

# 2020

## Annual Report

Federal Financial  
Supervisory Authority



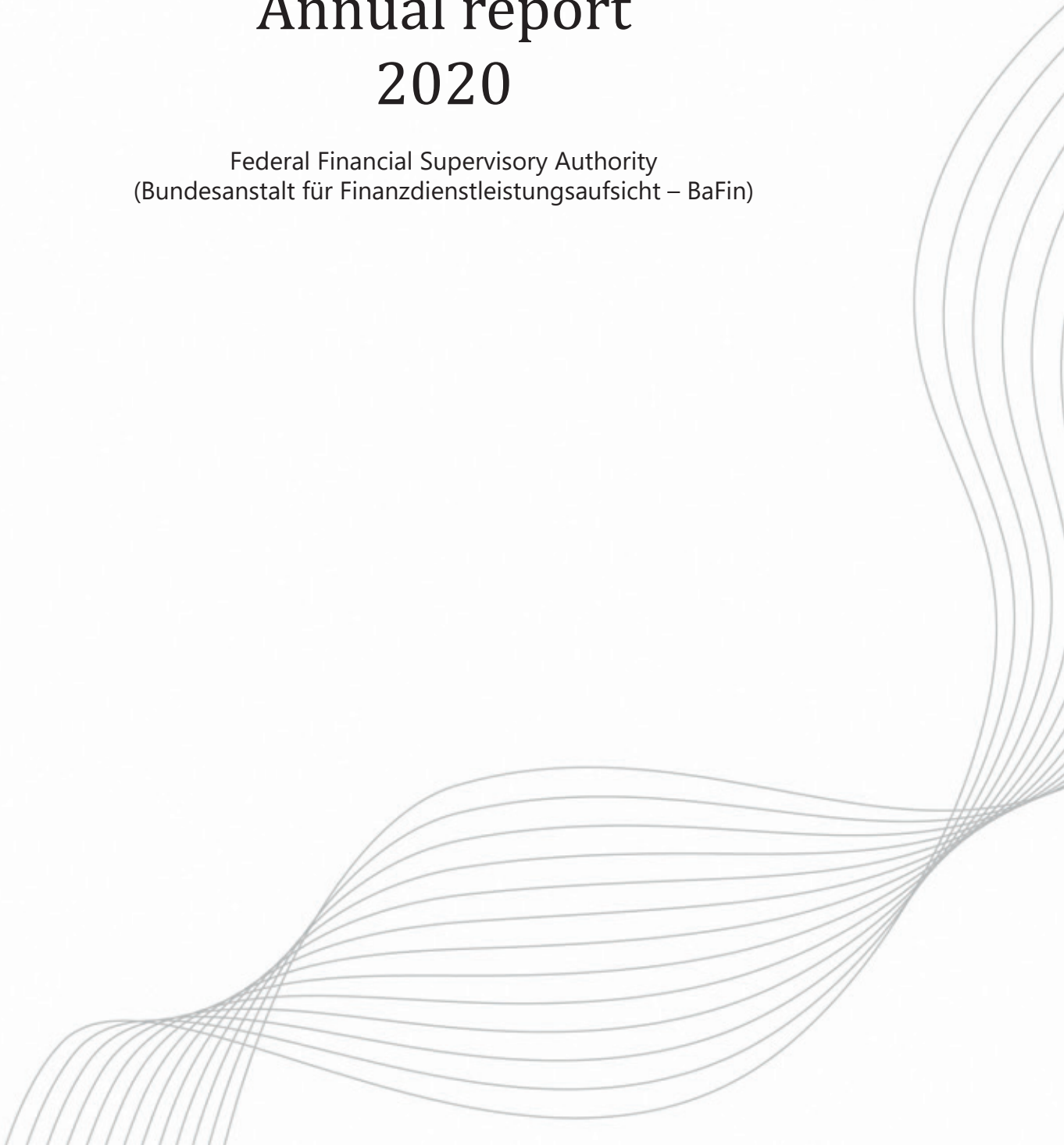
# BaFin

Bundesanstalt für  
Finanzdienstleistungsaufsicht



# Annual report 2020

Federal Financial Supervisory Authority  
(Bundesanstalt für Finanzdienstleistungsaufsicht – BaFin)



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# Preface



2020 turned out differently to what we had planned. The fact that we would be facing exceptional times started becoming apparent in January, with growing reports that people in China were coming down with a new coronavirus. Just a few weeks later it was clear that this would develop into a global pandemic. For us as a financial supervisory authority, but also for governments and central banks around the world, the challenge was to contain the pandemic's impact on national economies – and hence on the financial sector.

What did BaFin do? Like other supervisory authorities, it used the flexibility offered by the existing frameworks to temporarily adapt a number of supervisory requirements. Its goal was and still is to help financial undertakings mitigate the consequences of the pandemic for the economy. The main focus here was on banks and savings banks, which perform the extremely important function within economies of routing money where it is needed. In other words, they have a particularly responsible role to play during the coronavirus pandemic. In line with this, BaFin offered the institutions some leeway, but only as far as the law, accounting standards and financial stability permit.

Very quickly the question arose as to whether the pandemic would trigger a systemic banking crisis. This did not seem likely at the end of 2020. German institutions have done pretty well, despite being known for weak earnings. What is more, a stress test conducted by BaFin and the Deutsche Bundesbank in the summer of 2020 showed that, in the aggregate, the banks were

adequately capitalised even in the most severe assumed scenario<sup>1</sup>. However, the words “in the aggregate” are decisive here: it cannot be ruled out that individual institutions – especially those that were already very weak – may not survive the pandemic. When exactly, and how many, loan defaults will be seen can only be estimated. Nevertheless, the fact that there will be a rise in defaults can be taken as given. Dealing responsibly with this uncertainty is the job of both BaFin and the sector itself.

Another serious event happened in June 2020: Wirecard AG filed for insolvency. Since then suspicions of massive fraud have been raised. The scandal surrounding the Aschheim-based company has led to a loss of trust. At the same time, it revealed weaknesses in the regulatory regime and supervisory structures in Germany. BaFin is playing its part in identifying the lessons to be learned from what happened.

Lawmakers have already introduced draft legislation designed to comprehensively strengthen BaFin's financial reporting enforcement powers as the federal supervisory authority. It is intended to give BaFin the statutory powers to intervene more rapidly in future, and to clearly define responsibilities. In addition, the Federal Ministry of Finance (*Bundesministerium der Finanzen*) commissioned a consulting firm to review organisational structures at BaFin. The latter is now facing a series of key strategic decisions. It is pressing ahead vigorously with this process in tandem with the Federal Ministry of Finance.

Together with the Finance Ministry, I decided to resign my position with effect from 1 April 2021. My colleague and BaFin Deputy President Elisabeth Roegele left BaFin on 1 May. The last eight years as a member of BaFin's top team – six of them as its President – were both challenging and rewarding for me. Now the time has come for BaFin to turn a new page. I would like to wish both BaFin and my successor all the best.

Felix Hufeld – BaFin President until 31 March 2021

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<sup>1</sup> See expert article dated 3 August 2020: “Small and medium-sized credit institutions are largely stress-resilient” ([www.bafin.de/dok/14521038](http://www.bafin.de/dok/14521038)).

# BaFin in brief



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# BaFin: an integrated supervisory and national resolution authority

## 1 Responsibilities

### **BaFin's mission**

BaFin's mission is to ensure the functioning, stability and integrity of the German financial market. Bank customers, insurance policyholders and investors should be able to trust the financial system. BaFin therefore aims to ensure that market participants comply with the relevant laws.

### **Undertakings overseen by BaFin**

In 2020,<sup>1</sup> BaFin had the following entities under its supervision as an integrated financial supervisor:

- 1,477 directly supervised less significant institutions (LSIs),
- 52 significant institutions (SIs) supervised as part of the Single Supervisory Mechanism (SSM) headed by the European Central Bank (ECB),
- 1,146 financial services institutions,
- 56 payment institutions and 8 e-money institutions,
- 11 account information service providers,
- 93 German branches of foreign credit institutions from the European Economic Area,
- 25 third-country branches,
- 536 insurers and 34 *Pensionsfonds*,
- 574 asset management companies,
- 7,214 domestic funds, and
- 4,078 agents performing payment services.

### **BaFin's functions**

- **Solvent undertakings:** BaFin's solvency supervision helps ensure that credit institutions, insurers and financial services providers are able to meet their payment obligations.
- **Fair conditions:** BaFin's functions also include ensuring fair and transparent market conditions. In addition, BaFin provides collective consumer protection.
- **Preventing money laundering:** BaFin is also tasked with preventing the financial system from being abused for money laundering and terrorist financing purposes. This is why it ensures that the companies it supervises comply with the requirements designed to prevent these offences.
- **Authorised business only:** In Germany, banking, financial services, investment, insurance, payment services and e-money business may not be conducted without official authorisation. BaFin oversees compliance with this prohibition.
- **Resolution in emergencies:** BaFin is also Germany's national resolution authority (NRA) for banks, investment firms and financial market infrastructures.
- **International activities:** As a member of numerous European bodies, BaFin is engaged in creating a single European financial market. At an international level, it is involved in developing global supervisory and resolution standards.

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<sup>1</sup> As at 31 December 2020.

### **BaFin's management**

BaFin is managed by a six-person Executive Board. In 2020, this body comprised President Felix Hufeld and the Chief Executive Directors for BaFin's five sectors: Banking Supervision (Raimund Röseler), Insurance and Pension Funds Supervision (Dr Frank Grund), Securities Supervision/Asset Management (Elisabeth Roegele), Resolution (Dr Thorsten Pötzsch), and Internal Administration and Legal Affairs (Béatrice Freiwald).

### **How BaFin is funded**

BaFin is a public-law institution with legal capacity. It is funded solely by fees and contributions from the institutions and businesses that it supervises and as such is independent of the federal budget.

## **2 A look at BaFin's core tasks**

### **2.1 Banking supervision**

Only a stable financial system can provide the financial resources that a national economy requires. Banking supervision makes a major contribution to this.

#### **BaFin within the system of European banking supervision**

Since 4 November 2014, BaFin has been part of the SSM, which is headed by the ECB. BaFin employees are involved at all levels of the SSM.

The SSM directly supervises the eurozone's 117 significant institutions (SIs)<sup>2</sup>. This is done in Joint Supervisory Teams, in which BaFin

staff work side by side with supervisors from throughout the eurozone. A total of 52 German institutions were classified as significant in 2020 and were directly supervised by the ECB as part of the SSM.

The eurozone's less significant institutions (LSIs) are supervised indirectly by the SSM and are still subject to national supervision. In Germany, 1,324 CRR credit institutions<sup>3</sup> were classified as less significant in 2020 and were supervised directly by BaFin. BaFin works together with the *Deutsche Bundesbank* to supervise less significant institutions.

BaFin aims to ensure that:

- only authorised institutions offer services on the market and that these institutions are managed by directors who have proved they have the necessary professional qualifications and are fit and proper; and
- the institutions conduct their business in a proper manner and comply with all relevant legal and supervisory provisions. One of the most important principles is that banks must have an adequate capital buffer to cover the risks that they assume.

Banking supervision is not responsible for preventing each and every bank failure. If a bank becomes insolvent, the statutory deposit guarantee schemes ensure that customers do not lose all of their deposits. These schemes are also supervised by BaFin.

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2 As at 31 December 2020.

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3 "CRR" stands for "Capital Requirements Regulation".

## 2.2 Insurance supervision

In the insurance business, trust is of particular importance. Customers expect their private insurers to be reliable contractual partners – often over a very long period of time. BaFin seeks to ensure that policyholders' interests remain protected and that insurers can meet their contractual obligations at all times. By doing so, it fulfils an important economic and social function.

BaFin ensures that:

- only authorised insurers operate in the market and that these undertakings are managed by directors who have proven they have the necessary professional qualifications and are fit and proper; and
- the insurers conduct their business in a proper manner and comply with all relevant legal and supervisory provisions. In particular, undertakings have to invest their capital in a manner appropriate to the risks they assume, i.e. safely and profitably.

## 2.3 Securities supervision

Securities trading can only run smoothly if all market participants can rely on fair and transparent market conditions being in place. If market manipulation or insider trading is suspected, BaFin investigates the matter. In addition, it monitors listed stock corporations and their shareholders to ensure they comply with their publication requirements. Among other things, companies must publish ad hoc disclosures, managers' transaction reports and financial reports. Shareholders are required to report if they hold significant percentages of the voting rights in a listed company. Anyone who holds 30% or more of the voting rights must make an offer to the other shareholders to buy their shares.

In addition, as the securities supervisor, BaFin monitors financial services providers, asset management companies and the investment funds that they launch.

BaFin also examines prospectuses, including listing prospectuses, and checks whether they contain the minimum information required. However, legislators have not made BaFin responsible for examining whether the content of prospectuses is factually correct, or whether the offerors are trustworthy.

Together with the Financial Reporting Enforcement Panel (*Deutsche Prüfstelle für Rechnungslegung*), BaFin also examines the financial reporting of publicly traded companies. There were 545 such undertakings<sup>4</sup> in 2020 (previous year: 549). Lawmakers are planning to reform the current two-tier financial reporting enforcement system and to give BaFin greater powers.

## 2.4 Collective consumer protection

Another of BaFin's core tasks is to protect consumers' collective interests. This extends to all financial products and services that BaFin deals with in its supervisory capacity.

When it comes to enforcing claims by individual consumers, however, BaFin has to refer them to the competent ombudspersons, arbitration bodies and courts. There is only one exception: if a customer has the right to open a basic payment account, BaFin can enforce this claim individually. However, BaFin can issue orders to prevent or remedy deficiencies

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<sup>4</sup> The number is determined on 1 July of each year. The figure given is as at 1 July 2020.

related to consumer protection if a general clarification seems to be in the interests of consumer protection. In serious cases, it can even restrict or prohibit the distribution of products. Collective consumer protection also includes analysing market activity and assessing its consequences for consumers so as to combat any deficiencies in this way, too.

In addition, BaFin endeavours to ensure that the range of financial products, insurance products and financial services on offer is transparent and comprehensible. The goal is to enable consumers to understand how the products and services concerned function and the risks involved, and to enable them to assess their real cost.

BaFin regularly provides consumers with information on its website and warns them among other things of unauthorised providers. In 2020, its consumer helpline (phone: +49 (0) 800 2 100 500) answered 23,777 enquiries from citizens. In addition, BaFin received 20,464 written enquiries and complaints about banks, insurance undertakings and financial services providers. If the complaints suggest that consumer protection regulations affecting a large number of people have been breached, BaFin examines whether the preconditions for taking supervisory measures have been met.

## 2.5 Combating money laundering and unauthorised business activities

The financial sector is particularly susceptible to abuse in the form of money laundering and terrorist financing. This makes combating these offences even more important. However, BaFin does not prosecute money launderers. Its job is to ensure that all companies supervised by it

use suitable preventive systems to protect themselves against being abused for the purposes of money laundering and terrorist financing. Companies must report suspicious activities without undue delay to the Financial Intelligence Unit (FIU).

The banking, financial services, investment and insurance business, and payment services and e-money transactions may not be conducted in Germany without authorisation from BaFin. BaFin oversees this prohibition and takes action against providers who fail to abide by it. Lawmakers have provided it with a wide range of powers of investigation and intervention. In 2020, BaFin took action in 176 cases against undertakings that were conducting business without authorisation or that were involved in initiating, entering into or settling unauthorised business transactions.

## 2.6 Resolution

What happens if a bank, investment firm or financial market infrastructure (FMI) with a banking licence is failing or likely to fail, and this threat cannot be averted by private-sector intervention or supervisory means?

If the institution concerned cannot be allowed to become insolvent because this would be a threat to financial stability, BaFin – as the national resolution authority (NRA) – is required to take action. It can use a number of resolution tools to resolve the bank in an orderly manner without putting the stability of the financial market at risk; this can be done on its own authority or on the instruction of the Single Resolution Board (SRB).

The latter heads the European Single Resolution Mechanism (SRM), of which BaFin is also a member in its capacity as an NRA. Within the SRM, BaFin is responsible for



those German institutions that are classified as less significant in the SSM. These also include FMIs with a banking licence.

The SRB, on the other hand, is responsible for significant institutions and for certain less significant institutions with cross-border activities (including a total of 37 German institutions in 2020). Similar to the arrangement in the SSM, there are Internal Resolution Teams (IRTs) in which BaFin employees cooperate with representatives of the SRB and, where appropriate, other NRAs.

However, BaFin does not wait until there is an emergency before it takes action as an NRA. It continuously monitors whether the institutions for which it is responsible can be reorganised or seamlessly resolved without unreasonable risk to the financial system. It makes sure that any impediments to resolution are removed. The aim is to be ready in an emergency.

## 2.7 BaFin's international role

BaFin works closely together with supervisory authorities in other countries. It is also represented in numerous European and international organisations and working groups addressing issues relating to supervision, consumer protection, resolution and regulation. BaFin was a member of roughly 600 such groups in 2020.

## 2.8 Internal Administration and Legal Affairs

The Internal Administration and Legal Affairs Sector performs core organisational, human resources and budgetary tasks for the whole of BaFin, freeing up the other Sectors by providing a wide range of services. The central Legal Affairs department ensures that the legal bases are applied consistently throughout BaFin, and supports the organisational units with legal questions. It is also the unit within BaFin responsible for representing BaFin in court.

BaFin's work is increasingly going digital, and this also includes sharing data with other authorities. The IT department creates the technical foundations for this with its own data centres in Bonn and Frankfurt. It provides supervised undertakings with an up-to-date, secure infrastructure for transmitting reporting data and communicating with the Supervisory Authority. The IT department and the Digital Office are driving forward implementation of BaFin's digital transformation strategy<sup>5</sup> and advise the organisational units on how to digitalise their business processes. This helps to further improve the supervisory and support processes and to develop appropriate new supervisory tools.

In addition, the Sector is responsible for budget planning at BaFin and ensures that the authority has sufficient funds and human resources in order to perform its statutory duties.

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<sup>5</sup> [www.bafin.de/dok/13477846](http://www.bafin.de/dok/13477846).



Key  
indicators at  
a glance

## Key indicators at a glance

	2016	2017	2018	2019	2020
<b>Credit institutions<sup>1,2</sup></b>					
<b>Capital resources<sup>3</sup></b>					
Tier 1 capital (€ billion)	489.6	491.2	514.7	511.7	567.9
Own funds (€ billion)	562.0	559.7	580.5	573.0	629.6
Tier 1 capital (% ratio)	15.7%	16.6%	16.8%	16.6%	17.6%
Own funds (% ratio)	18.0%	18.9%	18.9%	18.6%	19.5%
<b>Asset structure and portfolio quality</b>					
Total assets (€ billion) <sup>4</sup>	8,024.3	8,411.2	8,329.8	8,755.1	9,244.9
Total assets (€ billion) <sup>5</sup>	7,995.3	8,379.5	8,303.3	8,826.8	9,291.4
<b>Structure of loans and advances to banks and non-banks (%)<sup>6</sup></b>					
Domestic banks	16.5%	21.4%	19.8%	18.3%	19.8%
Foreign banks	10.9%	9.3%	9.2%	9.0%	11.2%
Non-banks – other financial institutions	2.5%	2.6%	2.7%	2.9%	2.9%
Non-financial corporations	16.2%	15.8%	16.7%	17.3%	17.7%
Private households	30.7%	29.3%	30.2%	31.0%	32.0%
Private non-profit organisations	0.3%	0.3%	0.3%	0.3%	0.3%
Public sector	5.5%	5.2%	4.8%	4.5%	4.5%
Foreign non-banks	17.4%	16.0%	16.2%	16.5%	11.7%
<b>Amounts due to non-banks as a proportion of loans and advances to non-banks (%)<sup>7</sup></b>	104.3%	104.3%	103.0%	102.0%	105.1%
<b>Proportion of foreign-currency loans to private households (%)</b>	0.4%	0.3%	0.2%	0.2%	0.2%
<b>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>8</sup></b>	2.2%	1.6%	1.1%	1.2%	1.4%
<b>Structure of equity and liabilities (proportion in %)<sup>9</sup></b>					
Amounts due to domestic banks	13.0%	12.6%	12.3%	12.4%	13.3%
of which to the <i>Deutsche Bundesbank</i>					3.7%
Amounts due to foreign banks	8.2%	7.5%	6.8%	7.0%	7.3%
Deposits from domestic non-banks	41.5%	40.9%	42.2%	39.7%	41.9%
Deposits from foreign non-banks	6.5%	6.4%	6.0%	5.6%	3.8%
Securitised debt including subordinated capital	11.3%	15.3%	11.8%	15.2%	13.5%
<b>Income statement structure (in % of average total assets)<sup>10</sup></b>					
Net interest income	1.09%	1.04%	1.07%	0.97%	0.94%
Net commissions received	0.36%	0.37%	0.36%	0.37%	0.37%
General administrative expenses	1.06%	1.07%	1.09%	1.06%	1.02%
Net trading income	0.04%	0.07%	0.04%	0.03%	0.04%
Operating profit/loss before measurement gains/losses	0.47%	0.42%	0.40%	0.33%	0.42%
Measurement gains/losses	-0.10%	-0.04%	-0.08%	-0.08%	-0.02%
Operating profit/loss	0.37%	0.37%	0.32%	0.26%	0.40%
Net amount of other and extraordinary income and expenses	-0.03%	-0.04%	-0.08%	-0.19%	n/a

	2016	2017	2018	2019	2020
Profit for the year before tax	0.33 %	0.33 %	0.23 %	0.07 %	n/a
Profit for the year after tax	0.24 %	0.24 %	0.15 %	-0.02 %	n/a

1 See chapter III.1.3 for the number of undertakings under supervision.

2 See chapter III.1.3 for further information on credit institutions in Germany.

3 Including financial services institutions.

4 Assets based on balance sheet statistics (BISTA) and data provided under the 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 Based on FinaRisikoV data.

9 Based on BISTA only. The "Securitised debt including subordinated capital" item also includes the FinaRisikoV data (financial services institutions, etc.).

10 The data for 2015 to 2019 was taken from publications by the *Deutsche Bundesbank* (monthly report on the performance of German credit institutions). The figures for 2020 have been based on the preliminary FinaRisikoV notifications and an approximate income statement structure has been given, since the 2020 annual financial statement data is not yet available in full.

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

		Life insurers				Private health insurers				Property/casualty insurers			
		2017	2018	2019	2020 <sup>2</sup>	2017	2018	2019	2020 <sup>2</sup>	2017	2018	2019	2020 <sup>2</sup>
Gross premiums written	(€ billion)	85.6	87.4	97.6	98.1	39.0	39.7	40.9	42.7	76.0	78.2	83.3	86.5
Investments	(€ billion) <sup>3</sup>	906.1	949.2	985.4	1,024.2	272.9	287.7	302.3	316.1	171.2	175.8	182.3	190.2
Average SCR coverage	(%) <sup>4,5</sup>	382.1	448.3	382.0	357.7	495.5	430.3	440.5	430.0	284.0	283.1	283.5	276.5
<b>Pensionskassen</b>													
		2017	2018	2019	2020 <sup>2</sup>								
Gross premiums earned	(€ billion)	7.3	7.2	6.8	6.5								
Investments	(€ billion) <sup>3</sup>	162.2	168.5	176.9	186.1								
Average solvency	(%)	133.7	135.1	139.7	138.4								
<b>Pensionsfonds</b>													
		2017	2018	2019	2020 <sup>2</sup>								
Gross premiums written	(€ billion)	2.4	10.2	2.6	5.0								
Investments	(€ billion) <sup>3,6</sup>	36.9	42.7	48.7	54.6								
Beneficiaries		942,782	1,058,215	1,112,677	1,171,314								
Benefit recipients		291,165	373,134	370,857	375,036								

1 See also chapter III.2 for the key figures for BaFin's Sector Insurance and Pension Funds Supervision.

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

3 Carrying amounts in accordance with the German Commercial Code (*Handelsgesetzbuch*).

4 Figure for the fourth quarter.

5 Up to and including 2018, certain undertakings were exempt from interim reporting requirements on SCR coverage in accordance with section 45 of the German Insurance Supervision Act (*Versicherungsaufsichtsgesetz*).

