a.	1

5402	LVM SACH	657,852	17
5061	MANNHEIMER VERS.	49,654	2
5412	MECKLENBURG. VERS.	110,706	2
5334	MEDIENVERS. KARLSRUHE	n.a.	2
5426	NÜRNBG. ALLG.	73,470	5
5198	ÖFF. FEUER SA	48,792	1
5446	PROV.NORD BRANDKASSE	294,320	1
5095	PROV.RHEINLAND VERS.	550,907	13
5438	R+V ALLGEMEINE VERS.	1,019,647	25
5798	RHEINLAND VERS. AG	n.a.	2
5121	RHION VERSICHERUNG	n.a.	1
5773	SAARLAND FEUERVERS.	74,509	1
5491	SCHLESWIGER VERS.V.	n.a.	6
5125	SIGNAL IDUNA ALLG.	194,564	9
5036	SV SPARK.VERSICHER.	1,650,889	15
5042	VERSICHERUNGSK.BAYERN	n.a.	2
5400	VGH LAND.BRAND.HAN.	465,653	13
5862	VHV ALLGEMEINE VERS.	135,402	3
5461	VPV ALLGEMEINE VERS.	69,547	1
5093	WESTF.PROV.VERS.AG	582,945	9
5525	WGV-VERSICHERUNG	86,233	2
5783	WÜRTT. VERS.	451,212	9

Please refer to the "Explanatory notes on the statistics" on page 177.

## 4.9 Legal expenses insurance

Reg. no.	Name	Number of insured risks	Complaints
5826	ADAC-RECHTSSCHUTZ	2,144,564	12
5809	ADVOCARD RS	1,429,071	67
5312	ALLIANZ VERS.	2,450,089	26
5405	ALTE LEIPZIGER VERS.	298,571	15
5800	ARAG SE	1,495,840	78
5801	AUXILIA RS	565,742	30
5838	BADISCHE RECHTSSCHUTZ	172,634	4
5319	BAYER. HAUSBESITZER	n.a.	1
5338	CONCORDIA VERS.	484,604	7
5340	CONTINENTALE SACHVERS	130,817	4
5343	DA DEUTSCHE ALLG.VER.	n.a.	3
5549	DEBEKA ALLGEMEINE	436,033	5
5803	DEURAG DT. RS	1,200,354	65
5513	DEVK ALLG. VERS.	n.a.	1
5829	DEVK RECHTSSCHUTZ	1,130,779	33
5834	DMB RECHTSSCHUTZ	801,562	20
5472	ERGO VERSICHERUNG	2,010,411	57
5818	HUK-COBURG RS	1,755,274	18
5521	HUK-COBURG-ALLG. VERS	n.a.	1
5086	HUK24 AG	128,550	2
5573	IDEAL VERS.	n.a.	2
5401	ITZEHOER VERSICHERUNG	n.a.	14
5402	LVM SACH	803,470	5
5412	MECKLENBURG. VERS.	148,779	3
5805	NEUE RECHTSSCHUTZ	413,724	12
5813	OERAG RECHTSSCHUTZ	1,866,431	53
5438	R+V ALLGEMEINE VERS.	788,965	5
5807	ROLAND RECHTSSCHUTZ	1,712,665	48
5400	VGH LAND.BRAND.HAN.	211,424	1
5525	WGV-VERSICHERUNG	426,173	15
5783	WÜRTT. VERS.	699,482	7

Please refer to the "Explanatory notes on the statistics" on page 177.