6 Total investments.

	2016	2017	2018	2019	2020
<b>Capital market companies<sup>1, 3, 4</sup></b>					
Supervised financial services institutions	708	722	722	706	710
Supervised branches	94	106	110	94	43
Total number of approvals <sup>1</sup>	1.652	1.405	1.174	1.097	904
of which prospectuses	348	301	303	291	301
of which registration documents	33	38	35	41	32
of which supplements	1.271	1.066	836	765	571
Authorised asset management companies <sup>2</sup>	136	142	146	143	143
Registered asset management companies <sup>2</sup>	260	309	379	404	431
Number of investment funds <sup>2</sup>	6.122	5.752	5.932	6.082	6.172
Assets under management by these funds (€ billion) <sup>2</sup>	1.908	2.062	2.062	2.391	2.551

1 Data comparability between different periods is limited, due to the change in the data collection method during the period under review.

2 The term "asset management company" (*Kapitalverwaltungsgesellschaft – KVG*) was only defined in 2013, when the German Investment Act (*Investmentgesetz*) expired and section 17 of the German Investment Code (*Kapitalanlagegesetzbuch – KAGB*) came into force. This fundamental change in the system means that comparative figures are not available for the years up to 2013.

3 See chapter III.3 3.5 for the number of undertakings under supervision.

4 See also chapter III.3.3.5 for information on the key figures for BaFin's Securities Supervision/Asset Management Sector.

**Key:**

n/a: not available.

Tier 1: the highest category of own funds.

KVG: 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*).

I

# Spotlights





# 1 COVID-19

## 1.1 Adjustments in response to the crisis

The entire world was dominated by the COVID-19 pandemic in 2020. Like many other institutions, BaFin suddenly found itself facing a threefold challenge: it had to protect its employees and help slow the spread of this novel coronavirus. It had to keep all its processes functioning as a public authority. And of course considerable demands were also placed on it as a supervisor.

Since BaFin offers staff the opportunity to work from home anyway, it was able to roll out large-scale working from home shortly after the pandemic started. To do this, it rapidly created additional IT capacity and adapted its organisational processes on the fly. As a result, it was able both to protect its employees and to continue functioning as a public authority. The lessons learned during the pandemic in 2020 are reinforcing BaFin's determination to make even greater use of state-of-the-art digital technology going forward.

Shortly after the pandemic struck, BaFin temporarily modified some aspects of its supervisory practice in order to allow financial sector companies to focus on their core business during the pandemic. "We have adapted our supervisory requirements in light of the

crisis", said BaFin President Felix Hufeld, summing up the temporary measures taken by BaFin since the outbreak of the coronavirus pandemic.<sup>1</sup> The measures are aimed at strengthening financial institutions and offering them relief to ensure that they are able to mitigate the effects of the crisis on the real economy.

### 1.1.1 Banking supervision

Right from the start, banks and *Sparkassen* had a key role to play in combating the economic effects of the coronavirus crisis. Among other things, they were tasked with implementing the special state aid programmes launched at the KfW, which BaFin helped to develop. BaFin also took suggestions from the banking sector into account when considering how to ease the burden on institutions. However, BaFin President Felix Hufeld emphasised that, in making the amendments, BaFin had only gone as far "as financial regulation, accounting standards and financial stability allow".

<sup>1</sup> BaFin has published its amended supervisory requirements on its website at [www.bafin.de](http://www.bafin.de) in the form of frequently asked questions (FAQs).

### **Simplified credit quality assessments**

BaFin published clarifying information about loans under the KfW instant loan program for which the federal government has fully exempted institutions from liability (i.e. in these cases the institutions themselves do not assume any liability). Above and beyond this, BaFin allowed institutions to perform simplified credit assessment procedures so as to process requests more quickly.

### **Flexible approach to governance requirements**

Equally, BaFin eased governance requirements for institutions as far as this was justified from a legal perspective. For instance, bank employees are also allowed to conduct trading activities from home during the coronavirus crisis. Normally, strict requirements must be met if such trading activities are conducted outside institutions' business premises. However, during an acute pandemic conducting trading activities from home does not constitute a breach of the Minimum Requirements for Risk Management (*Mindestanforderungen an das Risikomanagement – MaRisk*).

BaFin also permitted institutions to deploy staff more flexibly during the coronavirus crisis. For example, staff who normally only work in the internal audit function could also be seconded to other areas where resources were temporarily lacking, subject to certain conditions.

### **Deferred loan repayments**

Institutions deferred loan repayments due from customers right from the start of the coronavirus crisis. In the case of consumer loans, they did this by implementing the statutory payment moratorium set out in Article 240 (3) of the Introductory Act to the German Civil Code (*Einführungsgesetz zum Bürgerlichen Gesetzbuch*). They also helped their clients to overcome crisis-related liquidity bottlenecks by deferring payments on an individual basis or by participating in general payment moratoria as defined in the guidelines<sup>2</sup> issued by the European Banking Authority (EBA). These guidelines are set to expire on 31 March 2021.

### **New requirements: limiting the pressure on institutions**

BaFin also delayed publication of the updated version of the MaRisk, which was originally planned for the end of 2020, to 2021 in order to avoid putting any extra

pressure on institutions. The amended requirements were therefore not relevant for audits with the reference date of 31 December 2020.

### **SREP capital add-on suspended**

In addition, BaFin suspended the cycle for determining the capital add-on under the Supervisory Review and Evaluation Process (SREP) in 2020. The resets scheduled for 2020 were deferred and the capital add-ons already determined remained unchanged in 2020.

### **Changes to reporting requirements**

Reports and data on the current situation are especially important in times of crisis. Nevertheless, BaFin made some concessions towards institutions during the crisis as regards reporting, too. For example, BaFin did not raise any objections if it received certain reports late. The same approach also applied to the disclosure of accounting documents under section 26 of the German Banking Act (*Kreditwesengesetz*). BaFin did not investigate potential violations of statutory reporting deadlines in the period up to 30 June 2020.

### **Dividends**

BaFin appealed to the banking industry in 2020 not to make any untimely dividend payments or profit distributions so as not to weaken their capital base. BaFin made clear that it expected supervised entities intending to make a distribution to report their plans to it and the Deutsche Bundesbank before passing a binding resolution under company law. In such cases, BaFin examines extremely closely whether the banks' capital, liquidity, risk profile, internal capital adequacy and other factors are stable enough, including under stress conditions, to permit an appropriate distribution to be made.

### **How institutions are faring during the pandemic**

Hardly had the coronavirus pandemic hit when the question was asked as to how Germany's banking industry would cope with its consequences. As is known, institutions were already in a difficult position before this: earnings had been weak for years, interest rates low and digital competitors agile. At an operational level, institutions proved resilient right from the start of the crisis. Banking services were available more or less smoothly even during the lockdown. Economically, too, the German banks directly supervised by BaFin came through the crisis well in 2020. One of the main reasons is that the banking sector is now more robust than it was before the global financial crisis in 2007/2008. This is due above all to the tough regulatory reforms made since then. "These are to thank for the fact that we now have more liquidity in the banking system despite

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<sup>2</sup> <https://eba.europa.eu/regulation-and-policy/credit-risk/guidelines-legislative-and-non-legislative-moratoria-loan-repayments-applied-light-covid-19-crisis>.



strong demand resulting from the pandemic, and even though institutions are generally accommodating their customers' wishes for payment deferrals and are also extending new loans", underscored Raimund Röseler, BaFin's Chief Executive Director of Banking Supervision. Another key point is that banks now have thicker and better capital cushions thanks to the post-crisis reforms.

In the summer, BaFin and the Deutsche Bundesbank jointly simulated what could happen if there were to be a deep recession despite all the rescue packages. This exercise revealed that even if GDP were to slump by 10.8%, less significant institutions (LSIs) would have average Common Equity Tier 1 capital ratios of 11.2%. This is more than is required by law from the individual banks.

However, the question of how well banks will be able to deal with the fallout from the coronavirus pandemic depends to a very large extent on the trend in credit defaults. In the period up to the end of 2020, bank balances were still largely unaffected by major effects caused by the pandemic. Total earnings by all German banks declined only moderately (by about 8%) despite the pandemic.<sup>3</sup> The percentage of non-performing loans even fell slightly year-on-year compared to 2019. Equally, average impairment rates have not yet risen. This is probably due among other things to government support measures, as well as to the temporary and partial suspension of the requirement to file for insolvency.

Röseler also warns that "the longer the pandemic lasts, the more likely it is that we shall see credit defaults, despite all the efforts by governments and central banks. What is more, many problems are more deep-rooted – in banks' and savings banks' business models and processes. Their management boards must tackle these issues, make reforms, cut costs and get their institutions fit for the future, which will continue to be dominated by low interest rates. I also expect that isolated banks that were already weak anyway will not survive the pandemic."<sup>4</sup>

## 1.1.2 Insurance and pension fund supervision

BaFin also gave insurance undertakings some leeway in the area of reporting. For example, insurers subject to the European Solvency II supervisory regime were permitted to submit some reporting templates and the narrative part of their Solvency and Financial Condition Reports (SFCR) later.<sup>5</sup> Equally, they were allowed to perform the extensive Holistic Impact Assessment<sup>6</sup> required by the European Insurance and Occupational Pensions Authority (EIOPA) – in which insurers report how potential changes to Solvency II under the ongoing review process would impact them – two months later than originally scheduled. This was made possible by pushing back the deadline for submitting the opinion on the Solvency II review to the European Commission for half a year, to the end of 2020.

### Dividends

BaFin does not consider a blanket ban on distributing dividends by insurers and *Pensionskassen* to be justified. At the same time, it expects undertakings to keep their eye firmly on their capital base and future developments to it when examining whether to distribute dividends.

### Guarantee assets

In 2020, BaFin extended the deadlines for the guarantee assets (*Sicherungsvermögen*) that *Pensionsfonds* have to establish under their various pension plans. Where *Pensionsfonds* and employers agreed that additional contributions required to remedy underfunding would not be declared due immediately, the *Pensionsfonds* had to provide BaFin with a plan for re-establishing cover, since claims do not qualify as guarantee assets. In those cases in which BaFin approved this plan, it will not object to the underfunding. Previously, in cases of underfunding of between 5% and 10% BaFin required the plan for re-establishing cover, which details how the company intends to get back on track, to be submitted at the latest three months after the underfunding occurred.

In the case of *Pensionskassen* and small insurers that are required to invest guarantee assets on the basis of the German Regulation on the Investment of Guarantee Assets of *Pensionskassen*, Funeral Expenses Funds and Small Insurance Undertakings (*Anlageverordnung*), BaFin avoided emergency real estate sales being triggered under supervisory law provisions by temporarily not

3 See also 6.1 for further information on the situation at the banks.

4 See 6.1.

5 [www.bafin.de/dok/13847822](http://www.bafin.de/dok/13847822) (only available in German).

6 [www.bafin.de/dok/13869882](http://www.bafin.de/dok/13869882) (only available in German).

objecting to the proportion of investments in real estate exceeding 25%.

All insurance undertakings benefited from operational simplifications in that they only had to submit the hard copy register of guarantee assets as at 30 June 2020 – three months later than usual.

### **How insurers are faring during the pandemic**

The pandemic did not have any major impact on business in the insurance sector up to the end of 2020. The figure for life insurance premium waivers and cancellations rose moderately in the second quarter but normalised again in Q3.

In the health insurance area, customers only made limited use of the opportunity to defer premiums in connection with COVID-19. Equally, COVID-19 payments accounted for only a small proportion of overall benefits.

Premiums received by property and casualty insurers in 2020 were largely either stable or increased slightly. Declines were only seen in isolated lines of business that were hit particularly hard, such as medical expenses insurance, travel assistance insurance and business closure insurance.

### **Business closure insurance – a deeper dive**

A large number of businesses – especially in the hospitality trade – were officially ordered to close following the outbreak of COVID-19 in Germany. Some of these had taken out business closure insurance.

Special surveys by BaFin of the insurers concerned revealed that the general terms and conditions used on the market for such insurance generally vary. Dr Frank Grund, Chief Executive Director of Insurance and Pension Funds Supervision, commented on this as follows: “There are both cases that are clearly covered and claims for losses that are clearly unjustified and that cannot be met at the expense of policyholders as a whole. And then there’s a grey area.” As a result, it is not possible to say in general terms whether insurance policies cover the consequences of a pandemic or not. The courts have passed a small number of individual verdicts on this in the meantime, but no definitive final-instance decisions had been taken by the end of 2020.

### **Volatility adjustment**

Capital market volatility due to the pandemic and the further fall in interest rates led to a reduction in insurers’ own funds in the first quarter of 2020. However, their ability to meet regulatory solvency requirements did not change critically as a result. This is due among

other things to the stabilising effect of the volatility adjustment. Certain institutions for occupational retirement provision (IORPs) saw a decline in their valuation reserves, but this was also manageable given the coverage levels.

### **Risk and solvency assessments**

Insurers performed stress tests as part of their internal Own Risk and Solvency Assessments (ORSAs). A BaFin analysis shows that, overall, the insurance sector is well positioned to overcome a capital market scenario such as that seen in March 2020 in the medium term, too. The insurance sector’s liquidity position is generally good.

## **1.1.3 Securities supervision**

The key challenge for BaFin’s Securities Supervision Sector during the COVID-19 pandemic was to strike the right balance between ensuring effective investor protection and making adjustments to help the industry.

### **Working from home**

For example, investment services enterprises with staff working from home sometimes found it difficult to meet all of the requirements of the European Markets in Financial Instruments Directive II (MiFID II). Problems arose, for example, in relation to recording phone conversations electronically or providing customers with suitability reports and ex-ante cost information in good time. BaFin therefore made it clear that it will not investigate breaches of the directive if the companies in question take suitable alternative measures. What is essential is that they make the necessary effort and keep customers informed.

BaFin also made concessions towards asset management companies. It temporarily eased the strict rules governing asset transactions by investment funds to allow staff to work from home. Companies that had previously ruled out trading outside their business premises had to explicitly suspend this prohibition in some cases and provide clear guidelines as to the conditions under which, and for how long, the new rule would apply, and had to document this in their work instructions.

BaFin also adjusted its supervisory practice to the situation by largely allowing electronic submissions to replace original hard copies of documents. In addition, valuers of fund properties were permitted under certain conditions not to view the properties in person.

In certain cases, fund managers submitted their annual or half-yearly reports too late. Like other national

securities supervisors, BaFin did not make it a priority to pursue such cases. However, fund managers were requested to inform BaFin if they were unable to submit their reports by the relevant deadlines.

### The financial markets during the pandemic

The mood on the financial markets shortly after the outbreak of the pandemic was extremely nervous. This led to share prices plummeting and high outflows from certain funds. Fears of a renewed liquidity crisis as in 2007/2008 were voiced. However, the support provided by the fiscal authorities and the European Central Bank (ECB) led to a much calmer liquidity situation as early as April. Nevertheless, based on the lessons learned in comparable situations BaFin advised asset managers to safeguard their liquidity even more strictly than before using the new instruments offered by the German Investment Code (*Kapitalanlagegesetzbuch*) since the end of March 2020. BaFin was in close communication with the sector on the concrete implementation of these measures.<sup>7</sup>

### Trading activity during the coronavirus crisis studied

BaFin conducted a study to examine trends in trading activity on the German market since the onset of the coronavirus crisis in February 2020. This revealed that trading by retail investors has increased considerably in the period since then. Trading in shares has risen in particular. Another finding that applied especially to shares in DAX-listed companies was that purchasing volumes substantially outstripped sales from the beginning of March onwards. In addition, trading in leverage certificates and contracts for difference (CFDs) increased.

## 1.1.4 Combating money laundering

Even during the coronavirus pandemic, combatting money laundering and terrorist financing remains a core priority. When identifying the recipients of state-aided loans, banks can apply the simplified due diligence requirements under section 14 of the German Money Laundering Act (*Geldwäschegesetz*). These state, among other things, that a copy of identification documents is sufficient. However, this requires that there is only a small risk of money laundering or terrorist financing. If, over the course of a business relationship, ongoing customer and transaction monitoring suggests a higher risk is involved, the banks must take additional measures, such as subsequently performing personal identification procedures in which original identity documents are submitted.

<sup>7</sup> See also 9 for information on the new liquidity tools.

## 1.1.5 Authorisation requirement

BaFin provided relief for real-economy SMEs in particular with its decision regarding authorisation requirements for guarantees. If suppliers run out of funds and are therefore unable to supply their customers, this can quickly lead to production being halted. In order to prevent this from happening, customers often want to act as guarantors.

BaFin therefore clarified that, in such cases, customers are not deemed to be conducting guarantee business within the meaning of section 1 (1) sentence 2 no. 8 of the Banking Act, nor do they have to obtain authorisation from BaFin. This also applies if the customers provide guarantees for numerous suppliers. However, guarantors are not permitted to charge fees for these guarantees.

# 2 Wirecard

The events surrounding financial services provider Wirecard AG shook trust in Germany as a financial centre. On 22 June 2020, the Aschheim-based company published an ad hoc disclosure, stating that there was “a prevailing likelihood that the bank trust account balances in the amount of €1.9 billion do not exist”<sup>8</sup>. On 18 June 2020, Wirecard AG had already announced in an ad hoc disclosure that the publication date for the annual and consolidated financial statements for 2019 would be delayed due to indications of presentation of spurious balance confirmations.<sup>9</sup> The share price for the payment services provider plummeted after the two disclosures. On 25 June 2020, Wirecard AG filed an application to open insolvency proceedings due to imminent insolvency and overindebtedness.<sup>10</sup> Then, on 24 August 2020, the technology group exited the DAX and the TecDAX. Insolvency proceedings were opened one day later.

<sup>8</sup> Ad hoc disclosure by Wirecard AG dated 22 June 2020: Statement of the Management Board about the current situation of the Company, [https://www.wirecard.com/wp-content/uploads/2021/01/AH\\_2020\\_06\\_22\\_Stellungnahme-Vorstand.pdf](https://www.wirecard.com/wp-content/uploads/2021/01/AH_2020_06_22_Stellungnahme-Vorstand.pdf).

<sup>9</sup> Ad hoc disclosure by Wirecard AG dated 18 June 2020: Date for publication of annual and consolidated financial statements 2019 delayed, <https://www.wirecard.com/2020/06/18/wirecard-ag-date-for-publication-of-annual-and-consolidated-financial-statements-2019-delayed-due-to-indications-of-presentation-of-spurious-balance-confirmations/>.

<sup>10</sup> Ad hoc disclosure by Wirecard AG dated 25 June 2020: Application for opening of insolvency proceedings, [https://www.wirecard.com/wp-content/uploads/2021/01/AH\\_2020\\_06\\_25\\_Antrag-Insolvenz.pdf](https://www.wirecard.com/wp-content/uploads/2021/01/AH_2020_06_25_Antrag-Insolvenz.pdf).

## Numerous reforms

BaFin has been criticised for its handling of Wirecard. This also applies to its February 2019 prohibition on short selling the shares of the company and to its filing of a criminal complaint with the public prosecutors regarding suspected market manipulation in April 2019.

As a result, calls were made immediately after the alleged accounting fraud became known to throw light on the Wirecard case and to reform both the law and BaFin.

In July 2020, Federal Minister of Finance Olaf Scholz presented the Government Action Plan to Combat Financial Reporting Fraud and to Strengthen Controls over Capital and Financial Markets<sup>11</sup>. One of the key focuses is a fundamental reform of the financial reporting enforcement system.

## German Act to Strengthen Financial Market Integrity

Revamping financial reporting enforcement is one of the key elements of the draft German Act to Strengthen Financial Market Integrity (*Gesetz zur Stärkung der Finanzmarktintegrität – FISG*). This was submitted by the Federal Ministry of Finance (*Bundesministerium der Finanzen*) and the Federal Ministry of Justice and Consumer Protection (*Bundesministerium der Justiz und für Verbraucherschutz*). The draft was adopted by the Federal Cabinet in December 2020. The FISG implements key elements of the Action Plan mentioned above. It aims to give BaFin extensive new powers, enabling it to officially intervene more rapidly in the future. Another goal is to establish clear responsibilities. For example, BaFin is to be solely responsible for examinations with cause in the future. Although the FISG provides for the creation of a financial enforcement body under private law, this body will only be responsible for random checks and will interact more closely with BaFin. It will report regularly to BaFin and be required to supply supervisors with information on request to a far greater extent than before.

BaFin will be strengthened in other areas as well. The FISG will increase its official powers with respect to third parties. The aim is to give supervisors direct powers of intervention with respect to companies to which material banking functions are outsourced. This practice

is common in the financial sector, but in some cases can make it difficult to identify risks early enough. The goal is to enable BaFin to uncover such risks more quickly, and manage them more effectively in future.

The Wirecard case also shows that the traditional supervisory approach is not suitable for all supervised credit institutions. For example, Wirecard Bank's solvency and liquidity indicators did not reveal the in some areas disastrous situation at Wirecard AG. BaFin therefore drew up initial reforms designed to remedy this weakness in 2020. The draft FISG also addresses this topic.

## Employee transactions

The FISG also largely prohibits BaFin employees from trading in financial instruments – a move welcomed by BaFin. In line with this, the authority has already tightened its rules on employee transactions ahead of the new legislation. Since 16 October 2020, employees in risk category A may no longer conduct any private transactions in financial instruments of financial corporations that are headquartered or have branch offices in the European Union (EU). Risk category A covers all employees with access to inside information by virtue of their official duties, i.e. due to the tasks they perform. This comprises more than 85% of all BaFin staff.

In June 2020, BaFin launched a special review of employee transactions relating to Wirecard AG.<sup>12</sup> The objective was to find out whether employees illegally used inside information to which they had access due to the tasks they perform when conducting such transactions. The special review covered transactions reported by risk category A employees in the period between 1 January 2018 and 30 September 2020. BaFin appointed auditing firm Deloitte to audit the special review and has published the results of the special review and of the audit on its website.<sup>13</sup>

## Organisational review

The Wirecard case also revealed a number of weaknesses in BaFin's structures. As a result, the Federal Ministry of Finance launched an organisational review at BaFin. Consulting firm Roland Berger was commissioned to perform this.

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<sup>11</sup> Federal Ministry of Finance, Government Action Plan to Combat Financial Reporting Fraud and to Strengthen Controls over Capital and Financial Markets.  
[https://www.bundesfinanzministerium.de/Content/DE/Downloads/Finanzmarktpolitik/2020-10-08-aktionsplan-bekaempfung-bilanzbetrug.pdf?\\_\\_blob=publicationFile&v=2](https://www.bundesfinanzministerium.de/Content/DE/Downloads/Finanzmarktpolitik/2020-10-08-aktionsplan-bekaempfung-bilanzbetrug.pdf?__blob=publicationFile&v=2).

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<sup>12</sup> See chapter V.3.

<sup>13</sup> [www.bafin.de/dok/15570054](http://www.bafin.de/dok/15570054) (only available in German).

One of the Ministry's overarching objectives is to make BaFin's supervisory and audit activities more effective, with respect both to classic solvency supervision and to conduct supervision in the areas of investor and consumer protection. In addition, it is planned to streamline internal structures and procedures and make better use of the opportunities offered by state-of-the-art technology.

To achieve these goals, the Federal Ministry of Finance developed a seven-point plan for reforming BaFin. This provides for the following measures, among others<sup>14</sup>:

A focus unit will be created for overseeing complex companies. This unit will cover all BaFin sectors and supervise companies even more closely than before. In addition, a new, forensically trained task force will be created to enable BaFin to perform ad hoc and special audits independently in future; where appropriate, this will be done on site in cooperation with the public prosecutor's office.

BaFin is also to be given substantially expanded rights of access. These are designed to give BaFin the authority to perform forensic audits independently at a minimum at the level of intervention that allowed the financial reporting fraud at Wirecard to be uncovered. Equally, information sharing with market participants will be stepped up and whistleblowers' insights will be systematically captured and analysed.

In the area of investor and consumer protection, BaFin's powers will be strengthened in particular by introducing mystery shopping. Other tools for proactive investor and consumer protection, such as active market monitoring, are to be expanded. Regular in-depth discussions with consumer and investor protection advocates will also be sought and the lessons learned from these will be incorporated into BaFin's supervisory work.

The Federal Ministry of Finance and BaFin aim to produce the first interim results from the reform project by August. The goal is to complete the entire project by the end of the year.

## 3 Brexit

Negotiations on a free trade agreement between the European Union and the United Kingdom proved to be an almost never-ending story. The United Kingdom had already formally left the EU at the end of January 2020. The transitional period during which the country nevertheless remained part of the Single Market and the Customs Union ended eleven months later. A breakthrough was not achieved until the end of December 2020, i.e. shortly before the deadline: the two parties reached an agreement comprehensively regulating their relationship in many areas of economic life.

The agreement entered into force, initially provisionally, on 1 January 2021. The European Parliament had not approved its permanent application by the end of 2020. What is more, the agreement only applies to financial services to a limited extent. In this area, EU and UK supervisory law will continue to apply unless other agreements are reached – for example on the basis of equivalence decisions by the European Commission.<sup>15</sup>

What is clear, however, is that financial services providers resident in the United Kingdom have not been able to use European passporting rights since 1 January 2021. They no longer have direct access to the entire European Economic Area (EEA) and therefore also cannot provide cross-border financial services there. One of the alternatives is to establish a subsidiary in an EEA state that can use European passporting rights, or to expand existing representative offices. Any entities wishing to make use of this without interruption had to have done so by 31 December 2020. Roughly 60 or so financial undertakings chose Germany as their preferred location and established a presence, or substantially expanded their business, here before the end of the year.

In order to allow them to transition smoothly and avoid market chaos, BaFin informed companies wanting to relocate very early on of the legal framework they could expect here and the preparations they should be making. Now, BaFin considers it extremely important that its close ties to the UK's supervisory authorities remain in place.

<sup>14</sup> Federal Ministry of Finance, Press release: More "bite" for the Financial Supervisory Authority, [https://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Financial\\_markets/Articles/2021-02-03-more-bite-for-the-financial-supervisory-authority.html](https://www.bundesfinanzministerium.de/Content/EN/Standardartikel/Topics/Financial_markets/Articles/2021-02-03-more-bite-for-the-financial-supervisory-authority.html).

<sup>15</sup> See [www.bafin.de/dok/15105408](http://www.bafin.de/dok/15105408).

## 4 Digitalisation

### Is COVID-19 accelerating digitalisation?

The financial industry has been undergoing a fundamental digital transformation process for some time now. In 2020, the sector had to cope with the COVID-19 pandemic<sup>16</sup> as well. Both staff and customers were forced to relocate a large part of their activities to a virtual environment. As a result, the assumption was quickly voiced that the pandemic would accelerate further innovation in the financial sector.

BaFin observed two parallel trends: Firstly, established banks in particular focused less on innovation overall at the start of the pandemic. Understandable enough, other topics were more important. Institutions were busy working to mitigate the devastating consequences of the coronavirus pandemic on the real economy.<sup>17</sup> On the other hand, though, greater use of digital offerings such as online banking and online advisory services was made throughout. BaFin therefore also sees the pandemic as a test for such services.

### Dealing with algorithmic decision-making processes

One topic that BaFin continued addressing in depth in 2020 was algorithmic decision-making processes. BaFin has already stated its position on these several times, including in an expert article published in April 2020<sup>18</sup>. This makes clear that, with very few exceptions, BaFin does not approve of algorithmic decision-making processes. Nevertheless, many market participants would like to obtain BaFin's consent even before an algorithm is deployed. Such a practice would not be feasible, nor would it make sense for most of the algorithms used. This is because the critical factor with algorithms is how supervised entities actually incorporate them into their decision-making processes. This is why BaFin focuses not on the algorithm alone but on the overall decision-making process – from the data to the results – and on the associated risks. As a matter of principle, BaFin reviews such processes independently of the technology involved in the course of its ongoing supervisory activities.

Special cases that are regulated by law are an exception to this rule. However, BaFin does not grant general approval in such cases but examines whether a

procedure is fit for purpose. This is the case, for example, with internal models used by banks and insurers to determine their regulatory capital requirements.

In 2020, BaFin decided to publish a paper on this topic in order to provide guidance to undertakings. Another aim is to contribute to the international discussion on this subject. The paper was scheduled to be published in March 2021.

### Working group on machine learning in internal risk models

In 2020, BaFin established a working group on "machine learning in internal risk models" that is looking at using machine learning (ML) methods in the context of internal models for banks and insurance companies.

The current regulations are largely principles-based and technology-neutral. Therefore, the use of machine learning does not present BaFin with any fundamentally new challenges when auditing internal risk models. Nevertheless, it is conceivable that interpretations and the practical application of the regulations – or indeed the regulations themselves – may need to be refined in certain cases.

The working group is looking at concrete application cases here. It is recreating ML methods such as neural networks and investigating these under laboratory conditions. BaFin is also closely tracking developments in ML processes in order to be able to identify any need for changes early on. It does this by exchanging information and in discussions with the sector and with other supervisory authorities.

### BaFin tests new "TechBridge" information sharing format

The digital innovation spiral is making regular information sharing with the sector more and more important. In 2020, BaFin tested new information sharing formats as part of its "BaFin TechBridge" project. What is special about this is that innovative undertakings that are not (yet) (directly) supervised were able to use technology workshops with BaFin's teams of experts to discuss unclear issues and cases of doubt, plus areas where interpretations might be missing. The feedback on this new format was extremely positive, and BaFin is therefore examining whether and how it can make it a permanent fixture.

### Supervisory upgrade: the digital agenda set by BaFin and the Bundesbank

In 2020, BaFin's Banking Supervision Sector and the *Deutsche Bundesbank* established a milestone for the

<sup>16</sup> See 1.

<sup>17</sup> See I.1. and III.1 for further information on the measures taken by banks and banking supervisors in reaction to the COVID-19 pandemic.

<sup>18</sup> See <https://www.bafin.de/dok/14009206>.

future of supervision. The two institutions defined their strategic supervisory objectives in a joint digital agenda.<sup>19</sup>

More specifically, BaFin and the Deutsche Bundesbank defined three areas of innovation for themselves:

1. Data will be obtained and processed more quickly and easily. Instead of requesting information to be reported by a specific deadline as part of an inflexible procedure, supervisors should be able to obtain the information they need from the institutions directly if and where required. Ideally, supervisors would be able to gather more up-to-date and more precisely tailored information without overburdening the banks.
2. The quality of analyses will be enhanced: for example, supervisors should be able to easily access, link and analyse all of the available data and information regarding a bank. This relates not only to reporting data but also to information from the media, analysts and other sources. Evaluating large volumes of data using artificial intelligence, for example, enables new warning functions to be created.
3. Finally, internal processes – including those linking BaFin and the Deutsche Bundesbank – will be optimised and a common desktop should allow a joint view of the data and information at all times.

Raimund Röseler, Chief Executive Director of Banking Supervision, underscores the fact that the joint BaFin/Deutsche Bundesbank digitalisation initiative is primarily intended to help the people working in supervision: “Supervisors will continue to be the ones who assess information and ultimately reach decisions. Even the best algorithm cannot replace human judgement. Nevertheless, the digital agenda will certainly help supervisors reach decisions on the best possible informational basis.”

### Internal digitalisation at BaFin

However, digitalisation is not just a challenge for BaFin in its supervisory activities. Progress in this area will also increasingly change the way BaFin organises its work. BaFin recognised this early on and started developing plans for its digital future. The digitalisation strategy<sup>20</sup> that it published in the summer of 2018 devotes a separate area of activity to internal digitalisation at BaFin.

BaFin continued making systematic progress with the individual topics making up this area of activity in 2020. It has identified six core areas: information gathering, information analysis, process support, the digital literacy of its staff, cooperation and networking, and digital culture.

The key measures planned with respect to digital process support across all BaFin sectors is the introduction of an electronic file (“e-file”). The use of big data and artificial intelligence to combat market abuse is being expanded in order to strengthen information analysis. In addition, BaFin is successively linking information – including across different BaFin sectors – to create new ways of evaluating and analysing data. The above-mentioned points from BaFin and the Deutsche Bundesbank’s joint digital agenda are only one example of this. The goal is for state-of-the-art technology and digital processes to help further extend BaFin’s strengths as an integrated supervisory authority.

As Béatrice Freiwald, Chief Executive Director of Internal Administration and Legal Affairs, says: “Becoming a digital authority is a complex, dynamic process. Increasing digitalisation is fundamentally changing both the way we work and our workflows. Digital transformation demands that we redefine what supervision means in certain areas and think outside the box. However, this makes us stronger as an authority and will help us perform our tasks in the future, too.”

<sup>19</sup> [www.bafin.de/dok/15039048](http://www.bafin.de/dok/15039048).

<sup>20</sup> [www.bafin.de/dok/12126168](http://www.bafin.de/dok/12126168).

## 5 Sustainable finance

The entire world was dominated by the COVID-19 pandemic in 2020. However, other topics such as combating climate change have not become less important. The period between June and August 2020 was the warmest summer ever recorded in the Northern Hemisphere.<sup>21</sup> Worldwide, the ten warmest years since records began have all been since 2005.<sup>22</sup> Global warming is already dangerously close to the critical 1.5 degrees mark. This means that enormous efforts still have to be made if we are to achieve our goal of greenhouse gas neutrality by 2050. Banks, insurers and investment firms could also find themselves confronted by climate-related risks in many areas in the near future.

2020 saw a number of regulatory developments regarding sustainability – something that BaFin welcomes.<sup>23</sup> BaFin considers the Taxonomy Regulation<sup>24</sup>, which defines environmentally sustainable economic activities and which was published in June 2020, to be a milestone on the road to sustainability. The regulation sets standards for the development of sustainable financial products for the first time and, above and beyond this, could also drive a change in behaviour across the financial sector.

In addition, BaFin welcomes the various activities by the European supervisory authorities in which it was involved, and the ECB's Guide on climate-related and environmental risks. This was inspired among other things by BaFin's Guidance Notice on Dealing with Sustainability Risks. BaFin also considers its supervisees' efforts to ensure sustainability risks are adequately managed as positive. The BaFin Guidance Notice provided important input here. BaFin's continues to consider it important to recognise both the opportunities associated with a sustainable financial sector and the risks involved in transforming the economy and in changing environmental and social conditions, and to deal with these adequately. However, it must also be clear that, just like conventional financial products, sustainable products are not risk-free.

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21 NOAA, Northern Hemisphere just had its hottest summer on record, <https://www.noaa.gov/news/northern-hemisphere-just-had-its-hottest-summer-on-record>.

22 NCEI, NOAA study: Most of the years in next decade very likely to rank as Top 10 warmest years, <https://www.ncei.noaa.gov/news/projected-ranks>.

23 A comprehensive list of regulatory projects in 2020 can be found on BaFin's website at [www.bafin.de/dok/15590998](http://www.bafin.de/dok/15590998) (only available in German).

24 Regulation (EU) 2020/852 dated 18 June 2020.

## 6 Low interest rate environment

### 6.1 The situation at credit institutions

Low interest rates have been impacting the earnings situation at German banks for more than a decade now. There is no immediate end to the trend in sight. In fact, the ECB has even expanded its proactive monetary policy in order to contain the impact of the COVID-19 pandemic; its Pandemic Emergency Purchase Programme (PEPP) now has a volume of €1,850 billion. These measures have already been prolonged until March 2022. This means that German banks' net interest income is also likely to remain under pressure.

Aggregate net interest income recorded a slight decline year-on-year for 2020 as a whole. By contrast, other sources of earnings remained relatively stable and, as in the case of net fee and commission income, exceeded last year's levels. In addition, German banks and savings banks succeeded in cutting administrative expenses slightly in 2020. As a result, the cost-income ratio for the German banking sector improved somewhat year-on-year, but is still well above the European average.

### 6.2 The situation at insurers and *Pensionskassen*

Low interest rates continued to put pressure on insurance undertakings in 2020 – life insurers in particular faced major challenges as a result of the persistent low interest rate environment. However, Dr Frank Grund, Chief Executive Director of Insurance and Pension Funds Supervision, did not consider them to be failing or in danger of doing so: "I am working on the assumption that German life insurers overall are robust enough to survive the coming years". Nevertheless, BaFin monitored economic developments and risk-bearing capacity at life insurers in depth, with roughly 20 undertakings being tracked particularly closely.

Grund expressed his concern that low market rates could become a problem if the gap to guaranteed interest rates were to increase further: "Only those life insurers that can actually generate the maximum technical interest rate over time should be using it."

Many *Pensionskassen* have been suffering under the low interest rates for a long time. The COVID-19 pandemic<sup>25</sup>

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25 See 1.



put a significant brake on hopes of an interest rate turnaround. Consequently, Chief Executive Director Grund remarked several times that *Pensionskassen* would be well advised to increase their provisions for existing insurance portfolios. However, he also said that whether their sponsors and shareholders can help *Pensionskassen* would depend on how they themselves are doing. BaFin made clear to regulated *Pensionskassen* that it would no longer approve guaranteed interest rates in excess of 0.25% for an unlimited period. At the end of December 2020, BaFin was closely supervising an unchanged number of 36 *Pensionskassen*.

Lawmakers took the opportunity of the low interest rate period to extend the protection offered by the Pension Security Association (*Pensions-Sicherungs-Verein*) to *Pensionskassen* as well. This protection relates to commitments for occupational retirement provision and *Pensionskassen* that are not already protected by the guarantee scheme under section 223 of the German Insurance Supervision Act (*Versicherungsaufsichtsgesetz*).

## 7 Money laundering prevention

In 2020, BaFin contributed its expertise in the field of money laundering prevention to European bodies that were discussing a number of reforms. For example, in 2020 the European Commission was working on a comprehensive programme to harmonise money laundering regulations. The objective is to use a binding EU-wide regulation to set down certain money laundering prevention requirements – such as the need to identify customers as part of customer due diligence requirements – in future. To date, the relevant requirements are only set out in the EU Money Laundering Directive and must be implemented and fleshed out in practice by the individual member states. This gives rise to a certain room for manoeuvre, which is also being used. By contrast, a regulation would have to be implemented directly. Another advantage would be that it could pave the way for the formation of a European Anti-Money Laundering Authority. However, the regulation is not expected to be adopted before 2022.

The question also arises as to where such an authority should be located. The European Central Bank (ECB)'s banking supervisory operations and the European Banking Authority (EBA) are being discussed in this

context. Another possibility would be to establish a new, independent authority.

Dr Thorsten Pötzsch, BaFin's Chief Executive Director responsible for the prevention of money laundering, welcomes the plans to create a European anti-money laundering supervisor. He is in favour of a new, independent authority: "Such a new, independent authority offers a wide range of possible ways of approaching the important topic of money laundering prevention efficiently and effectively. However, whether a new authority is actually established at the end of the day or whether a new unit is created at the ECB or the EBA will be the result of political negotiations".

### **Credit institutions must store certain virtual IBANs in the account information access system**

In 2020, BaFin received an increasing number of indications from law enforcement agencies that virtual International Bank Account Numbers (IBANs) were being misused, e.g. for fraud during online retail sales. Credit institutions had issued the virtual IBANs to intermediary payment services providers, most of which were located abroad. In turn, these passed them on to their customers. The people making the payments were under the impression that the accounts were maintained in Germany. In reality, however, the money was paid to an account abroad. In many cases the perpetrators could not be identified. However, there were also indications that virtual IBANs had been misused for terrorist financing.

As a result, BaFin issued a general administrative act on 8 December 2020 according to which credit institutions are required to store virtual IBANs that they issue to payment services providers for passing on to their end customers in the account information access system (section 24c (1) of the Banking Act). Credit institutions must also enter the name of the end customer that receives a virtual IBAN from a payment services provider.

Credit institutions that issued virtual IBANs before the new general administrative act came into force must enter the missing information completely and correctly in the file system within six months. If they do not do this, there are two possibilities: Either they must terminate the accounts of the payment services provider used to settle the virtual IBANs that have been issued without undue delay. Or they have to take other suitable measures to ensure that virtual IBANs that have already been issued can no longer be used. Chief Executive Director Pötzsch emphasised how important this measure is: "If something looks like an account and can be used like an account, it must also meet the legal

requirements for an account. This also includes adding virtual IBANs to the account information access file. This measure increases the reliability of account information access – which is a great help for law enforcement agencies.”

## 8 Solvency II review

In the period up to the end of 2020, the European Commission requested EIOPA to perform a regular review of selected elements of the Solvency II Framework Directive<sup>26</sup>. This found that the framework had proven its worth but that it needed tightening up in some areas. Now it is up to the European Commission to submit a proposal on this basis.

### **EIOPA proposal as a compromise**

The proposal submitted to the European Commission by the European Insurance and Occupational Pensions Authority (EIOPA) at the end of 2020 was produced with BaFin’s assistance. The deadline for submission – 30 June 2020 – was postponed due to the pandemic. Dr Frank Grund, Chief Executive Director of Insurance and Pension Funds Supervision, saw the EIOPA proposal as a “compromise where we, too, had to make concessions, but one that I consider to be reasonably acceptable overall. What was important for us”, he continued, “was to ensure that the long-term business that is typical for the German insurance sector is still possible in a regulatory system that is even more market-oriented, as is provided for by the review.”

### **Long-term guarantees**

In line with this, Grund also welcomed the measures proposed in relation to long-term guarantees (LTGs). One of the most commonly used LTG measures in Germany at present is volatility adjustment. A total of 86 German undertakings used this in 2019, including 58 life insurers. Volatility adjustment has proven its worth not only in stress tests but also in real-life stress situations, such as the market turbulence caused by the coronavirus pandemic in the spring of 2020. However, the current volatility adjustment mechanism is not perfect in BaFin’s opinion. Among other things, it cannot take the features of the liabilities involved into account.

The new volatility adjustment mechanism aims to take the illiquidity of obligations into account and to kick in earlier so as to stabilise solvency capital results during turbulent periods. “A good idea”, was how Grund sums this up.

However, the Chief Executive Director was critical of the changes to the way the interest rate term structure is extrapolated that were proposed by EIOPA: “These would negatively impact German life insurers”, he pointed out. This is because the alternative method also factors in market information after the starting point for extrapolation – in the case of the euro, this means market information for the period beyond 20 years. If interest rates were to remain extremely low, this would lead to a lower interest rate term structure for the extrapolated portion. It is true that EIOPA has provided for an “emergency brake” mechanism, which is intended to ensure that the size of the provisions to be recognised remains manageable for insurers even in difficult market situations. However, this mechanism is only temporary. Capital requirements for German life insurers, with their extremely long policy terms and high guaranteed interest rates from the past, would still rise successively and substantially in the period up to 2032. In Grund’s opinion there is still room for improvement in this area.

### **BaFin advocates greater proportionality**

In order to reduce the burden on lower-risk – and hence generally smaller – undertakings, BaFin again advocated further developments to the idea of proportionality in 2020 in the context of the work on the EIOPA proposal. For example, BaFin proposed raising the entry threshold for Solvency II – something that EIOPA included in its proposal. In addition, EIOPA has proposed simplifying the way in which the Solvency Capital Requirement (SCR) is calculated, plus relief for calculating the technical provisions.

### **Relief planned for reporting**

Additional relief is planned for reporting. EIOPA is proposing that undertakings should only submit non-core templates if they exceed the risk-based thresholds (which can also be qualitative in nature) determined for these. BaFin welcomes this approach. In addition, the Solvency and Financial Condition Report (SFCR) and the Regular Supervisory Report (RSR) are to be slimmed down. The SFCR is also to be made more suitable for its target audience, with a brief two-page summary for policyholders and a more detailed section for professional readers. BaFin agrees with these proposals as well.

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<sup>26</sup> Directive 2009/138/EC, OJ EU L 335/1.

The European Commission is currently examining the EIOPA proposal, after which it will make a proposal on its implementation to the European Council and the European Parliament. After this, the trilogue negotiations will start; it is uncertain how long this process will take.

## 9 Improved liquidity management for open-ended investment funds

Since 28 March 2020, asset management companies have been able to better manage the liquidity of their open-ended investment funds. The German Investment Code (*Kapitalanlagegesetzbuch*) offers three ways of doing this: redemption notice periods, redemption gates and swing pricing.

Before these instruments were introduced, asset management companies had no alternative in the case of liquidity bottlenecks: if an investment fund did not have sufficient liquidity to service all redemption requests, it had to suspend the redemption of the units – a move that had serious consequences for investors. In such cases, they could not return their units to the investment fund until further notice. The new tools and measures are designed to prevent this difficult situation for investors. As a result, BaFin is convinced that the new liquidity tools serve to protect investors. It therefore expects asset management companies to examine in detail whether they will make use of these new tools, and if so, which ones.

### Redemption notice periods

Asset management companies can now introduce redemption notice periods. This means that investors would be required to give advance notice if they wish to make a redemption request. This redemption notice period then applies permanently and to all redemption requests. In the case of open-ended retail investment funds, the notice period may not exceed one month.

### Redemption gates

Another option involves redemption gates once a certain threshold has been reached. If investors' requests for redemptions on a redemption date are so numerous that a threshold previously set by the asset management company is exceeded, the latter can restrict unit redemption. However, this only applies for a maximum of 15 working days. In the case of open-ended retail investment funds, asset management companies must publish information on the imposition and lifting of redemption gates on their websites.

Redemption gates are designed to help asset management companies overcome short-term liquidity bottlenecks that arise when investors return very large numbers of units. The aim is to avoid asset management companies having to suspend unit redemption.