## 4.10 Insurers based in the EEA

Reg. no.	Name	Complaints	Reg. no.	Name	Complaints
7985	ADVIGON VERS. (LI)	4	1317	R+V LUXEMB. LV (L)	2
5163	AIG EUROPE LIMITED (GB)	32	7415	R+V LUXEMBOURG L (L)	2
7778	ALPHA INS. A/S (DK)	5	9158	RCI INSURANCE (MT)	4
7509	AMTRUST INT. (IE)	1	9159	RCI LIFE LIM. (MT)	1
5090	AXA CORPORATE S. (F)	1	7453	SCOTT. WID. (GB)	11
9374	AXA LIFE EUROPE (IE)	3	9383	SCOTTISH FRIENDLY (GB)	1
5145	BALCIA INS. (LV)	6	1320	STANDARD LIFE (GB)	13
9349	BUILDERS DIRECT (LU)	1	7763	STONEBRIDGE (GB)	1
7811	CACI LIFE DAC (IE)	4	7878	SWISS LIFE (FL)	1
7786	CANADA LIFE (IE)	5	9069	SWISSLIFE PREVO. (F)	1
1300	CANADA LIFE (IRL)	9	9281	TVM VERZEK. (NL)	1
1182	CARDIF LEBEN (F)	7	7540	VALORLIFE LEBENS.(LI)	1
5056	CARDIF VERS. (F)	12	7643	VIENNA-LIFE (FL)	2
5902	CHUBB EUROPEAN (F)	2	5152	W.R. BERKLEY (L)	3
5142	CHUBB INSUR. (GB)	2	5151	ZURICH INSURANCE (IRL)	54
9306	CNP SANT. (IE)	7			
9307	CNP SANTANDER (IE)	8			
7614	DB VITA SA (L)	1			
7309	DONAU VERSICHERUNG (AT)	1			
5188	DTSCH.NIEDERL.BASLER (LU)	5			
7483	ERGO LIFE (LU)	5			
5115	EUROMAF SA (F)	3			
7433	EUROPEISKA (SE)	1			
5209	FRIDAY (L)	6			
9283	FRIENDS LIFE LIM. (GB)	4			
7203	FWU LIFE (LU)	1			
1324	FWU LIFE INS. (L)	1			
9016	GABLE INSURANCE (LI)	2			
9390	GEFION INS. (DK)	1			
9104	GLOBALITY S.A. (LU)	1			
9369	GREENVAL INS. (IE)	1			
7270	HANSARD EUROPE (IE)	1			
9031	LIBERTY EURO.(IRL/E)	2			
9139	LIECHTENSTEIN L. (FL)	4			
7671	MON. ASS. LUX. (LU)	1			
1323	MONUTA VERS. (NL)	3			
7723	PRISMALIFE AG (LI)	12			
7894	QUANTUM LEBEN AG(FL)	1			



## 5 Memoranda of Understanding (MoU)

<b>Banking Supervision</b>		<b>Banking Supervision</b>		<b>Securities Supervision</b>	
Albania	2012	Netherlands	1993	Dubai	2006
Argentina	2001	Nicaragua	2011	Estonia	2002
Armenia	2011	Norway	1995	France	1996
Australia	2005	Philippines	2007	Guernsey	2011
Austria	2000	Poland	2004	Hong Kong	2018
Belgium	1993	Portugal	1996	Hungary	1998
Bosnia and Herzegovina	2016	Qatar	2008	Iran	2016
Brazil	2006	Romania	2003	Israel	2017
Canada	2004	Russia	2006	Italy	1997
China	2004	Serbia	2011	Jersey	2012
Croatia	2008	Singapore	2009	Jersey	2001
Czech Republic	2003	Slovakia	2002	Korea	2010
Denmark	1993	Slovenia	2001	Lebanon	2016
Dubai	2006	South Africa	2004	Monaco	2009
El Salvador	2011	Spain	1993	Ontario (Canada)	2018
Estonia	2002	Sweden	1995	Poland	1999
Finland	1995	Turkey	2011	Portugal	1998
France	1992	United Kingdom (BE/FSA)	1995	Qatar	2008
Georgia	2011	United Kingdom (BSC)	1995	Russia	2001
Greece	1993	United Kingdom (SIB/SROs)	1995	Russia	2009
Guernsey	2011	USA (FDIC)	2006	Singapore	2000
Hong Kong	2004	USA (FedBoard/OCC)	2003	Slovakia	2004
Hungary	2000	USA (NYSBD)	2002	South Africa	2001
India	2013	USA (OCC)	2000	Spain	1997
Ireland	1993	USA (OTS)	2005	Switzerland	1998
Italy (BI)	1993	USA (SEC)	2007	Taiwan	1997
Jersey	2012	Vatican	2014	Turkey	2000
Jersey	2000	Vietnam	2010	United Arab Emirates	2008
Korea	2006			USA (CFTC)	1997
Kosovo	2011			USA (SEC)	1997
Latvia	2000	<b>Securities Supervision</b>		USA (SEC)	2007
Lebanon	2016	Argentina	1998	Vatican	2014
Lithuania	2001	Australia	1998		
Luxembourg	1993	Brazil	1999	<b>Insurance Supervision</b>	
Macedonia	2011	Canada	2003	Australia	2005
Malta	2004	China	1998	California (USA)	2007
Mexico	2010	Croatia	2008	Canada	2004
Moldova	2014	Cyprus	2003	China	2001
		Czech Republic	1998		

**Insurance Supervision**

Connecticut (USA)	2011
Croatia	2008
Czech Republic	2002
Dubai	2006
Egypt	2010
Estonia	2002
Florida (USA)	2009
Georgia (USA)	2012
Guernsey	2011
Hong Kong	2008
Hungary	2002
Jersey	2012
Korea	2010
Latvia	2001
Lebanon	2016
Lithuania	2003
Malta	2004
Maryland (USA)	2009
Minnesota (USA)	2009
Nebraska (USA)	2007
New Jersey (USA)	2009
New York (USA)	2008
Qatar	2008
Romania	2004
Singapore	2009
Slovakia	2001
Thailand	2010
USA (OTS)	2005
Vatican	2014

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