### Swing pricing

The third tool – swing pricing – allows transaction costs associated with the redemption or issuance of units to be passed on to their originators: the costs can be included in the calculations of a fund's net asset value (NAV). Asset management companies can either permanently adopt swing pricing or trigger it if a certain threshold is exceeded for net redemptions or subscriptions ("partial swing pricing").

If a very large number of investors want to return their units and the asset management company is forced, for example, to sell assets, the resulting transaction costs can be passed on to those investors who are returning their units. This is done by reducing the unit price. At the same time, it would not affect the remaining investors in the fund.

## BaFin's supervisory priorities in 2020

BaFin also adapted its supervisory priorities for 2020<sup>27</sup> in some areas in light of coronavirus pandemic. Originally, BaFin had identified the following priorities for all of its sectors:

1. digitalisation, IT risk and cyber risk
2. the integrity of the financial system and the fight against financial crime
3. sustainable business models
4. sustainable finance

After the pandemic broke out, the main focus of supervisory activity switched to closely monitoring the solvency of supervised undertakings. However, since these, too, moved over to working from home, additional cybersecurity issues also took centre stage.<sup>28</sup>

Despite the extraordinary situation, however, the sectors continued to pursue what are in most cases multi-year supervisory priorities. The following provides an overview.

### Banking Supervision

Shortly after the onset of the coronavirus pandemic<sup>29</sup>, BaFin granted institutions a series of limited-term supervisory relief measures.<sup>30</sup> In addition, it monitored them closely throughout 2020. Regular discussions with the institutions plus its own stress scenarios, among other things, provided it with insights.

As part of its "digitalisation, IT risk and cyber risk" supervisory priority, BaFin asked credit institutions, payment services providers and undertakings providing key IT services to the financial sector how they were dealing with the consequences of the pandemic and how, for example, they were mitigating IT risk. It also called on the institutions to inform it without undue delay of material new developments, such as any potential threats to

critical processes. Some of the inspections focusing on IT risk management that were performed in 2020 took place off-site.

BaFin also addressed the topic of multi-client service providers in the financial sector in detail as part of its "digitalisation, IT risk and cyber risk" activities. Above and beyond this, the focus was on the strong customer authentication for online payments introduced by the revised Payment Services Directive 2 (PSD2). BaFin worked closely with the undertakings involved on its implementation.

Activities performed in relation to the "sustainable business models" supervisory priority included follow-up work on the most recent stress test for less significant institutions (LSIs) and on the survey on real estate financing and credit standards. BaFin discussed conspicuous findings with the institutions and took supervisory measures where necessary.

### Insurance Supervision

In addition to the coronavirus pandemic<sup>31</sup>, Insurance and Pension Funds Supervision paid close attention to the "sustainable business models" supervisory priority. Ongoing low interest rate levels remain a cause for concern at many life insurers and *Pensionskassen*. BaFin is continuing to monitor these undertakings closely. For example, the projections for 2020 surveyed the economic situation and BaFin also asked life insurers about Solvency II requirements for the first time. Evaluation of the findings had not been completed as at the end of 2020. However, life insurers have already been shown to be robust enough to meet their existing obligations in the future, based on the requirements set out in the German Commercial Code (*Handelsgesetzbuch*). At the same time, undertakings must make more of an effort to comply with the requirements relating to the *Zinszusatzreserve* (the additional interest provision).

27 [www.bafin.de/dok/13918786](http://www.bafin.de/dok/13918786).

28 See 1.1.1.

29 See 1 and chapter III.1.

30 See 1.

31 See 1 and chapter III.2.

Insurance Supervision also closely monitored how real estate prices and capital market trends impacted insurers in 2020. BaFin's comprehensive analyses showed that real estate exposure (a single-digit percentage of all investments overall) represented a manageable risk for the surveyed undertakings' capital resources. A significant proportion of the undertakings had reduced the measurement amounts for directly held commercial real estate in line with Solvency II.

Corporate loans remained highly important to the sector in 2020. Although BaFin noted a slight increase in weaker credit ratings, there were no indications that rating downgrades and expected write-downs might impact insurance undertakings on a broad front. In addition, BaFin analysed the risk of a bond rating downgrade. This found that indirect holdings of such bonds could indeed be a cause of potential losses. However, BaFin considers this risk to be still acceptable as at the end of 2020.

### Securities Supervision

As part of the "digitalisation" supervisory priority, Securities Supervision<sup>32</sup> helped the BMF develop a German Electronic Securities Act (*Elektronisches Wertpapiergesetz*) in 2020. At the same time, BaFin's Securities Supervision Sector helped formulate a common regulation for these previously unregulated instruments at European level. In the area of investment supervision, the Sector worked together with asset management companies and association representatives to address a series of questions regarding the interpretation of the Supervisory Requirements for IT in Asset Management Companies (*Kapitalverwaltungsaufsichtlichen Anforderungen an die IT – KAIT*). In addition, it discussed administrative practice, and the expectations associated with KAIT audits and reporting, with the *Institut der Wirtschaftsprüfer* in 2020.

As part of the "improving data quality" supervisory priority, BaFin's Securities Supervision Sector substantially streamlined monitoring of compliance with the reporting requirements under Article 26 of the Markets in Financial Instruments Regulation (MiFIR) and Article 9 of the European Market

Infrastructure Regulation (EMIR) in 2020. This was done by automating the preliminary assessment of incoming notifications.

Since 2020, Securities Supervision has also had a new, (partially) automated data analysis tool for market abuse monitoring. This permits irregular trades to be identified much faster than before.

Particularly at the start of 2020, the Sector addressed in detail the federal government's plans to transfer responsibility for supervising financial investment intermediaries to BaFin, as part of a corresponding supervisory priority. The legislative process has become bogged down since then, and preparations have been on hold since mid-2020.

### Consumer protection

In the area of consumer protection<sup>33</sup>, BaFin focused among other things on ensuring that online brokerages comply with the investor protection requirements set out in the German Securities Trading Act (*Wertpapierhandelsgesetz*). One question was whether trading apps improve the quality of offerings so much that this justifies investment firms' acceptance of inducements from third parties. In addition, systems failures such as those seen in the first quarter of 2020 led BaFin to prioritise the existence of robust IT infrastructures at individual credit institutions.

BaFin also progressed with its collective consumer protection activities, and took specific measures to educate consumers, in 2020. Among other things, it launched large-scale consumer surveys of the unregulated capital market and precious metals, so as to be able to provide specific information to the public.

### Resolution

One of the key focuses of BaFin's Resolution Sector<sup>34</sup> in 2020 was on crypto-assets, which formed part of the "integrity of the financial system and the fight against financial crime" supervisory priority. The trading and dissemination of these assets are continuing to increase in both Germany and Europe. BaFin therefore analysed the crypto market, focusing in particular on the inherent money laundering

<sup>32</sup> See chapter III.3.

<sup>33</sup> See chapter III.4 for information on BaFin's overall consumer protection activities.

<sup>34</sup> See chapter III.5, chapter III.6 and chapter IV.

risks. The Sector combated this risk by analysing the markets more closely and carrying out in-depth inspections at companies. These activities covered both crypto custodians, which have been included in supervision since 1 January 2020, and established financial institutions and credit institutions that can serve as cryptocurrency exchange services and trading exchanges, among other things.

In addition, Resolution systematically enforced the authorisation requirement in digital environments in 2020 and continued to step up its investigation of unauthorised business activities.<sup>35</sup>

The development of the Anti Financial Crime Alliance (AFCA) is remarkable. This project was only launched in September 2019 as a public-private partnership.

Nevertheless, it has grown into a cornerstone of efforts to combat money laundering and terrorist financing within an extremely short space of time.<sup>36</sup>

The Sector evaluated and enhanced its processes and methodology in order to improve its resolution planning and crisis preparedness, and to increase institutions' resolvability. It also issued a large number of notices against money transfer companies acting for fraudulent trading platforms. The objective was to stop these transactions, break up networks of intermediaries in Germany and, if possible, return money to investors<sup>37</sup>. The Sector took formal action against the operators of unauthorised business activities 176 times in 2020 – more often than ever before.

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<sup>35</sup> See chapter III.6.

<sup>36</sup> See chapter III.5 for details of the AFCA.

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<sup>37</sup> See chapter III.6.



# II

## BaFin's international role







# 1 Germany's EU Council Presidency

Germany assumed the Presidency of the Council of the European Union (EU) for the 13th time in the second half of 2020<sup>1</sup>. One of the key tasks in this six-month period was to advance Council discussions about EU legislative acts.

BaFin assisted the Federal Ministry of Finance (*Bundesministerium der Finanzen*) by providing technical expertise<sup>2</sup> during the Council negotiations. This applied in particular to the legislative proposals published by the European Commission on 24 September 2020 as part of its Digital Finance Package<sup>3</sup> on crypto-assets (Proposal for a Regulation on Markets in Crypto-Assets – MiCA) and on digital operational resilience (Proposal for a Regulation on Digital Operational Resilience for the Financial Sector – DORA).<sup>4</sup>

## 1.1 MiCA – Markets in Crypto-Assets

The MiCA Regulation is intended by the European Commission to close the current regulatory gap in Europe regarding crypto-assets, which are not regulated either as financial instruments under the Markets in Financial Instruments Directive II (MiFID II) or as e-money under the Electronic Money Directive II (EMD II).

The European Commission defines crypto-assets in the draft MiCA Regulation as digital representations of values or rights which may be transferred and stored electronically using distributed ledger technology or similar technology. Under the MiCA Regulation, issuers of crypto-assets must submit and publish a crypto-assets white paper. The aim is for issuers to inform potential customers of the features, functions and risks associated with the crypto-assets before such customers make a purchase. The European Commission is planning new authorisation requirements for providers of services referencing crypto-assets, such as consultants, operators of trading platforms or custodians.

The Commission's objective is to introduce authorisation requirements for the two types of "stablecoins" defined in the draft: in future, only undertakings that have been officially authorised to do so should be permitted to issue asset-referenced tokens and e-money tokens. Asset-referenced tokens are crypto-assets that, for example, reference several fiat currencies or commodities.

Under the draft regulation, the European Banking Authority (EBA) in cooperation with the competent national supervisors will be responsible for overseeing issuers of asset-referenced tokens and e-money tokens that are particularly large or that are used throughout Europe.

<sup>1</sup> Information on Germany's presidency of the Council of the European Union can be found at <https://www.eu2020.de/eu2020-en>.

<sup>2</sup> See BaFinJournal October 2020, page 9 ff. (only available in German).

<sup>3</sup> European Commission, Digital Finance Package, [https://ec.europa.eu/info/publications/200924-digital-finance-proposals\\_en](https://ec.europa.eu/info/publications/200924-digital-finance-proposals_en).

<sup>4</sup> See also chapter III.6.

## 1.2 DORA – Digital operational resilience for the financial sector

To help achieve its goal of enhancing digital operational resilience<sup>5</sup> in the area of information and communications technology (ICT), the European Commission has introduced the Digital Operational Resilience Act (DORA) – a common framework for managing ICT risks and ICT third-party risks for all enterprises in the European financial sector. DORA also includes a reporting obligation for ICT incidents and a new approach to overseeing critical ICT third-party service providers such as cloud service providers.

The proposed framework harmonises and supplements the requirements relating to ICT risk management and ICT third-party risk management that were previously largely set out in sector-specific guidelines.<sup>6</sup> At the same time, DORA introduces mandatory threat-led penetration tests (TLPTs) for significant financial sector firms.<sup>7</sup> These are controlled attempts to more comprehensively assess and improve a firm's resilience on the basis of its reaction to a simulated hack attack.

In addition, the European Commission aims to use DORA to introduce a European supervisory regime for critical ICT third-party service providers. The aim is to build on the existing financial supervisory structures in the European Union.

Above and beyond this, the draft DORA establishes a comprehensive obligation to report serious ICT incidents to the supervisory authorities, such as BaFin. This reporting obligation will apply to all enterprises in the financial sector. As a result, the framework closes the current gap in the case of insurance undertakings and investment firms. At the same time, the European Commission intends to use DORA to simplify the existing obligations.

## 1.3 European Capital Markets Union

Another focus of Germany's Council presidency was deepening the European Capital Markets Union. In September 2020, the European Commission submitted an action plan<sup>8</sup> for this, with which it aims to drive forward the work on the Capital Markets Union that began 2015, introduce new highlights and deepen the union.

The action plan sets out three key objectives:

- to support a green, digital, inclusive and resilient economic recovery in the EU by making financing more accessible to European companies, and especially SMEs;
- to develop an EU financial marketplace in which individuals can save and invest for long-term even more safely; and
- to integrate national capital markets into a genuine single market.

The Commission aims to achieve these goals using a series of measures; these will be split up into a number of different supervisory and company law areas and will largely be decided in 2021 and 2022. Among other things, a single access point for company information is planned. In addition, initiatives will be launched to strengthen shareholders' rights and improve consumers' financial education.

The Council conclusions published in December<sup>9</sup> at the end of Germany's Council presidency make reference to the European Commission's action plan. In this document, the Council highlights the fact that the COVID-19 pandemic has made the need for deeper and more uniform capital markets even more urgent. Providing companies, and especially SMEs, with easier access to these markets could help to better mitigate the economic consequences of the pandemic in Europe.

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5 Digital operational resilience is a firm's ability to be robust and resilient enough to maintain the integrity of its digital (operational) processes even during and after disruptions.

6 See BaFin Perspectives issue 1/2020, page 23 ff., [www.bafin.de/dok/14279540](http://www.bafin.de/dok/14279540).

7 See loc. cit., page 47 ff.

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8 European Commission, A Capital Markets Union for people and businesses – new action plan, <https://eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0590&from=EN>.

9 Council of the European Union, Council Conclusions on the Commission's CMU Action Plan, <https://data.consilium.europa.eu/doc/document/ST-12898-2020-REV-1/en/pdf>.

## 2 Bilateral and multilateral cooperation

BaFin works closely together with supervisory authorities in other countries. It is also represented in numerous European and international organisations and working groups concerned with issues relating to supervision, resolution and regulation.

### Memoranda of understanding

Financial sector enterprises are becoming more and more international in scope. As a result, memoranda of understanding (MoUs) are playing an increasingly important role. They allow BaFin to share information with partner institutions in other countries on cross-border credit institutions, investment services institutions and insurance undertakings. A distinction must be made here between institution-specific and general MoUs, with the latter being the normal case. In turn, these can be either sector-specific or cross-sector. In 2020, BaFin negotiated with a number of other supervisory authorities on entering into general MoUs.

For example, in December 2020 it agreed such an MoU with the Security and Futures Commission of Hong Kong (SFC). This MoU formalises cooperation and information sharing on the activities of central counterparties (CCPs). BaFin and the SFC had already signed a more general supervisory agreement back in 2004, and the new MoU now supplies more specific rules.

Also in December 2020, BaFin signed an MoU with the United States Securities and Exchange Commission (SEC). This MoU recognises the German supervisory regime for US derivatives transactions as the equivalent of the national regime. BaFin had applied to the SEC for substituted compliance for the supervisory standards. The SEC approved this in December 2020. As a result of this decision, institutions supervised by BaFin that engage in derivatives transactions in the USA can be exempted from the requirement to comply with the SEC's supervisory requirements. In return, BaFin undertakes to provide the SEC with relevant information that it might need to supervise the derivatives transactions in the USA. Should the SEC give notice to terminate this special status, the German institutions will be granted a transitional period of ten months.

BaFin also signed a multilateral MoU. This was entered into by the European supervisory authorities on the one hand and the Prudential Regulatory Authority (PRA) as part of the Bank of England on the other; the lead negotiator was the European Securities and Markets Authority (ESMA).<sup>10</sup> This cooperative agreement covers the supervision of central counterparties and central securities depositories (CSDs). It was required because of Brexit/the end of the agreed transitional period.

### Technical cooperation

Technical cooperation in 2020 was impacted by the COVID-19 pandemic. As a result, specialist information had to be exchanged, and issues discussed, with supervisory authorities and central banks abroad primarily in videoconferences and by post or e-mail. One example here is our extensive cooperation with the National Bank of Georgia, which focused on fintechs and cryptocurrencies.

BaFin is a member of the European Supervisor Education Initiative (ESE). The specialist seminars that it and others regularly host also could not take place in 2020 because of the pandemic. The initiative is working towards being able to offer digital events in the future.

July 2020 saw the successful conclusion of the European Union's twinning project with partner country Montenegro. The project was originally scheduled to take two years, but was prolonged for three months due to the restrictions on social contact caused by the COVID-19 pandemic. The focus was on topics from the areas of banking, insurance, securities supervision and the prevention of money laundering. Germany's representatives were BaFin, as the project manager, and the Deutsche Bundesbank; the other participants were Croatia and the Netherlands. Montenegro will now align its supervisory system to comply with EU requirements.

### Multilateral cooperation

A large number of financial sector enterprises today operate on a global level. As a result, multilateral cooperation by supervisory authorities is becoming more and more important. In line with this, BaFin works closely together with supervisory authorities in other countries. Within the European Union, this cooperation largely takes place under the umbrella of the European supervisory organisations. However, BaFin is also a member of the global standard-setting bodies (see info box on page 44). In 2019, BaFin belonged to roughly

<sup>10</sup> See also chapter I.3.

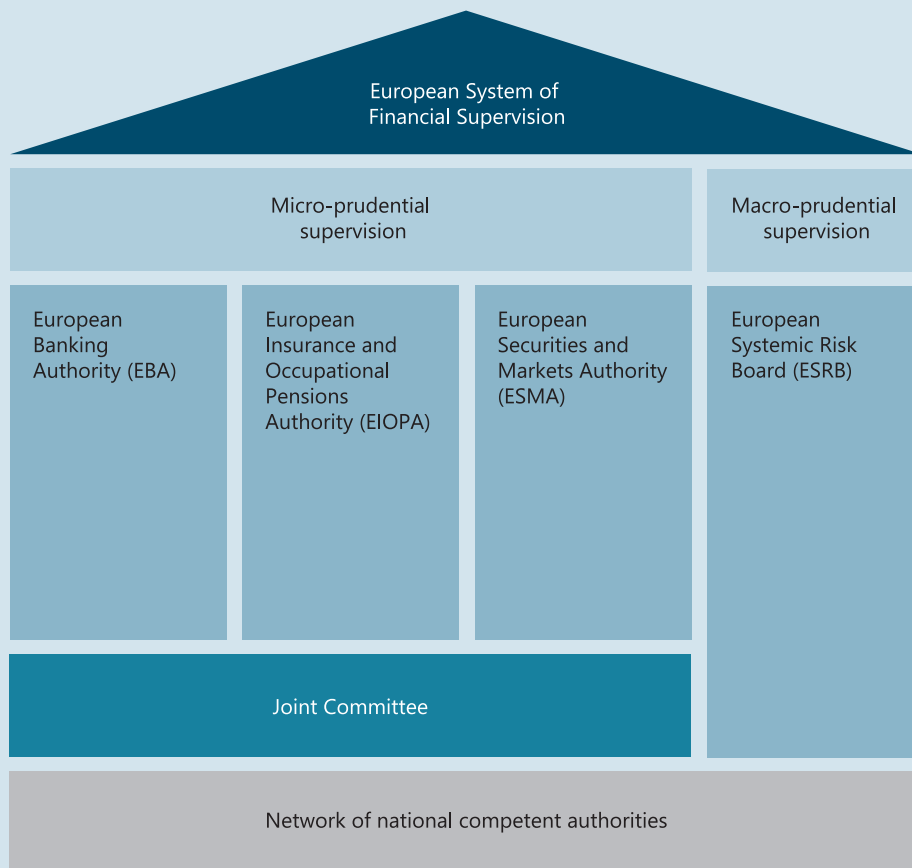
600 groups of this type, some of which are or were of a temporary nature.

Work by these institutions and groups in 2020 was dominated by the impact of the COVID-19 pandemic and by preparations for Brexit. Other key topics were sustainable finance and improving supervisory convergence.

## BaFin in the European System of Financial Supervision

BaFin is an active participant in the European System of Financial Supervision (ESFS) established at the start of 2011 (see Figure 1).

**Figure 1: European System of Financial Supervision**



The three European Supervisory Authorities (ESAs) are responsible for preparing technical standards for the European Commission on the basis of EU regulations and directives (Level 2 of the European legislative process, see Figure 2). The ESAs also publish their own guidelines and recommendations (Level 3).

**Figure 2: The levels in the EU's legislative process and the role of the ESAs**



Another core task performed by the ESAs is ensuring that the national competent authorities apply these provisions on a convergent basis. Despite their name, however, the ESAs – apart from a few closely defined exceptions – are not supervisory authorities. The Joint Committee works on topics which are significant across all sectors. The ESAs and the Joint Committee operate at a micro-prudential level, i.e. their primary function is to monitor whether individual undertakings are complying with quantitative and qualitative requirements.

The European Systemic Risk Board (ESRB) within the European Central Bank (ECB) is responsible for macro-prudential matters. It is tasked with identifying systemic risks for the European financial system and issuing warnings at an early stage. The micro- and macro-prudential levels are closely interlinked to ensure that information flows between them in both directions.

## BaFin in the banking union

Within the framework of the European banking union, BaFin forms part of the Single Supervisory Mechanism (SSM) and the Single Resolution Mechanism (SRM). Information on these can be found starting on page 56 (SSM) and page 131 (SRM).

## BaFin in global organisations

BaFin is also a member of a number of global bodies, such as

- the International Organization of Securities Commissions (IOSCO),
- the International Association of Insurance Supervisors (IAIS)
- and the Basel Committee on Banking Supervision (BCBS). BaFin is also represented on this organisation's supervisory body, the Group of Governors and Heads of Supervision (GHOS).

BaFin collaborates in these international associations on the development of global regulatory standards. In addition, it is involved, for example, in the Financial Action Task Force (FATF) and the Islamic Financial Services Board (IFSB). BaFin is also represented on the Financial Stability Board (FSB). The G20 Heads of State and Government gave the FSB a wide-ranging mandate as part of the regulatory reforms introduced after the outbreak of the global financial crisis: among other things, it was entrusted with overseeing the international financial system. If it discovers weak points in the course of its work, it is expected to develop proposals on how they should be eliminated. The FSB is also responsible for coordinating and promoting cooperation and the exchange of information between its members.

## 3 Work of the three ESAs

The three European supervisory authorities' work programmes in 2020 were largely dominated by the COVID-19 pandemic. The ESAs devoted most of their work to containing the pandemic's consequences for the financial markets.

### 3.1 EBA

For example, starting in March the European Banking Authority (EBA) worked to provide relief for credit institutions during the pandemic.<sup>11</sup> It published initial guidelines on this on 2 April 2020: these set out the preconditions for granting payment relief under government or private moratoria on loan repayments in order to avoid the exposures concerned being classified as forborne or defaulted. However, the EBA's annual programme also included the following tasks, among others:

- implementation of its mandates under the Risk Reduction Measures package<sup>12</sup>,
- review of the Basel Framework's Pillar 2<sup>13</sup>, especially with respect to the use of consistent approaches in the Supervisory Review and Evaluation Process (SREP<sup>14</sup>),
- finalisation of the project for a European Centralised Infrastructure of Data (EUCLID),
- strengthening of the role of the EBA in the fight against money laundering and terrorist financing,
- inclusion of sustainability risks in banking regulation, and
- the EBA's FinTech Roadmap.

### 3.2 EIOPA

The European Insurance and Occupational Pensions Authority (EIOPA) worked with national supervisors and the European Commission in 2020 to ensure financial stability, market integrity and consumer protection during the COVID-19 pandemic. EIOPA conducted a large number of virtual investigations on topics such as market, credit, return and solvency risks. Key interest rate information was published on a weekly basis at times. In addition, EIOPA published a position paper on

the options for insuring future pandemics. It also called on undertakings to explain the impact of the coronavirus crisis in their Solvency and Financial Condition Reports (SFCRs).

Above and beyond this, EIOPA published a large number of comments on acting in a consumer-friendly manner and issued recommendations on dividends, among other things. Insurers must consider these carefully and must document their risk-bearing capacity.

EIOPA granted undertakings temporary relief with respect to submission deadlines, and also extended consultation deadlines.

#### **Pan-European personal pension product**

EIOPA's work also focused on the pan-European personal pension product (PEPP). In 2020, the European Commission completed its Level 2 work on this subject (see Figure 2 on page 45). Among other things, the Commission issued regulatory technical standards (RTSs) providing concrete details on the following:

- the PEPP key information document (KID)
- PEPP Benefit Statement
- additional information for supervisory reporting
- the criteria governing EIOPA's product intervention powers
- costs and fees for the basic PEPP
- risk mitigation techniques

EIOPA had produced the draft RTSs, with BaFin staff contributing to them.

In addition, the Commission provided concrete descriptions of the format for supervisory PEPP reporting in implementing technical standards (ITSs). It also specified in detail the way in which EIOPA and the national competent authorities should communicate and exchange information with each other. In this case, too, EIOPA had drafted the ITSs and BaFin contributed to them.

Article 5 (1) of the PEPP Regulation sets out that the distribution of PEPPs is dependent on their having been entered in a central public register kept by EIOPA. However, the national competent authorities – in Germany BaFin and, in relation to intermediaries, the authorities responsible for their supervision – remain primarily responsible for registration, ongoing supervision, complaints, publications, product interventions and sanctions.

<sup>11</sup> See chapter I.1 for information on the measures taken by BaFin on the course of the coronavirus pandemic.

<sup>12</sup> The Risk Reduction Measures package revised the European Capital Requirements Regulation (CRR), the Single Resolution Mechanism Regulation (SRMR), the European Capital Requirements Directive (CRD) and the Bank Recovery and Resolution Directive (BRRD).

<sup>13</sup> See also the 2016 Annual Report, page 94 ff.

<sup>14</sup> See chapter III.1.3.1.

Other key items in EIOPA's annual programme were:

- An opinion on the Solvency II Review, submitted to the European Commission<sup>15</sup>
- an opinion on the supervision of remuneration principles, submitted to the European Commission
- guidelines on information and communication technology security and governance
- guidelines on outsourcing to cloud service providers
- a continuing commitment to sustainability and preventing climate change
- discussion papers on value chains/insurtech and stress test methodology
- assistance with the international Insurance Capital Standard being developed by the International Association of Insurance Supervisors (IAIS)

#### Change at the top of EIOPA

The ten-year term of office of EIOPA Chairman Gabriel Bernardino expired at the end of February 2021. Until his successor is appointed, the authority is being temporarily led by the Deputy Chairman, Dr Peter Braumüller.

### 3.3 ESMA

Work by the European Securities and Markets Authority (ESMA) in 2020 was also strongly impacted by the COVID-19 pandemic. From the very start, ESMA observed and analysed the effect of the pandemic on the European financial markets. ESMA provided market participants with specific supervisory relief and clarified the expectations of the supervisory authorities, to the extent possible within the legal framework and with a view to consumer protection, market stability and market integrity. In addition, it addressed the introduction in a number of member states of measures relating to short selling.

#### Changes at the top of ESMA

On 12 October 2020, Steven Maijoor took part in his last annual meeting of the European Parliament's Committee on Economic and Monetary Affairs (ECON) as Chairman of ESMA. He will be leaving the authority at the end of March 2021 after ten years as its head. A new Executive Director will also be appointed in 2021. Verena Ross will be leaving the authority at the end of May 2021. The search for a successor for both positions has already begun.

### 3.4 Sustainability-related disclosures

ESMA, EIOPA and the EBA are working together with the national competent authorities to finalise the regulatory technical standards (RTSs) designed to flesh out the details of the Sustainable Finance Disclosure Regulation (SFDR)<sup>16</sup>. This requires certain financial undertakings to disclose how sustainable their products are. The regulation is to be applied as from 10 March 2021. However, work on the RTSs was delayed as a result of the coronavirus and was only submitted to the European Commission on 3 February 2021. A public consultation on the draft RTSs was held from April to August 2020<sup>17</sup>. In parallel, the ESAs worked to create binding templates for precontractual and periodic disclosure and reporting obligations on sustainability risks. These will be included in the annex to the RTSs. The plan is to combine the RTSs under the SFDR with the disclosure obligations under the Taxonomy Regulation<sup>18</sup>. This should produce a single rulebook for sustainability-related disclosure requirements.

Since the European supervisory authorities wanted to provide undertakings with clarity for the transitional period from 10 March 2021 until the (delayed) approval of the RTSs by the Commission, they developed a joint Supervisory Statement. However, this had not been finalised at the end of 2020. It is intended to make clear to undertakings what the supervisory expectations are during this interim period.

<sup>15</sup> See chapter I.8 for the proposals on the Solvency II Review.

<sup>16</sup> Regulation (EU) 2019/2088.

<sup>17</sup> ESMA, Joint ESA consultation on ESG disclosures, <https://www.esma.europa.eu/press-news/consultations/joint-esa-consultation-esg-disclosures>.

<sup>18</sup> Regulation (EU) 2020/852.

## 4 Work of the global standard setters

### 4.1 Basel Committee draws a line under post-GFC agenda

Work by the Basel Committee on Banking Supervision (BCBS) in 2020 concentrated on mastering the coronavirus pandemic. The main challenge here was to develop and implement appropriate short-term emergency regulatory measures and to monitor the consequences of the pandemic and the impact of the emergency measures.

In addition, the BCBS drew a line under the post-GFC agenda<sup>19</sup>, i.e. the period since the global financial crisis in 2007/2008, which saw extensive regulatory and supervisory reforms. The BCBS has also adopted a new strategic perspective for the future: it will be focusing on monitoring the implementation of, and evaluating, the Basel III reforms that have been resolved.

BaFin employees are active in a number of Basel Committee working groups.

### 4.2 IAIS implements new frameworks

The International Association of Insurance Supervisors (IAIS) resolved a large number of major projects in November 2019.<sup>20</sup> This marked the start of the phase in which the various frameworks are to be introduced and applied in practice.

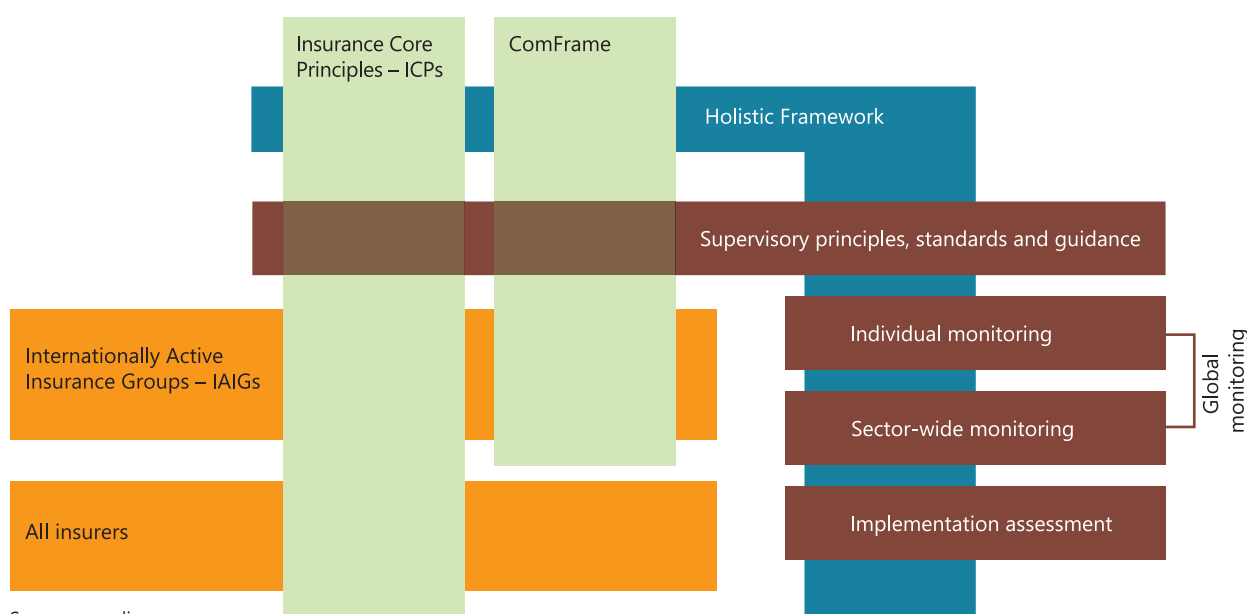
In parallel to the monitoring period for the global Insurance Capital Standard (ICS), the standard-setter for the insurance sector began putting the individual building blocks in the Holistic Framework for Systemic Risk – i.e. implementation assessment and monitoring – in place.

At the same time, the IAIS continued its work on a number of different application papers. These provide the supervisory authorities with examples of how the standards in the Insurance Core Principles (ICPs) and the Common Framework (ComFrame) for the supervision of large internationally active insurance groups (IAIGs) are to be applied. Figure 3 provides an overview of the IAIS's global regulatory frameworks.

19 The abbreviation "GFC" stands for "global financial crisis".

20 See the 2019 Annual Report, page 52 ff.

**Figure 3: The IAIS's global regulatory frameworks**



Source: own diagram.



Work was started as planned and continued largely regardless of the coronavirus pandemic. However, the IAIS did have to adapt its timelines in several cases of places. BaFin is a member of a large number of IAIS working groups.

### 4.3 IOSCO in the pandemic period

The International Organization of Securities Commissions (IOSCO) also concentrated on the COVID-19 pandemic in 2020, and on its impacts on the markets and financial stability.

In this context, IOSCO published two reports on money market funds in November 2020. These show how the COVID-19 pandemic and the market volatility that was partially caused by this impacted money market funds. In addition, they evaluated how different money market funds performed in key markets.

Apart from the consequences of the pandemic, IOSCO worked on a number of projects on topics such as crypto-assets, sustainable finance and artificial intelligence that it had launched in the previous year.

IOSCO published a large number of other reports in 2020. Examples include the following:

- a report on the regulatory impact of global stablecoin initiatives,
- a two-tier procedure for consistently measuring investment fund leverage,
- guidance for supervisory authorities in dealing with conflicts of interest and conduct-related risks among market intermediaries during the capital raising process, and
- a report detailing good practice for decisions on equivalence.

IOSCO's work also influenced the law and market structures in the European Union and its Member States. BaFin is active in a large number of IOSCO working groups.

### 4.4 FSB investigated the consequences of the coronavirus pandemic

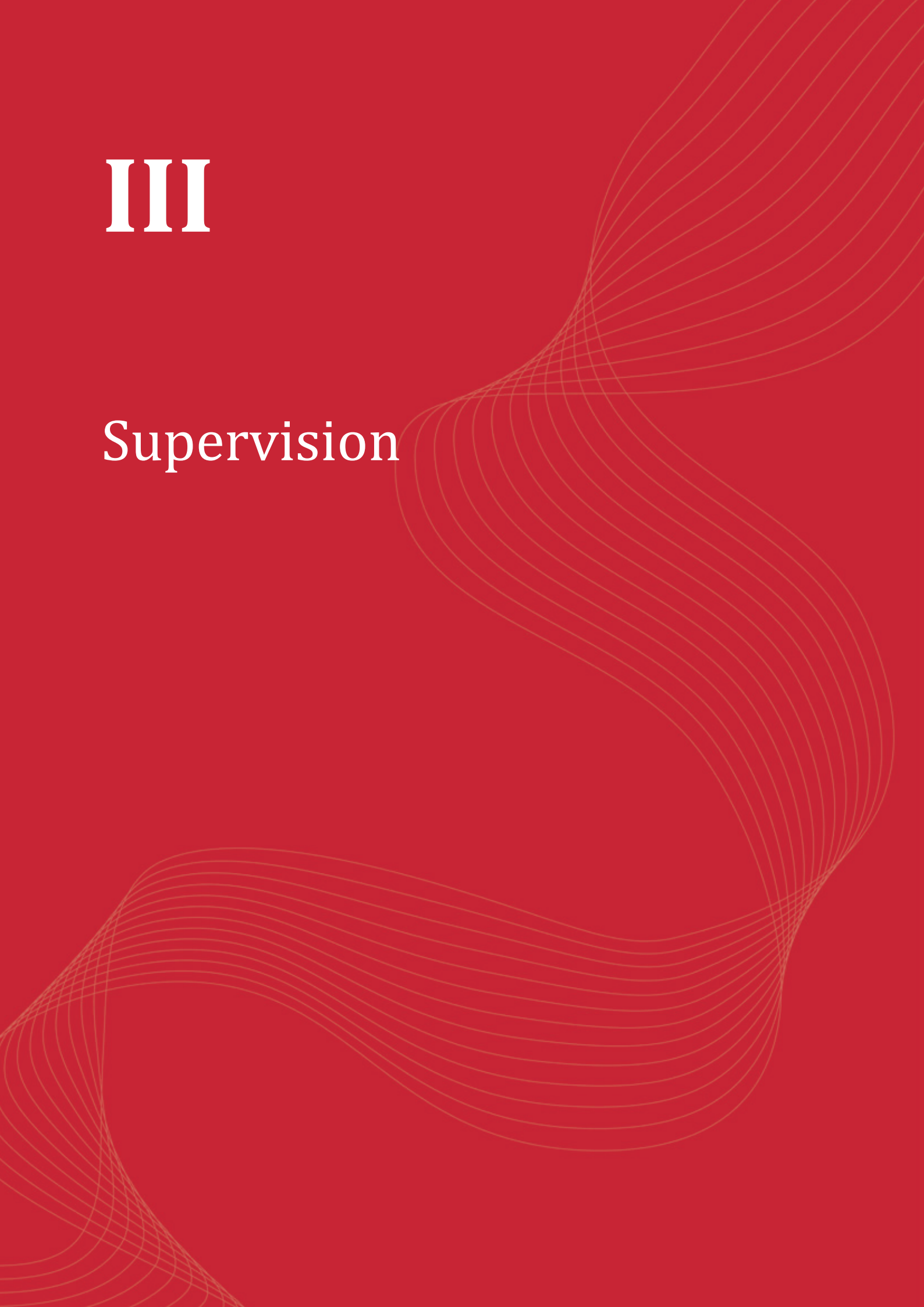
The Financial Stability Board (FSB) examined the impacts of the COVID-19 pandemic on global financial stability in depth. Among other things, it continuously oversaw and assessed vulnerabilities in the financial system and coordinated the collection and analysis of information relating to the crisis. In addition, the FSB expressed an opinion in a report on the extent to which the supervisory measures taken in the course of the coronavirus crisis are compatible with existing international financial standards. Put briefly, it found that a large majority of the COVID-19 measures taken were within the scope of the applicable standards. Measures going beyond them were strictly limited in time and represented an appropriate reaction to the exceptional economic situation.

BaFin is a member of the FSB and contributed the German supervisors' perspective. Among other things, it kept the FSB informed on a regular basis of current national regulatory and supervisory COVID-19 measures.

The FSB made significant progress in 2020, with assistance from BaFin, on a number of reform projects dating back to the global financial crisis in 2007/2008. These include developments in cross-border payments and the replacement of the LIBOR reference rate, plus recommendations on the regulation and oversight of asset-referenced tokens and on dealing with cyber risks.

# III

## Supervision





# 1 Banks, financial services providers and payment institutions

## 1.1 Fundamental aspects of supervisory practice

### 1.1.1 New IRBA requirements

#### 1.1.1.1 Implementation of the requirements

Changes to the requirements for the definition of default contained in Article 178 of the Capital Requirements Regulation (CRR) came into force at the end of 2020/beginning of 2021. Since then, institutions that have been approved to use the Internal Ratings-Based Approach (IRBA) to calculate credit risk have had to comply among other things with new rules on how to estimate the probability of default.

IRBA institutions that had not received approval in 2019 to make the necessary changes to their models had to assess for themselves the extent to which they meet the various new requirements as the basis for their suitability assessments. BaFin issued its approval notices on schedule as at the end of the year. As agreed with the European Banking Authority (EBA), BaFin mainly focused on ensuring that the institutions used the amended rules to determine defaults.

#### 1.1.1.2 New EU rules from the IRB repair programme

Internal models came in for criticism after the outbreak of the financial crisis in 2007/2008. The EBA has harmonised the requirements for using the IRBA procedures. It had already formulated a number of requirements in 2019 as part of the IRB repair programme.<sup>1</sup> Then, in May 2020, it published its last component: Guidelines on Credit Risk Mitigation for institutions applying the IRB approach with own estimates of LGDs.<sup>2</sup> These guidelines set out in greater

<sup>1</sup> See the 2019 Annual Report, page 61.

<sup>2</sup> EBA/GL/2020/05.

detail the requirements<sup>3</sup> relating to the eligibility of funded and unfunded protection and the impact of the credit risk mitigation. BaFin plans to implement the guidelines in full as from the start of their application in January 2022.

### Regulatory technical standards

The Commission sent the EBA proposed amendments to the final drafts of three regulatory technical standards (RTSs) for the IRB repair programme that form the basis for future Commission Delegated Regulations. In April 2020, the EBA agreed to the proposed amendment to the RTS on assigning risk weights to specialised lending exposures.<sup>4</sup> The EBA issued an opinion in August on the proposed amendments to the RTS on the specification of the nature, severity and duration of an economic downturn.<sup>5</sup> At the end of the year, it again commented on the European Commission's proposal on the specification of the assessment methodology for competent authorities regarding compliance of an institution with the requirements to use the IRB Approach.<sup>6</sup>

#### 1.1.2 Countercyclical capital buffer reduced to zero

Developments following the outbreak of the COVID-19 pandemic led BaFin to cut the countercyclical capital buffer (CCyB) for all credit and financial services institutions<sup>7</sup> to 0% as at the second quarter of 2020.<sup>8</sup> BaFin believes that the CCyB will not be increased before the end of 2021. The background to this is need for credit in the real economy and potential loan defaults in the further course of the COVID-19 pandemic. The decision is intended to give the German banking sector planning certainty and make it easier for institutions to absorb losses from credit defaults while continuing to make appropriate levels of loans available to companies and private households.<sup>9</sup>

In 2019, BaFin had increased the CCyB to 0.25% for the first time; before that it had been 0% ever since its introduction in 2015. The 2019 increase was based

on a recommendation by the German Financial Stability Committee (FSC), whose members include representatives from BaFin. The FSC identified an increase in cyclical systemic risks in three risk areas:

1. Risks relating to economic trends that are not comprehensively captured by micro-prudential credit risk measurement ("economic risk" from underestimated credit risks)
2. Real estate finance risk ("real estate risks" from increases in real estate prices over many years)
3. Interest rate risk if interest rates continue to remain at the zero lower bound for some time ("low interest rate environment") or rise sharply ("interest rate risk").

The institutions would have had to make the buffer available as of 1 July 2020.

However, the outbreak of the COVID-19 pandemic at the start of 2020 triggered substantial uncertainty on the financial markets and it was not clear how the real economy would perform going forward. The size of any potential losses and the duration of the global crisis were completely unknown. BaFin therefore decided to reduce the CCyB to 0% again. This is what is supposed to happen: the preventive measure enhances the German banking sector's ability to extend loans and absorb losses. The FSC<sup>10</sup> welcomed BaFin's move.

#### 1.1.3 General administrative act on credit cooperatives' share capital

On 1 January 2020, BaFin published its revised general administrative act on the share capital of cooperatives. This implements the provisions of the European Capital Requirements Regulation (CRR II) relating to own funds requirements and the provisions of the supplementary Delegated Regulation (EU) No 241/2014, known for short as the Own Funds RTS. Under these regulations, institutions must obtain permission from the supervisors before they redeem Common Equity Tier 1 instruments. This regulatory procedure is not feasible in practice in the case of credit cooperatives due to their large

3 Set out in Article 181 (1) f and Article 183 1 c of the CRR.

4 EBA/Op/2020/06.

5 EBA/Op/2020/12.

6 EBA/Op/2020/20.

7 Significant institutions (SIs) and less significant institutions (LSIs).

8 [www.bafin.de/dok/13991372](http://www.bafin.de/dok/13991372).

9 [www.bafin.de/dok/15790052](http://www.bafin.de/dok/15790052).

10 Deutsche Bundesbank, FSC statement on the countercyclical capital buffer, <https://www.bundesbank.de/en/tasks/topics/statement-on-the-countercyclical-capital-buffer-by-the-german-financial-stability-committee-828822>.

number – 841 institutions in 2020 – and the customary fluctuation in their members.

However, a simplifying regulation exists: Article 32 (2) of the Own Funds RTS permits BaFin to authorise a defined repayment amount for shares, net of the amount subscribed for new Common Equity Tier 1 instruments, in advance for a period of up to one year.

#### **A general administrative act for each year**

BaFin has made use of this opportunity each year since 2015 by issuing a general administrative act. Each such administrative act is valid for one year and only less significant institutions (LSIs) with the legal form of a registered cooperative society are entitled to apply them. BaFin coordinates its approach with the *Deutsche Bundesbank* in each case.

The various general administrative acts state that approval for the repayment of share capital is deemed to have been granted where such capital does not exceed 0.5% of Common Equity Tier 1 capital and the other conditions in the general administrative act relating to the level of own funds have also been met. The institutions must also continue to comply with the own funds requirements, including existing capital additions, own funds target ratios and a safety buffer, after making the repayment.

BaFin set the safety buffer at 0.75% in the general administrative act for 2020 and reviews it annually. Institutions that do not meet the requirements of the general administrative act must obtain BaFin's approval for repayments.

#### **1.1.4 Other systemically important institutions**

BaFin defines the institutions domiciled in Germany that must be classified as "other systemically important institutions" (O-SIIs) at least once a year in consultation with the Deutsche Bundesbank. It requires these O-SIIs to hold an additional capital buffer in the form of Common Equity Tier 1 capital. In the reporting period, it classified 13 institutions as O-SIIs and ordered each of them to hold an individually calculated capital buffer.

#### **BaFin and the Bundesbank adapt joint methodology**

In 2020, BaFin and the Deutsche Bundesbank adapted the methodology that they jointly developed for classifying institutions as O-SIIs<sup>11</sup>: the modifications

related firstly to the data pool and framework for the indicators and secondly to the design and calibration of the capital buffer. The data pool for the indicators was modified so as to better accommodate the requirements of the EBA Guidelines on the criteria for the assessment of O-SIIs<sup>12</sup>. BaFin and the Bundesbank reviewed the framework for the indicators used in order to ensure their suitability for identifying O-SIIs and, if necessary, to amend them.

#### **New approach: equal expected impact approach**

The cluster analysis in the capital buffer category approach previously used to design and calibrate the O-SII capital buffer was replaced by the equal expected impact approach. This approach reduces the expected systemic loss that the default of an O-SII can potentially have on the entire banking system to the level of the expected systemic loss caused by the default of an institution that is no longer currently classified as an O-SII. The capital buffer is now assigned on the basis of an economic model. In addition, the way in which capital buffer categories are formed was revised. In future, there will be 12 capital buffer categories. The capital buffer for the lowest category is 0.25 percentage points. The buffers increase by 0.25 percentage points per category; in other words, the capital buffer for the highest category is 3 percentage points. As in the past, the O-SIIs are assigned to a capital buffer category on the basis of their relevance to the system, as measured by their total number of points. However, the increased granularity of the capital buffer categories allows a more differentiated allocation of the capital buffers to be made in relation to the overall scores.

#### **1.1.5 Financial and Internal Capital Adequacy Information Regulation**

The Third Regulation amending the Financial and Internal Capital Adequacy Information Regulation (*Dritte Verordnung zur Änderung der Finanz- und Risikotragfähigkeitsinformationenverordnung*) entered into force as at 19 August 2020.<sup>13</sup> One of the reasons for this revision was the implementation of two EBA guidelines, which BaFin applies in accordance with section 7b (1) sentence 4 of the German Banking Act (*Kreditwesengesetz*). The amending regulation now also sets out how the material information on multiyear capital planning and internal liquidity management (internal liquidity adequacy assessment process – ILAAP) must be documented in supervisory reporting. The

11 [www.bafin.de/dok/8622724](http://www.bafin.de/dok/8622724).

12 EBA/GL/2014/10.

13 Federal Law Gazette I 2020, page 1890.

regulation follows the EBA's "Guidelines on ICAAP<sup>14</sup> and ILAAP information collected for SREP<sup>15</sup> purposes"<sup>16</sup>.

The regulation is designed in particular to set out the reporting requirements needed to permit the supervisors to gain an insight into trends in institutions' net assets and results of operations. In addition, it aims to ensure clarity on changes in credit institutions' risk positions and risk management procedures, including liquidity management and plans for refinancing. The reports are submitted every quarter.

### **BaFin redesigns reporting forms**

BaFin has revised the existing reporting forms to meet the requirements of the amending regulation. The new forms now capture data on liquidity management and the capital planning process for the first time, which are evaluated in the context of internal capital adequacy. This helps further harmonise the administrative practices adopted by supervisory authorities within the European Union (EU) when implementing the SREP.

The EBA guidelines on the management of interest rate risk arising from non-trading book activities<sup>17</sup> that were implemented in the amending regulation are designed to ensure that the national competent authorities within the EU handle interest rate risk in the non-trading book in a uniform manner. The modification of the existing reporting forms on interest rate shock scenarios at solo and group level now captures information on the eight scenarios set out in the EBA guidelines. Previously, information was only requested on two scenarios. Details of these interest rate shock scenarios were previously regulated by BaFin Circular 06/2019<sup>18</sup>.

In addition, the amending regulation provides for a uniform reporting cycle, with all institutions only having to submit information on their internal capital adequacy and liquidity annually in future. Overall, the modifications are designed to simplify the previous reporting process.

## **1.1.6 Circular on risk exposure types: BaFin adopts EBA guidelines**

Circular 13/2019 (BA) entered into force on 1 January 2020. In it, BaFin implemented the EBA guidelines on specification of types of exposures to be associated with high risk in accordance with Article 128 (3) of the CRR (EBA/GL/2019/01) in full in its administrative practice.

Institutions are now required to apply EBA guidelines 2019/01 when allocating risk weights to new loans. However, if they establish that modifications are required in their existing portfolio, it is enough to apply the guidelines in their regular review of the exposure concerned.

The EBA guidelines provide a non-exhaustive list fleshing out Article 128 (1) of the CRR. This includes the financing of speculative investments in financial and non-financial assets, specialised lending for physical assets involving significant deficiencies or uncertainties regarding the finance, and equity exposures to a given issuer whose unsubordinated liabilities have already been assigned, or would be assigned, a risk weight of 150%. The items listed are based on Article 128 (2) (d) of the CRR and rules contained in the new standardised approach under the Basel III framework. These provide for a risk weight of 150%.

Where an institution independently creates a new group of exposures that are associated with particularly high risks under the general provision set out in Article 128 (1) of the CRR, the requirement to notify BaFin offers a procedure for involving the supervisory authorities (BaFin and the EBA) in their assessment, and of sharing the results with other institutions.

In addition, the EBA guidelines contain explanations clarifying the items listed in Article 128 (2) (a) and (c) of the CRR (investments in venture capital firms and investments in private equity).

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<sup>14</sup> "ICAAP" stands for "Internal Capital Adequacy Assessment Process".

<sup>15</sup> "SREP" stands for "Supervisory Review and Evaluation Process".

<sup>16</sup> EBA/GL/2016/10.

<sup>17</sup> EBA/GL/2018/02.

<sup>18</sup> Circular 06/2019 (BA) – Interest rate risks in the banking book.

### 1.1.7 BaFin bases new form for netting notifications on ECB process

For institutions to be able to recognise contractual netting agreements within the meaning of Article 295 (a), (b) or c) of the CRR as risk-reducing, these have to have been recognised by the supervisory authorities. A standard recognition procedure has applied since 31 January 2020 for the significant institutions (SIs) supervised by the European Central Bank, including a specially developed notification form. BaFin designed its own recognition procedure and the reporting form that it made available on 17 July 2020 in line with this.<sup>19</sup>

BaFin's recognition procedure applies to less significant institutions (LSIs). Above and beyond this, however, non-CRR credit institutions to which the CRR must be applied in accordance with section 1a of the Banking Act, and institutions as defined under point (3) of Article 4 (1) in conjunction with point (2) of the CRR, have also had to submit their netting notifications using the new form since the implementation deadline expired on 1 October 2020.

BaFin's new format reduces the checking involved in the recognition process and hence the amount of work that the institutions have to do. As is the case with the confirmation procedure used by the ECB for SIs, BaFin requires its institutions to use the notification form to submit the confirmations required (e.g. that the procedures set out in Article 297 (1) of the CRR exist).

### 1.1.8 Web form for LSI recovery plans

BaFin published an electronic web form in 2020. This replaces the Excel form entitled "Recovery planning based on the simplified requirements under section 19 of the SAG". The institutions can use the new form to create their recovery plans on the basis of simplified requirements (see info box) and then submit it to BaFin via the latter's reporting and publishing platform (the MVP Portal). Before doing so, institutions must register to use this specially created procedure. Roughly 20 institutions already submitted their electronic recovery plans using this channel in the reporting period. The recovery plans for all other institutions are to follow in 2021.

#### Note

### The German Recovery and Resolution Act

Section 12 (1) of the German Recovery and Resolution Act (*Sanierungs- und Abwicklungsgesetz*) requires institutions to draw up recovery plans and submit them to BaFin. Exceptions apply to institutions belonging to banking networks, which are exempted from this under section 20 (1) of the Recovery and Resolution Act. Section 19 of the Recovery and Resolution Act allows for simplified requirements for recovery planning under certain circumstances.

#### BaFin digitalises recovery planning

The electronic web form is a component of the "NIKE" project, which BaFin launched in October 2018. Its goal is the large-scale digitalisation of recovery planning using the simplified requirements set out in section 19 of the Recovery and Resolution Act. A number of database-driven applications are to support supervision of the recovery plans, from the consultation hearing and request to prepare a recovery plan through its submission and evaluation down to the provision of feedback to the institutions.

A database-driven evaluation tool is another component of the digitalisation project. This enables BaFin to evaluate recovery plans electronically and agree the findings. However, humans remain in charge of all steps in the process, allowing BaFin to take the specific situation at individual institutions into account.

### 1.1.9 European Covered Bonds Directive

The European Covered Bonds Directive (CB Directive) entered into force on 8 January 2020. This necessitates amendments to the German Pfandbrief Act (*Pfandbriefgesetz*), which must be adopted by 8 July 2021 and applied as from 8 July 2022 at the latest. These are probably unlikely to have any effect on future issuing activities by the *Pfandbrief* banks.

<sup>19</sup> See BaFinJournal August 2020, page 24 (only available in German).

### 1.1.10 German Securities Institutions Act

2020 saw the inception of the German Securities Institutions Act (*Wertpapierinstitutegesetz*). This is based on Directive (EU) 2019/2034 of the European Parliament and of the Council of 27 November 2019 on the prudential supervision of investment firms and will come into force on 26 June 2021.

In addition, Regulation (EU) 2019/2033 of the European Parliament and of the Council of 27 November 2019 on the prudential requirements of investment firms must be applied to these firms. The undertakings covered by the new rules will then no longer be subject to the Banking Act, as in the past.

The new rules are designed to establish an appropriate supervisory regime for securities trading firms and to take two specific features into account. On the one hand, these firms' business models differ to those used by classic credit institutions in particular due to the fact that securities trading firms do not accept deposits. On the other hand, the size and lack of interconnectedness of small securities institutions – which account for the bulk of securities trading firms – means they are not systemically important.

In addition, BaFin is active in EBA working groups that are drafting the regulatory technical standards (RTS) required by the regulation.

## 1.2 German institutions directly supervised by the ECB

In 2020, 52 German institutions were classified as significant institutions and were therefore subject to the Single Supervisory Mechanism (SSM) and directly supervised by the ECB.<sup>20</sup> BaFin was involved in the supervision of these institutions through the SSM's Joint Supervisory Teams (JSTs).<sup>21</sup>

### SSM activities during the COVID-19 pandemic

The coronavirus pandemic<sup>22</sup> in March 2020 also hit SSM Member States hard. The pandemic and the associated lockdowns impacted all European Union economies, albeit it to different extents. For example, Germany came through the crisis relatively well from an economic perspective in the period up to the end of the reporting

period. By contrast, other states, and particularly the southern EU Member States, were affected more badly. Comprehensive monitoring was immediately established within the SSM in order to be able to assess the pandemic's impact on banks in the various Member States and to react appropriately. The goal was and is to procure the information needed to assess the banks' economic position without placing an excessive organisational or operational burden on the institutions during what was already an intense crisis.

In the case of the Joint Supervisory Teams, which are responsible for supervising the banks, ECB Banking Supervision established additional supervisory contacts that, due to the pandemic, took and take place exclusively online. These focus on the core risk categories (business model and profitability; internal governance; credit, market and operational risk; and liquidity and funding risk). The insights gained and the information from regular reporting requirements and the reporting system are incorporated into a risk dashboard. Since the outbreak of the pandemic, the Supervisory Teams have focused in particular on the banks' ability to continue operating and on business continuity, e.g. on staff availability and the closure of bank branches and ATMs.

In addition, the SSM developed an evaluation tool that provides the Joint Supervisory Teams with information on the assumptions associated with, and results of, the sensitivity studies that the banks must produce. At the same time, the Teams responsible for supervising the largest SSM banks (Clusters 1 and 2) have been monitoring market risk trends (including counterparty credit risk) even more closely since the outbreak of the pandemic.

All additional SSM supervisory strategies introduced since the beginning of the COVID-19 pandemic are based on the principle of proportionality. Consequently, the frequency with which they are deployed depends on the risk position of the bank concerned. In 2020, the impacts of the pandemic on the SSM banks were still extremely limited, something that is undoubtedly due to the financial policy measures taken by the governments, but also to the more flexible supervisory approach. However, an increase in credit defaults as a result of the pandemic is to be expected in coming years. Equally, banks are still burdened by low profitability and low interest rate margins due to the low interest rate policy.

20 See the ECB's annual report, <https://www.ecb.europa.eu/pub/annual/html/index.en.html>.

21 See page 14 for information on BaFin's role within the SSM.

22 See also chapter I.1.



### The ECB's TRIM project

Further progress was made with the SSM's Targeted Review of Internal Models (TRIM) project despite the pandemic. Representatives of the ECB, BaFin and other supervisory authorities largely completed their work on it in 2020. The project, which was launched in 2016, aims among other things to ensure the same capital requirements apply within the SSM for the same risk positions, and to harmonise the supervision of internal models. BaFin's work on the project is helping to rebuild trust in the use of internal models, which was shaken by the financial crisis in 2007/2008.

Following publication in 2019 of the ECB Guide to Internal Models (EGIM) – a key milestone in the TRIM project – the SSM primarily put the finishing touches to the outstanding decisions on the basis of the results of the model reviews and the final version of the EGIM in 2020. To do this, the audit team conducted roughly 200 model reviews to establish whether the supervisory requirements had been observed. The plan was to wind up the project in early 2021. The enhanced supervision of internal models resulting from the TRIM project is to continue after this.

Following the successful completion of the TRIM project, banks and supervisors now face further challenges: the banks must remedy the deficiencies found in the reviews and the supervisors must check that they have done so.

### 1.3 Institutions directly supervised by BaFin

The process of consolidation in the German banking sector continued in 2020. At the end of 2020, BaFin was responsible for supervising a total of 2,750 institutions (see Table 1 on page 59). Of this figure, 52 were significant institutions supervised by the ECB, although BaFin was included in their supervision via the Joint Supervisory Teams. 2,698 institutions were directly supervised by BaFin, of which 1,324 were less significant institutions (see info box).

#### Continued high level of applications for authorisation by payment institutions

Once again, an increasing number of new players entered the market in 2020 following the transposition into national law of the Second Payment Services Directive (PSD2). The number of new applications for authorisation in the segment rose. BaFin granted seven new authorisations in 2020. Additional applications for authorisation were being processed at the end of the year.

#### At a glance

### Allocation to two sectors

The Banking Supervision Sector was responsible for supervising credit institutions, payment institutions and e-money institutions, and finance leasing and factoring institutions that were regarded as financial services providers. In addition, the Sector supervised 38 securities trading banks, since these are subsidiaries of institutions allocated to the SSM as significant institutions.

Otherwise, the supervision of securities trading banks is the responsibility of the Securities Supervision/Asset Management Sector. The same applies to financial services institutions. Allocation of the supervised institutions to the two sectors is based initially on whether they are credit institutions or financial services institutions, unless the business model for a particular type of institution is better suited to the supervisory focus and European supervisory framework of the other sector. For example, securities trading banks are generally supervised as securities trading firms in the Securities Supervision/Asset Management Sector although they are national credit institutions, while finance leasing and factoring institutions are covered by the Banking Supervision Sector although they are financial services providers.

#### New rules on crypto-assets in the Banking Act

The crypto custody business was included as a new financial service in section 1 (1a) sentence 2 no. 6 of the Banking Act by the German Act Implementing the Directive Amending the Fourth EU Anti-Money Laundering Directive (*Gesetz zur Umsetzung der Änderungsrichtlinie zur vierten EU-Geldwäscherichtlinie*). Undertakings wishing to perform this service therefore require authorisation. At the same time, crypto-assets were included in the catalogue of financial assets set out in section 1 (11) of the Banking Act. The act entered into force on 1 January 2020.

## 1.3.1 Credit institutions

### 1.3.1.1 Risk classification

The EBA's SREP Guidelines<sup>23</sup> require BaFin and the Deutsche Bundesbank to prepare an annual risk profile for all LSIs, i.e. less significant institutions, under their direct supervision (see Table 2 on page 59). Building on these EBA guidelines, the ECB published the SSM-LSI-SREP methodology in February 2020, in order to ensure a uniform procedure in the SSM for less significant institutions as well. Since then, BaFin has used two dimensions to classify institutions: the quality of the institution, which results from the application of the SREP, and the potential impact of a solvency or liquidity crisis at the institution on the stability of the financial sector.

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23 EBA/GL/2014/13 as amended on 18 July 2018.

When assessing the quality of the institutions, BaFin adopts the classification used in previous years: it defines four tiers ranging from 1 to 4 (very good to poor). In the same way, it classifies the impact dimension on a scale from I to IV (low to high).

It then uses this overall assessment as the basis for deriving the necessary supervisory measures and defining the audit cycles, the frequency of SREP capital determination and the depth of the annual risk analysis. No clear effects of the COVID-19 pandemic on the institutions' risk classifications were visible yet for the 2020 reporting period. BaFin expects to have robust insights towards the end of 2021.

### 1.3.1.2 Special audits

Special audits were not performed to the same extent in 2020 as in previous periods due to the coronavirus pandemic. BaFin ordered a mere 67 special audits in accordance with section 44 (1) sentence 2 of the Banking

#### 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 Banking Act 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.

Under 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 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).

**Securities trading banks** are not engaged in the deposit and credit businesses but in other banking business as specified in section 1 (1) of the Banking Act and therefore fall within the German definition

of a credit institution. A securities trading bank is engaged in the principal broking or underwriting business or provides a financial service in accordance with section 1 (1a) nos. 1 to 4 of the Banking Act as a credit institution. The business models operated by the securities trading banks range from traditional brokerage activities on the stock exchanges through own-account dealing down to the provision of corporate finance or trading in energy derivatives. Their product range includes equities and bonds, cleared and uncleared derivatives such as sovereign credit default swaps (CDSs), and energy derivatives and contracts for difference (CFDs). In addition, some securities trading banks offer crypto-asset services such as bitcoins.

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.

**Table 1: Institutions under German supervision**

As at 31 December 2020

<b>Credit institutions</b>		<b>1,529</b>
		1,378
of which	CRR credit institutions*+	of which SIs**+++ 52
		of which LSIs***+ 1,324
	Securities trading banks****++	38
	Other credit institutions*****+	41
	Of which development banks+	15
	Housing enterprises with savings schemes+	47
	Third-country branches+	25
Payment institutions and e-money institutions +		75
Financial services institutions*****		1,146
of which	Group III financial services institutions++	697
	Finance leasing and factoring institutions+	427
Institutions supervised by BaFin		2,750

\* 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.

\*\*\*\* Four of these credit institutions are supervised by BaFin's Banking Supervision Sector due to their group affiliation.

\*\*\*\*\* Including KfW. One of these credit institutions is supervised by BaFin's Securities Supervision Sector.

\*\*\*\*\* In addition to the institutions in financial services institutions Groups III and V (finance leasing and factoring institutions), institutions in Group I, II and IV are also included.

+ Supervised by BaFin's Banking Supervision Sector.

++ Supervised by BaFin's Securities Supervision/Asset Management Sector.

+++ Supervised by the ECB.

**Table 2: Risk classification results for LSIs in 2020\***

As at 31 December 2020

<b>Institutions in %</b>		<b>Quality</b>				
<b>Risk matrix</b>	<b>1</b>	<b>2</b>	<b>3</b>	<b>4</b>	<b>Total</b>	
Impact	High	0.0	0.5	0.2	0.0	0.7
	Medium	3.8	11.6	2.3	0.2	17.9
	Medium-low	7.7	40.5	7.7	0.6	56.5
	Low	2.7	14.9	6.4	0.9	24.9
<b>Total</b>	<b>14.2</b>	<b>67.5</b>	<b>16.6</b>	<b>1.7</b>	<b>100.0</b>	

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

Act (see Table 3). Normally the number of such audits is well over 100. For example, 161 special audits were performed in 2019. The question of whether a special audit is performed is closely related to an institution's risk classification. In addition to ad hoc special audits, a large number of routine audits are normally also performed (see info box). BaFin defines minimum numbers of these every year. However, most routine audits in 2020 were also cancelled.

#### At a glance

### Ad hoc or routine: special audits by BaFin

Audits in accordance with section 44 (1) of the Banking Act (special audits) are broken down into the following categories:

1. Ad hoc audits: In these cases, BaFin sees grounds to audit particular issues.
2. Scheduled or routine audits: no grounds are needed for these; they take place at regular intervals so as to enable BaFin to obtain a general impression of an institution.

BaFin always orders a special audit if it identifies a need for more information than cannot be satisfied using other sources such as the reporting system, the direct exchange of information with the institutions and the audit reports on the annual financial statements. Generally, special audits by BaFin focus on institutions' business organisation (compliance with the Minimum Requirements for Risk Management – MaRisk)<sup>24</sup> or the potential impairment of loan or securities portfolios. In addition, IT security is being audited more and more frequently (see Table 3).

**Table 3: Breakdown of special audits of LSIs in 2020 by areas of emphasis\***

As at 31 December 2020

	2020	2019
Impairment-related special audits	4	6
Section 25a (1) of the Banking Act (MaRisk)	63	133
Cover		5
Market risk models		1
IRBA (credit risk measurement)	12	16
AMA (operational risk measurement)		0
Liquidity risk measurement		0
<b>Total</b>	<b>79</b>	<b>161</b>

\* This table relates to less significant institutions (LSIs) under the supervision of the Banking Supervision Sector. "IRBA" stands for "Internal Ratings-Based Approach" and "AMA" stands for "Advanced Measurement Approach".

As a result, BaFin will catch up on a large number of audits once the pandemic is over. However, despite the adverse circumstances BaFin found ways of compensating for the cancelled audits. For example, it conducted more supervisory interviews or requested additional documentation, among other things so as to be able to obtain information more rapidly on the potential impact of the pandemic on institutions' business situations. It supplemented the information provided by the institutions by its own stress scenarios. These used data based on the previous LSI stress test. The objective was to obtain as comprehensive a picture as possible of the expected impact of the crisis on the banking market.

#### Highest audit ratio once again at other institutions

As in 2019, the majority of the special audits in 2020, were carried out in the cooperative sector, which represents the largest number of institutions in Germany. Measured in percentage terms, however, most audits were of other institutions – here too as in 2019. The largest audit ratio is for this group (see Table 4 on page 61).

Table 5 (on page 62) shows the breakdown of special audits of LSIs initiated by BaFin in 2020 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 12 special audits that had been requested by the institutions themselves.

<sup>24</sup> Circular 09/2017 (BA) – Minimum Requirements for Risk Management (*Mindestanforderungen an das Risikomanagement – MaRisk*).

### 1.3.1.3 Objections, measures and sanctions

The Banking Supervision Sector recorded a mere 491 objections and measures in 2020 (see Table 6 on page 62). In the previous year, there were 665 objections. The background is that fewer special audits took place and, as a result, there were fewer findings or grounds for objections or measures. In addition, BaFin had given banks greater leeway within the existing framework as a result of the pandemic so as to support them during the crisis.<sup>25</sup> This was another reason why it recorded fewer infringements regarding own funds, liquidity levels, and compliance with the rules for large exposures.

#### 1.3.1.3.1 Special factors associated with COVID-19

The supervisory risk analysis is based on the most recent audited annual financial statements, although it also incorporates other sources of information. The consequences of the coronavirus pandemic meant that the 2019 annual financial statements were only expected to be suitable for use as the basis for determining and imposing the SREP capital add-ons to a limited extent; as a result, the supervisors suspended the planned 2020 cycle for this and postponed scheduled resets. The capital add-ons that had previously been specified – the Pillar 2 Requirements (P2R) – therefore remained constant for 2020 apart from a few exceptions. However, BaFin will have to reset the SREP capital add-ons for all LSIs in 2021 and 2022.

<sup>25</sup> See also chapter III.7 for the measures.

### 1.3.1.4 The situation at credit institutions

#### Private, regional and specialist banks

Like all other credit institutions, private and specialist banks have been under pressure for years to cut costs due to ongoing low interest rates. In March 2020, the coronavirus pandemic brought new challenges. After a few, mostly technical, initial difficulties operations generally ran smoothly, even in crisis mode. Branches were only closed for a limited period and staff worked from home, or defined teams switched between working at home and working in the office.

Depending on the business model, additional organisational challenges arose when institutions were involved in applications for KfW<sup>26</sup> emergency loans. Equally, the advisory effort involved in deferrals and the need for associated technical adjustments were considerable in individual cases. BaFin stepped up its contacts with the institutions in order to receive an up-to-date picture of how the crisis was impacting this banking group's extremely heterogeneous business models. It also called for restraint when distributing dividends and profits. BaFin had issued a recommendation to this effect in March and repeated it in September to the German Banking Industry Committee.<sup>27</sup>

Generally speaking, the COVID-19 pandemic did not yet have any negative effects on the economic situation of private, regional and specialist banks in 2020. Going

<sup>26</sup> Kreditanstalt für Wiederaufbau.

<sup>27</sup> [www.bafin.de/dok/13888018](http://www.bafin.de/dok/13888018) (only available in German).

**Table 4: Breakdown of special audits of LSIs in 2020 by groups of institutions**

As at 31 December 2020

	Commercial banks	Savings bank sector	Cooperative sector	Other institutions
Impairment-related special audits	2	0	2	0
Section 25a (1) of the Banking Act (MaRisk)	11	24	27	1
Cover	0	0	0	0
Market risk models	0	0	0	0
IRBA (credit risk measurement)	8	0	0	4
AMA (operational risk measurement)	0	0	0	0
Liquidity risk measurement	0	0	0	0
<b>Total</b>	<b>21</b>	<b>24</b>	<b>29</b>	<b>5</b>
<b>Audit ratio in %*</b>	<b>18.1</b>	<b>6.4</b>	<b>3.6</b>	<b>26.3</b>

\* The ratio of the number of audits to the number of institutions in each group of institutions. This relates to LSIs supervised by BaFin's Banking Supervision Sector.

**Table 5: Breakdown of special audits of LSIs initiated by BaFin in 2020 by risk class**

As at 31 December 2020

Special audits initiated by BaFin		Quality of the institution				Total	Institutions* in %
		1	2	3	4		
Impact	High	0	2	0	0	2	25.0
	Medium	3	13	4	2	22	9.3
	Medium-low	0	19	7	1	27	3.6
	Low	1	7	6	2	16	4.8
	<b>Total</b>	<b>4</b>	<b>41</b>	<b>17</b>	<b>5</b>	<b>67</b>	<b>5.1</b>
<b>Institutions in %*</b>		<b>2.1</b>	<b>4.6</b>	<b>7.8</b>	<b>22.7</b>	<b>5.1</b>	

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

**Table 6: Supervisory law objections and measures under the Banking Act in 2020\***

As at 31 December 2020

Type of measure	Groups of institutions					Total
	LSIs				non-SSM	
	Commercial banks	Savings bank sector	Cooperative sector	Other institutions	Non-CRR credit institutions*	
Substantial objections/letters	39	40	68	3	8	158
Measures against managers	Dismissal requests***					
	Cautions					
Measures against members of supervisory/administrative boards	Dismissal requests***					
	Cautions					
Measures related to own funds/liquidity; exceeding the large exposure limit (sections 10, 13 and 45 of the Banking Act)	33	64	245	11	9	362
Measures in accordance with section 25a of the Banking Act	2				2	4
Sanctions in accordance with sections 45, 45b and 46 of the Banking Act**	7	2	1			10
<b>Total</b>	<b>81</b>	<b>106</b>	<b>314</b>	<b>14</b>	<b>19</b>	<b>534</b>

\* Including KfW.

\*\* 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.

forward, the results for the individual institutions are likely to be highly dependent on the business model involved. For example, institutions that are primarily active in the real estate and property development business or that finance high-value consumer goods are not expecting to suffer as a result of the pandemic. Banks that specialise in asset management and the securities business are even relatively upbeat about the future.

As at the end of the year, individual private banks applied to BaFin to expand their banking licences to include the crypto custody business as a financial service. They wanted to benefit from the advantages of blockchain technology and to respond to growing demand for crypto-assets.

### Savings banks

The situation at savings banks in 2020 was also largely dominated by the COVID-19 pandemic. However, with isolated exceptions this was not reflected in their balance sheets as starkly as had originally been feared. Although net interest income continued to decline due to the low interest rate environment, it was largely within the planning range. Growth in lending helped institutions here. Private mortgage lending in particular continued to increase. Savings banks were largely able to offset the lower fee and commission income resulting from the lockdown in spring over the course of the year. The ECB's call to systemically important institutions not to distribute any dividends or profits led at savings banks to the loss of income from investments in Landesbanks. For individual institutions this was quite painful.

There was no steep rise in impairment charges in the lending business during the reporting period, due among other things to the government aid measures. The impact of the pandemic is not expected to be felt until 2021. Equally, remeasurements effects in the securities business were not as high as originally thought due to the market recovery.

The trend towards branch closures continued in 2020, not least because of strong competitive pressure: some smaller branches that initially had to close temporarily in the course of the lockdown subsequently closed down their operations completely.

The savings banks largely followed BaFin's recommended relatively restrained approach to making distributions to their owners. Only a few savings banks with a strong capital base and consistently positive earnings forecasts distributed mostly small amounts to their owners.

### Bausparkassen

The Bausparkassen also had to deal in 2020 with both the low interest rate period, which has now gone on for years, and the current challenges posed by the pandemic.

Following the outbreak of the crisis, the entire sector initially recorded a tangible drop in new business in the spring. However, over the course of the year the *Bausparkassen* were able to significantly increase their new business. Nevertheless, they were unable to match the previous year's results in the period up to the end of December.

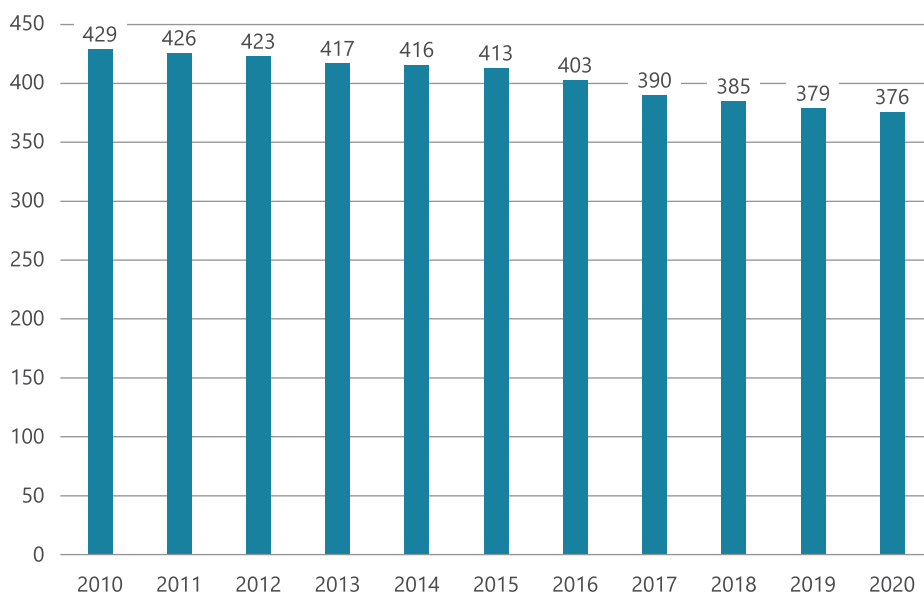
The decline in mortgage lending during the first wave of the pandemic was only moderate. Over the course of the year this business in fact performed positively, despite restrictions due to the coronavirus pandemic. As in previous years the sector succeeded in moving forward with its non-collective finance business, whereas demand for *Bauspar* loans remained low.

*Bausparkassen* offered their loan customers additional deferral agreements above and beyond the statutory moratorium rules under certain circumstances. There were no significant credit defaults due to the coronavirus pandemic in the entire sector in 2020.

Regardless of the pandemic situation, the *Bausparkassen* continued their efforts to reduce the impact on their earnings of older *Bauspar* plans paying interest that is no longer in line with market rates. They did this by terminating over-saved contracts and contracts that have been eligible for allocation for more than 10 years. New *Bauspar* plans that are in line with market interest rate are designed to improve earnings over the medium and long term while also lifting the proportion of *Bauspar* loans again.

There were 18 *Bausparkassen* in Germany at the end of the reporting period following the merger of Aachener Bausparkasse AG with Wüstenrot Bausparkasse AG.

**Figure 4: Number of savings banks\***



\* This statistic does not include six Landesbanks or DekaBank.

### Cooperative banks

The cooperative banks managed to maintain their position in financial year 2020 despite the difficult market environment. The problematic market situation, which was largely due to the COVID-19 pandemic, low interest rates and fierce competition, led to a decline in profits for the year after tax. Net interest income – the key source of income for the cooperative banks – also fell again year-on-year, despite positive effects from increased lending. Nevertheless, net fee and commission income rose slightly, exerting a stabilising effect on the results of operations. On the one hand, the cooperative banks benefited here from their modified fee strategy in the payments area. In addition, the ratio of administrative expenses to total assets fell slightly, although this was largely due to an increase in the latter.

The measurement gains/losses item deteriorated in 2020 compared to the prior-year figure. Whereas the cooperative banks recorded measurement gains in financial year 2019, a negative figure was produced in 2020, even though there were hardly any pandemic-related credit defaults. The background to this was that the institutions had increased their risk provisioning in the lending business as a precautionary measure, and in some cases sold securities, and realised the associated market losses, during the first lockdown because they wished to prevent further falls in prices that were feared. However, an increased need for write-downs and value

adjustments in the lending and securities business is to be feared in 2021 as a result of the pandemic.

The cooperative banks complied less often than other banking groups with the BaFin and ECB recommendations not to distribute any dividends in 2020 but rather to strengthen their capital base so as to cushion themselves against any potential impacts of the coronavirus pandemic. This was due not least to their relatively positive results for financial year 2019.

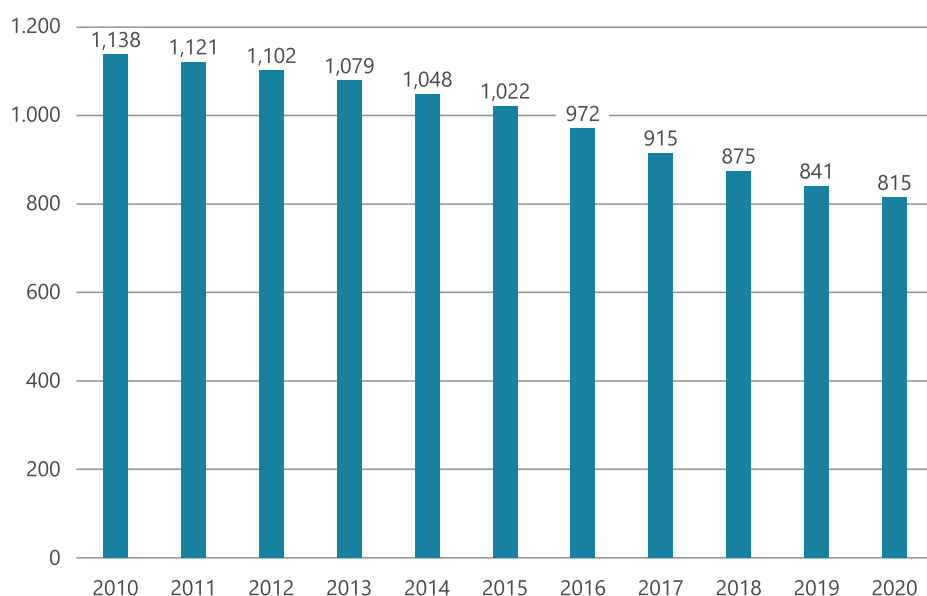
The institutions are continuing their drive to cut costs and improve efficiency since the environment will remain difficult going forward. In addition, they are pushing forward with digitalisation and sustainability projects.

### Pfandbrief business

The German *Pfandbrief* market performed well and issuance was robust in 2020 despite the COVID-19 pandemic. Although significantly fewer *Pfandbriefe* have been sold on the primary market since the start of the pandemic, *Pfandbrief* banks deposited an increased volume of retained *Pfandbriefe* as collateral with the ECB to procure liquidity. The background to this was the attractive terms offered by the ECB's targeted longer-term refinancing operations (TLTROs). The fact that *Pfandbriefe* are highly popular as a reliable and stable financial product, especially in times of crisis, can be



**Figure 5: Number of primary cooperative institutions**



seen from the further rise in the number of *Pfandbrief* banks year-on-year. The total at the end of 2020 was 86.

All in all, *Pfandbriefe* with a volume of €58.4 billion were sold in 2020 (see Table 7).

**Table 7: Gross *Pfandbrief* sales**

Year	Mortgage <i>Pfandbriefe</i> * (€ billion)	Public-sector <i>Pfandbriefe</i> (€ billion)	Total sales (€ billion)
2016	35.1	10.4	45.5
2017	36.8	11.9	48.7
2018	43.2	7.2	50.4
2019	43.7	11.2	54.9
2020	40.6	17.8	58.4

\* Including ship and aircraft *Pfandbriefe*, although these represent niche products.

In fact, at €363.3 billion, the total volume of outstanding *Pfandbriefe* was higher in 2020 than in the previous year (see Table 8).

**Table 8: Total volume of outstanding *Pfandbriefe***

Year	Mortgage <i>Pfandbriefe</i> (€ billion)*	Public-sector <i>Pfandbriefe</i> (€ billion)	Total volume outstanding (€ billion)
2016	203,7	155,2	358,9
2017	214,0	148,2	362,2
2018	230,5	134,1	364,6
2019	237,2	122,6	359,8
2020	242,4	120,9	363,3

\* Including ship and aircraft *Pfandbriefe*, although these represent niche products.

### Securities trading banks

Events on the financial markets in 2020 were dominated by trade disputes, the fallout from Brexit<sup>28</sup> and the COVID-19 pandemic. These developments also impacted the securities trading banks that do their business on the markets (see info box on page 58). Greater volatility allowed securities trading banks acting as market

<sup>28</sup> See also chapter I.3 for a discussion of Brexit.

makers, designated sponsors and liquidity providers to profit from the increased trading activity and lift their proceeds from trading.

In 2020, BaFin revoked one security trading bank's authorisation since it had repeatedly infringed its duties of conduct and organisation under the German Securities Trading Act (*Wertpapierhandelsgesetz*) and breached the Banking Act. Among other things, the institution had ignored the prohibition on accepting inducements and did not comply with its duty to take appropriate organisational measures to prevent conflicts of interest. In addition, it no longer had the requisite minimum number of two managing directors that have the necessary professional qualifications after its supervisory board had removed one. Following the revocation of its authorisation, the bank notified BaFin of its imminent insolvency. The competent court then opened insolvency proceedings at BaFin's request.

The United Kingdom's exit from the European Union as of 1 February 2020 and the transitional period until the end of the year also played a role in the supervision of securities trading banks. In the period since the Brexit vote, BaFin had granted a total of 12 new authorisations to securities trading banks wanting to relocate their business operations from London to Germany so as to be able to offer their services in the 27 remaining EU Member States. BaFin provided support for the new institutions that were setting up operations until the end of the transitional period. In particular, BaFin focused on the appropriateness of their workflows, organisational structures and human resources, and on whether they complied with the requirements for risk management and the outsourcing of significant areas.

### Foreign banks

The subsidiaries and branch offices of foreign institutions again played a significant role for the German market in 2020. Their business models range from niche activities, such as handling export trade financing with their country of origin, through investment banking and asset management, down to the full range of services offered by a universal bank.

These institutions are generally closely integrated with their parent groups' business strategy. From the perspective of a host supervisor, however, excessively close links can endanger the necessary independence of the management of such subordinate institutions or can negatively impact their proper business organisation. For example, if smaller units make substantial use of services provided by their foreign parent companies for cost or size reasons, they run the risk of no longer meeting

the requirements for quantitatively and qualitatively appropriate risk control and risk management – a precondition for their being able to take decisions independently.

This applies in particular to institutions that formed subsidiaries or branch offices in Germany for the first time in response to Brexit, or that transferred business from existing EU branches to them. The legal preconditions for Brexit were put in place by the 31 January 2020 exit date and BaFin and the ECB completed their authorisation and qualifying holding procedures in good time. However, some of the new arrivals still had difficulties when transferring customer relationships and establishing independent organisational structures. It seems likely that the uncertainty as to whether Brexit with all its consequences would actually happen at the end of the year 2020 prevented a large number of existing customers from switching from the UK unit to the company here.

In addition, the COVID-19 pandemic made relocating staff from the United Kingdom more difficult, and recruiting new employees was also more complicated in this situation. In some cases this also led to problems in approving internal models. Among other things, the necessary supervisory reviews became bogged down because portfolios had not been transferred or not enough staff were available to provide information.

This means that the temporary tolerance of the models, which had been granted to the parent companies by the UK's Prudential Regulation Authority (PRA) until 30 June 2022, will still require significant efforts to be made by both the banks and the supervisors.

### 1.3.2 Payment and e-money institutions

In 2020, BaFin granted nine authorisations under the German Payment Services Supervision Act (*Zahlungsdiensteaufsichtsgesetz*). At the end of 2020, therefore, a total of 76 institutions were authorised or registered as providers of payment services or e-money business operators.

Ongoing supervisory activities in this sector, as elsewhere, were dominated in 2020 by the effects of the COVID-19 pandemic. Payment and e-money institutions with customers primarily in the travel, tourism and events sectors, which were hit particularly hard by the crisis, experienced a clear decline in payment volumes in the second quarter of 2020 in particular. In addition, the

settlement of credit notes and chargebacks<sup>29</sup> impacted these institutions' liquidity situation.

Nevertheless, the institutions presented a robust picture overall during the COVID-19 crisis. Additionally, new opportunities opened up for institutions with business models featuring a high level of digitalisation – especially since many people are now increasingly switching to digital, contactless means of payment.

This is also reflected in the growth in the market for payment services. The number of new applications for authorisations remained at a high level in 2020. However, BaFin also observed a trend towards consolidation in the form of cross-border takeovers and mergers in parallel to the flow of new undertakings entering the market for payment services. For example, in January 2021 the Worldline Group confirmed that it was contributing several subsidiaries' operations to PAYONE GmbH. Then, on 9 March 2021 the European Commission approved the merger of Italy's Nexi Group and the Danish Nets Group. Both transactions impact payment services providers domiciled in Germany.

### 1.3.3 Financial services institutions

#### Securities trading firms

The term "securities trading firms" covers financial services institutions providing investment services, alone or in conjunction with ancillary services (see Table 9). They have one or more authorisations, e.g. to provide financial portfolio management, investment advice, investment broking and contract broking. Some institutions are also authorised to trade for their own account.

BaFin defined areas of emphasis in seven cases in 2020. It can use areas of emphasis in accordance with section 89 (4) of the Securities Trading Act or section 30 of the Banking Act to determine the content of audits above and beyond the statutory requirements, and hence to examine whether obligations under supervisory law have been complied with. The areas of emphasis related to the effectiveness of the Compliance function, the integration and monitoring of tied agents, customer education, suitability and appropriateness, costs and fees, and cold calling.

<sup>29</sup> The chargeback mechanism (the term used at Mastercard; known as the "dispute" procedure at VISA) is a contractually agreed transaction reversal mechanism provided by credit card companies. Credit card users can apply to the institutions issuing the cards (the "issuers") for a refund in certain defined situations (e.g. if a service was not actually provided).

**Table 9: Securities trading firms**

Securities trading firms	2020	2019
Securities trading firms under supervision	710	706 <sup>30</sup>
Domestic branches of foreign undertakings	43	94
Authorisations issued	24	44
Expanded authorisations issued	10	8
Authorisations returned	27	41
Tied agents	20,334	21,779
Liable undertakings	174	177
Inspections of institutions attended	4	6
Supervisory interviews with institutions	19	75

#### Finance leasing and factoring institutions

The leasing and factoring sectors also felt the impact of the COVID-19 pandemic. New leasing business for capital equipment fell by 8% in the first half of 2020; the same period of the previous year had seen an increase of 10%. The factoring industry recorded revenue growth of a mere 1.6% in the first half of 2020, following a strong increase (12%) in the prior-year period. Fraud represents the biggest risk for these institutions apart from default risk. For example, a factoring institution can be sold receivables that don't actually exist, or leasing institutions may enter into leases for items that do not exist, or that have been sold on and misappropriated. Such crimes and the risks resulting from them can endanger the institution's assets.

The firms involved seek to prevent this by, among other things, diversifying their clients and receivables, using limit systems and requesting balance confirmations. In addition, leasing institutions are inherently highly dependent in some cases on the leased assets and their manufacturers. Defaults were largely stable in 2020, but it remains to be seen how they will perform in 2021 in light of the pandemic.

<sup>30</sup> This figure also includes institutions that are exempt under section 2 (4) or (7) of the Banking Act.

**Table 10: Supervision of finance leasing and factoring institutions**

Facts	Figures 2020 (2019)
<b>Number of institutions under supervision</b>	
Finance leasing	249 (303)
Factoring	150 (158)
Both types of authorisation	28 (29)
<b>Routine cases processed</b>	
New authorisations	10 (23)
Terminated authorisations	68 (36)
Management changes	314 (177)
Supervisory board changes	83 (46)
Qualifying holding procedures	128 (224)
<b>Measures and sanctions</b>	
Substantial letters	13 (16)
Administrative fine proceedings initiated	21 (23)
Authorisations suspended	1 (1)

The substantial number of terminated authorisations and management changes is very largely due to a change in the law. The German Risk Reduction Act (*Risikoreduzierungs-gesetz*)<sup>31</sup> has exempted multiproperty leasing companies from the need to obtain authorisation in certain circumstances.

BaFin reacted to the COVID-19 crisis by sharing information regularly and closely with selected institutions since March 2020.

External sources notified BaFin of serious allegations about Grenke AG. Among other things, the institution was accused of accounting fraud. BaFin ordered an ad hoc special audit in accordance with section 44 of the Banking Act and commissioned an audit firm to perform this. According to the special auditor appointed, the final results of the audit will be submitted in the second quarter of 2021.

In the case of factoring institution AvP Deutschland GmbH<sup>32</sup>, which specialised in purchasing pharmacy receivables, BaFin took measures to avert danger as defined in section 46 of the Banking Act due to the concrete fear of payment difficulties: it appointed a special representative with the powers of a managing director, who applied for insolvency proceedings to be opened without delay and took measures to protect creditors. At the same time, BaFin filed a criminal complaint.

### 1.3.4 Crypto custody business

The crypto custody business was included as a new financial service in the Banking Act in the course of the implementation of the Fifth EU Anti-Money Laundering Directive.<sup>33</sup> At the same time, the lawmakers defined crypto-assets in section 1 (11) sentence 4 of the Banking Act. Firms wanting to provide this new financial service or conduct other business operations that now require authorisation as a result of the change in the law have required prior authorisation from BaFin since the law entered into force on 1 January 2020.

Firms that already conducted these business operations now requiring authorisation before the law took effect may continue to do so on the basis of transitional provisions. However, they had to apply for an authorisation by 30 November 2020 and to notify BaFin of their intention to do so by 31 March 2020.

BaFin provided the affected market participants with comprehensive information. One focus of both the authorisation procedures and the future supervision of the new service providers will be on the security of the cryptographic keys.

31 [www.bafin.de/dok/15626642](http://www.bafin.de/dok/15626642).

32 [www.bafin.de/dok/14744468](http://www.bafin.de/dok/14744468) (only available in German).

33 Federal Law Gazette I 19 December 2018, page 2602.



## 2 Insurance undertakings and *Pensionsfonds*

### 2.1 Bases of supervisory practice

#### 2.1.1 Amendment to the German Occupational Pensions Act

An amendment to the German Occupational Pensions Act (*Betriebsrentengesetz*) entered into force on 24 June 2020. Since then, employer pension commitments taking the form of a *Pensionskasse* have been included in the *Pensions-Sicherungs-Verein* (PSV)'s insolvency protection scheme.<sup>34</sup> Exceptions to this rule exist for pension commitments where the *Pensionskasse* belongs to the guarantee scheme for life insurers (*Sicherungsfonds für Lebensversicherer*) or is organised in the form of a common entity (*gemeinsame Einrichtung*) as defined by section 4 of the German Act on Collective Agreements (*Tarifvertragsgesetz*), or in cases in which the

employer is incapable of becoming insolvent (e.g. in the public sector).

Subject to any other rules governing the scope of insolvency protection, there is a claim against the PSV if one of the statutory insured events occurs at the employer and the *Pensionskasse* no longer fully provides the benefit that the employer has committed itself to. In the case of an insured event occurring before 1 January 2022, a claim exists against the PSV if the *Pensionskasse* curtails the intended benefit under the employer's pension commitment by more than one-half, or if the income received by the former employee falls below a defined threshold because of a curtailment. In the case of insured events occurring after 31 December 2021, BaFin can transfer the assets belonging to the *Pensionskasse* that are attributable to the employer, along with any liabilities, to the PSV.

Employers whose pension commitments fall under the above-mentioned insolvency protection scheme must pay contributions to the PSV as from 2021.

<sup>34</sup> Federal Law Gazette I, page 1271 ff.

The lawmakers also adapted the existing PSV insolvency protection scheme for pension commitments using *Pensionsfonds* in some areas in line with the new rules for *Pensionskassen*.

### 2.1.2 Amendments to the German Minimum Allocation Regulation and the German Regulation on the Supervision of *Pensionsfonds*

Due to the persistent low interest rate environment, life insurance undertakings, *Pensionskassen* and *Pensionsfonds* must top up their premium reserves so as to be able to service their guaranteed interest rates for the long term. Shareholders can help with finance by making equity injections, but are not generally obliged to do so.

The Minimum Allocation Regulation (*Mindestzuführungsverordnung*) and the Regulation on the Supervision of *Pensionsfonds* (*Pensionsfonds-Aufsichtsverordnung*) have been amended by the issuer in order to improve the conditions for voluntary equity injections.<sup>35</sup> The amendments came into force on 17 July 2020 and relate to the procedures to be adopted in cases in which it subsequently transpires that injections were not needed to finance the guaranteed benefit. In this case, the unused portions of the injections can be returned to the entities providing the capital in line with clearly defined procedure.

Due to the amendment of the Minimum Allocation Regulation, injections that have already been made by shareholders can be reflected in future capital flows under Solvency II, the European supervisory regime. This does not generally apply to shareholder capital injections that have been modelled. In such cases, the procedure to be adopted must be agreed in advance with BaFin.

### 2.1.3 Minimum requirements for own risk assessment

On 30 December 2020, BaFin published Circular 9/2020 (VA) regarding minimum supervisory requirements for own risk assessments to be observed by institutions for occupational retirement provision (IORPs).<sup>36</sup>

The Circular is addressed to IORPs that are supervised by BaFin, i.e. *Pensionskassen* and *Pensionsfonds*. In it, BaFin provides information on how to interpret the provisions for own risk assessment under the Insurance Supervision Act.

The Circular came into force upon publication.

### 2.1.4 Minimum requirements on the system of governance

The transposition into national law of the IORP II Directive at the beginning of 2019 brought about fundamental changes to the requirements on the system of governance for IORPs. As is the case for insurers under Solvency II, IORPs now have to establish certain key functions. In addition, they have to observe new, IORP-specific requirements, e.g. a whistleblowing obligation on the part of persons responsible for key functions.

BaFin fleshed out the new provisions on the system of governance for IORPs in more detail in its Circular entitled "Minimum requirements under supervisory law on the system of governance for IORPs" (MaGo for IORPs), which it also published on 30 December.<sup>37</sup>

The MaGo for IORPs applies alongside the supervisory law MaGo for Solvency II undertakings and the MaGo for small insurance undertakings. In these guidelines, BaFin provides information on how IORPs can take a principles-based approach to implementing the provisions relating to the system of governance, taking into account the room for manoeuvre open to them.

The Circular will enter into force on 1 June 2021. This means that BaFin is giving the IORPs sufficient time between publication and entry into force of the Circular, which they can and should use to make the necessary adaptations. In addition, BaFin drew up specific transitional provisions on outsourcing.

### 2.1.5 Genuine group insurance contracts

In the first half of 2020, BaFin conducted a consultation process for Circular 4/2020 (VA) "Notes on genuine group insurance contracts".<sup>38</sup> This aims to avoid

<sup>35</sup> Federal Law Gazette I, page 1688 ff.

<sup>36</sup> Circular 9/2020 (VA) – Minimum supervisory requirements for own risk assessments to be observed by institutions for occupational retirement provision (IORPs) (*Aufsichtsrechtliche Mindestanforderungen an die eigene Risikobeurteilung (ERB) von Einrichtungen der betrieblichen Altersversorgung*).

<sup>37</sup> Circular 8/2020 (VA) – Minimum requirements under supervisory law on the system of governance of institutions for occupational retirement provision (*Aufsichtsrechtliche Mindestanforderungen an die Geschäftsorganisation von Einrichtungen der betrieblichen Altersversorgung*).

<sup>38</sup> Draft Circular 4/2020 (VA).

shortcomings impacting the persons insured and to better protect and inform the latter. The Circular defines genuine group insurance contracts and supervisors' expectations with respect to the tripartite structure comprising insurers, policyholders and insured persons.

The Circular brings together the provisions on genuine group insurance contracts contained in the existing circulars 3/90, 3/94 and 2/97.

As a result of the opinions received in the course of the consultation procedure, BaFin excluded *Pensionskassen*, *Pensionsfonds* and direct insurance within the meaning of section 1b (2) of the Occupational Pensions Act from the Circular's scope.

## 2.2 Risk classification

BaFin assigns the insurance undertakings it supervises to risk classes that it uses to define how closely the insurers are supervised (see info box). In 2020, the number of good-quality insurers was on a par with the previous year (see Table 11 on page 72).

BaFin classified roughly 75% of insurers in the higher-quality range, i.e. as "A" or "B", in its 2020 risk classification. The proportion of undertakings with higher-quality ratings therefore remained at the same level as in the previous year. As in previous years, BaFin did not rate any insurers with high or very high market relevance as low-quality undertakings.

### Results for the individual classes of insurance

There were no significant shifts in either property/casualty insurers or reinsurers in 2020. The number of undertakings rated "A" or "B" in both classes was in excess of 80%.

#### At a glance

### Risk classification

Insurers are allocated to classes using a two-dimensional matrix that reflects the company's/ the group's market impact and quality. The market impact of *Pensionskassen* and *Pensionsfonds* is measured on the basis of their total investments. In the case of life insurers, calculated investment volumes also include investments from unit-linked life insurance. In contrast, the decisive factor used for health insurers, property/casualty insurers and reinsurers is these undertakings' total gross premium income. The total disclosed in the list of assets (= investments) was selected as the uniform criterion for classifying groups.

Market impact is measured on a four-tier scale of "very high", "high", "medium" and "low". The quality of the insurers is assessed on the basis of the following factors: "net assets and financial position";

"results of operations"; "system of governance"; "future viability"; and – in the case of group assessments – "group-specific factors".

BaFin determines the scores for first two factors using insurance-specific indicators, while the system of governance is assessed with the help of qualitative criteria. The "future viability" criterion comprises quantitative or qualitative criteria for specific classes of insurance that are suitable for assessing the company's/the group's prospective development. In addition, the "group-specific criteria" assesses all group-specific aspects going above and beyond the first four criteria. The rating system adds the ratings for the individual criteria together to produce an overall rating on a four-tier scale ranging from "A" (high quality) to "D" (low quality).

**Table 11: Risk classification results for 2020\***

Undertakings in %		Quality of the undertaking				Total
		A	B	C	D	
Market impact	very high	0.0	2.3	1.0	0.0	3.3
	high	1.3	7.2	3.0	0.0	11.5
	medium	3.8	17.6	6.5	0.4	28.3
	low	4.8	38.4	12.6	1.1	56.9
<b>Total</b>		<b>9.9</b>	<b>65.5</b>	<b>23.1</b>	<b>1.5</b>	<b>100.0</b>

\* The table shows the assessment based on the data as at 31 December 2020.

In the case of life insurers, over 95% were given “B” or “C” ratings. This represented an improvement in life insurers’ scores in the year under review. The proportion of life insurers with a “C” rating fell, while the proportion with a “B” rating rose.

By contrast, the proportion of health insurers with an “A” rating declined. Nevertheless, the proportion of health insurers in the upper quality range was still in excess of 70%.

*Pensionskassen* saw a slight increase in the organisations with a “C” rating, while in the *Pensionsfonds* category the proportion of organisations in the upper quality range increased.

#### **Slight decrease in the number of classified insurers**

The number of insurance undertakings and Pensionsfonds classified in 2020 fell marginally year-on-year.

#### **Classification of insurance groups**

As with risk classification for the above-mentioned insurance classes, the risk classifications for the insurance groups subject to Solvency II that are supervised by BaFin were validated and revised in 2020. Instead of simply adding together the classification results for the individual undertakings, the group classification uses both the classification results for the individual undertakings and qualitative and quantitative group-specific inputs. All in all, the classified insurance groups received a quality rating of either “B” (83%) or “C” (17%) during the year under review. 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. As a result, the data resulting from BaFin’s group-level risk classification add significant value and provide aggregated information on groups’ overall positions.

### **2.3 On-site inspections**

On-site inspections are also planned using a risk-based approach. Apart from the results of the risk classification, one of the factors that BaFin takes into account here 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 42 on-site inspections. This number was down significantly year-on-year due to the coronavirus pandemic. Other on-site inspections originally planned for 2020 were included in the planning for 2021, although their implementation will continue to depend to a large extent on how the pandemic progresses.

The risk matrix below (see Table 12 on page 73) shows the breakdown of inspections by risk class.



**Table 12: Breakdown of on-site inspections in 2020 by risk class**

On-site inspections		Quality of the undertaking				Total	Undertakings in %
		A	B	C	D		
Market impact	very high	0	2	0	0	2	4.8
	high	0	4	5	0	9	21.4
	medium	1	2	3	0	6	14.3
	low	2	14	9	0	25	59.5
	<b>Total</b>	<b>3</b>	<b>22</b>	<b>17</b>	<b>0</b>	<b>42</b>	<b>100.0</b>
<b>Undertakings in %</b>		<b>7.1</b>	<b>52.4</b>	<b>40.5</b>	<b>0.0</b>	<b>100.0</b>	

## 2.4 Authorised insurance undertakings and *Pensionsfonds*

The number of insurance undertakings supervised by BaFin declined slightly in 2020, while the number of *Pensionsfonds* rose marginally. At the end of the year under review, BaFin supervised a total of 536 insurance undertakings (previous year: 551) and 34 *Pensionsfonds* (previous year: 33 *Pensionsfonds*). Out of this total, 523 of the insurers were engaged in business activities and 13 were not.

**Table 13: Number of supervised insurance undertakings and *Pensionsfonds***

As at 31 December 2020

Insurance undertakings	with business activities	without business activities
<b>Life insurers</b>	81	5
<b><i>Pensionskassen</i></b>	135	2
<b>Funeral expenses funds</b>	31	1
<b>Private health insurers</b>	46	0
<b>Property and casualty insurers</b>	202	4
<b>Reinsurers</b>	28	1
<b>Total</b>	<b>523</b>	<b>13</b>
<b><i>Pensionsfonds</i></b>	34	0

## 2.5 Developments in the individual insurance classes

The following figures for 2020 are only preliminary. They are based on the interim reporting as at 31 December 2020.

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 some elements of interim reporting requirements.

### Life insurers

#### Business trends

New direct life insurance business in 2020 was down year-on-year, with approximately 4.6 million new policies as opposed to 5.1 million. The total value of new policies underwritten rose slightly by 2.8% to around €282.8 billion compared with €275.1 billion in the previous year.

The proportion of the total number of new policies accounted for by term life insurance policies fell from 32.8% to 30.0% year on year.

The proportion attributable to pension and other insurance contracts rose from 58.5% to 61.7% over the same period. The proportion of endowment life insurance policies declined by 0.4 percentage points to 8.3%.

Early terminations of life insurance policies (surrender, conversion to paid-up policies and other forms of early termination) remained at the prior-year level with 2.1 million contracts and a total sum insured of €106.5 billion.

There were a total of approximately 81.1 million direct life insurance contracts in force at the close of 2020, compared with 82.4 million in the previous year. However, the total sum insured increased by 2.9% to €3,319 billion. Term life insurance policies recorded a slight decrease in terms of the number of contracts, from 12.7 million to around 12.3 million, although the total sum insured increased from €853.6 billion to €888.5 billion. Pension and other insurance policies continued their positive trend of recent years, with the number of contracts growing from 57.3% to 58.9% of the total. The share of the total sum insured rose from 58.4% to around 59.5%.

Gross premiums written by German life insurers in the direct insurance business increased to €98.1 billion in the year under review (previous year: €97.6 billion).

### Investments

Aggregate investments increased in the year under review by 3.9% from €985.4 billion to €1,024.2 billion. Net hidden reserves rose to €215.0 billion at the year-end compared with €181.0 billion in the previous year as a result of the decline in interest rates. This corresponds to 21.0% of aggregate investments, following 18.4% in the previous year.

Preliminary figures indicate that the average net investment return amounted to 3.7% in 2020, below the prior-year level of 3.9%. One reason for continued high net investment return is likely to be the repeated increase in expenditure on building up the *Zinszusatzreserve* in 2020 and the associated realisation of valuation reserves.

### Projections

BaFin again prepared projections for the life insurers in 2020 (see the info box). BaFin uses the projections primarily to analyse how two different capital market scenarios affect insurers' performance for the current financial year.

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 can be expected that the undertakings' economic position will deteriorate further. BaFin will therefore continue to monitor the insurers very 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 suitable measures in good time and take appropriate precautions.<sup>39</sup>

#### At a glance

### Life insurance projections

The projection performed as at the 30 September 2020 reference date focussed on the medium- to long-term impact of the low interest rate levels on life insurers. To assess this, BaFin collected data on their forecast financial performance in accordance with the German Commercial Code (*Handelsgesetzbuch*) for the 2020 financial year and the following 14 financial years. When preparing the projections, BaFin assumed that new investments and reinvestments were made solely in fixed-interest investments with an interest rate of 0.5% and the conditions on the capital markets remained otherwise unchanged. In a second scenario, the life insurers were able to simulate new investments and reinvestments on the basis of their individual corporate planning, assuming no changes in capital market trends. In addition, the forecast Solvency II figures for three selected financial years were calculated for the first time.

### Solvency II

80 out of the 81 life insurers supervised by BaFin fell within the scope of Solvency II at the reporting date. A total of 70 out of the 80 undertakings employed the standard formula to calculate the solvency capital requirement (SCR) at the close of 2020, while 10 undertakings used a (partial) internal model. None of the life insurers used undertaking-specific parameters.

Of the total of 80 life insurers, 53 applied the volatility adjustment in accordance with section 82 of the Insurance Supervision Act and the transitional measure for technical provisions in accordance with section 352 of the Insurance Supervision Act. Four life insurers used only the transitional measure for technical provisions, while 10 undertakings employed the volatility adjustment in isolation.<sup>40</sup> Two undertakings applied the transitional measure for risk-free interest

<sup>39</sup> See also chapter I.5 on the impact of the low interest rate environment on insurers and *Pensionskassen*.

<sup>40</sup> Eleven life insurers used neither the volatility adjustment nor a transitional in 2020.

rates in accordance with section 351 of the Insurance Supervision Act, i.e. the transitional discount curve, in combination with the volatility adjustment. In total, therefore, 65 life insurers used the volatility adjustment, 57 life insurers the transitional measure for technical provisions and 2 life insurers used the transitional discount curve.

**SCR coverage**

All of the life insurance undertakings were able to report adequate SCR coverage as at 31 December 2020. The SCR ratio for all undertakings together (eligible own funds for the sector in relation to the SCR for the sector) amounted to 357.7% compared with 382.0% in the previous year.

Figure 6 shows the trend in SCR coverage ratios for the life insurance undertakings subject to interim reporting obligations.

**Composition of the SCR**

The SCR amounted to €40.8 billion as at 31 December 2020. Measured in terms of the gross basic SCR, an average of 72% of the capital requirements for undertakings applying the standard formula that were subject to interim reporting obligations in 2019 was attributable to market risk (excluding diversification effects). In addition, a significant proportion of the SCR related to underwriting risks for life (30%) and health (26%) insurance. By contrast, counterparty default risks (2%) were of relatively minor importance. The percentages given add up to more than 100% because diversification

effects, which reduce the gross basic SCR, have not yet been taken into account. These amounted to 28%.

The SCR required to be covered is calculated on the basis of the gross basic SCR, taking other variables into account. The loss-absorbing effects of the technical provisions (72%) and of deferred taxes (9%) contributed to a lower figure. Conversely, operational risk (3%) slightly increased the amount.

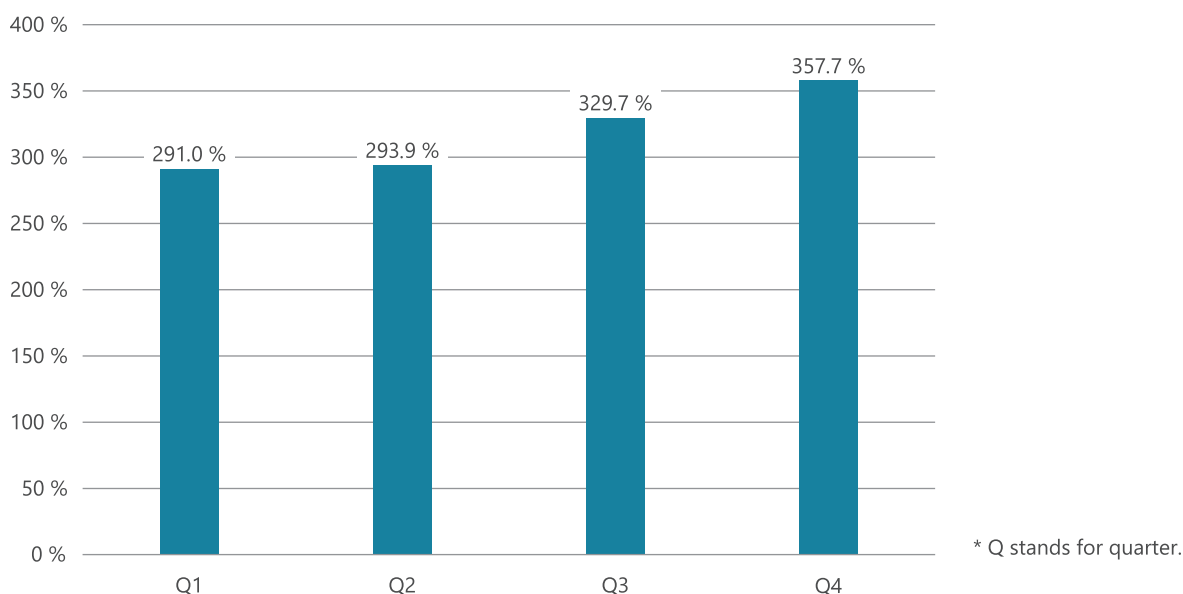
**Composition of own funds**

The own funds eligible for the SCR of the life insurance undertakings subject to interim reporting requirements amounted to €146.0 billion as at 31 December 2020. 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 a large majority of the remainder to the second-highest class (Tier 2). On average across the sector, the reconciliation reserve accounted for 67% of basic own funds, while surplus funds accounted for 25%. Other noteworthy components at the reporting date were share capital including issuing premiums (3%) and subordinated liabilities (2%).

**Remediation plans**

If undertakings apply one of the transitional measures incorporated in Solvency II and report inadequate SCR coverage without that measure, they must submit a remediation plan in accordance with section 353 (2) of the Insurance Supervision Act. In the plan, the

**Figure 6: SCR coverage ratios**



undertaking must set out the step-by-step introduction of measures planned to generate sufficient own funds or to reduce its risk profile, to ensure that it will comply with the solvency capital requirements 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 in their annual progress reports on the progress made with the measures, even if adequate SCR coverage has been restored at that time without the application of transitional measures.

### **Development of discretionary bonuses**

Most life insurers are making a moderate reduction in the 2020 level of discretionary bonuses for 2021 in view of the continuing low level of interest rates. The current total return, i.e. the sum of the guaranteed technical interest rate and the interest surplus, for the tariffs available in the market for endowment insurance policies is an average of 2.0% for the sector as a whole, down from 2.2% in the previous year. The figure in 2019 was 2.3%.

### **Changes in the *Zinszusatzreserve***

Since 2011, life insurers have been required to build up an additional interest provision (*Zinszusatzreserve*) to prepare for lower investment income in the future on the one hand and continuing high guarantee obligations on the other. More than €10.4 billion was expended on this in 2020. The cumulative *Zinszusatzreserve* at the end of 2020 amounted to €85.9 billion. The reference interest rate used to calculate the *Zinszusatzreserve* was 1.73% at the end of 2020.

### **Guaranteed interest rates in life insurers' new business**

High guaranteed interest rates from existing contracts can pose a challenge for life insurers in today's interest rate environment. This is why such risks must be avoided when calculating contributions and benefits in new business.<sup>41</sup>

For financial year 2020, BaFin examined the extent to which interest rate risk was included in new business. Long-term savings products account for 75.7% of new business, measured in terms of the contributions payable over the term of the policy. Pension insurance accounts for the largest proportion of this (90.9%). 12.6% of this figure was invested as unit-linked pension insurance without any guaranteed interest rates and 40.4% as hybrid pension insurance, where part of the money is invested conventionally and part is unit-linked. By 2024, the share of hybrid products in new pension insurance business is expected to grow to almost 50%.

The median guaranteed interest rate during the deferral period for all savings products with guaranteed interest rates across all life insurance undertakings was 0.68%. The figure for the payout phase was 0.77%.

### **Effects of the COVID-19 pandemic**

An increase in premium waivers can be observed for the second quarter of 2020. Equally, the number of new policies taken out fell. Similar effects were not observed in the remaining quarters of 2020.

By contrast, no significant impacts of the COVID-19 pandemic on the benefits extended by life insurance undertakings could be observed to date.

### **Private health insurers**

#### **Business trends**

The 46 private health insurers supervised by BaFin generated premium income totalling around €43 billion in 2020. This is roughly 4.5% more than in 2019. The growth in premiums was therefore higher than in the previous year. It was mainly attributable to new business, especially in supplementary insurance, and to premium adjustments.

With around 8.7 million persons insured and premium income of €28 billion (approximately 67% of total premium income), comprehensive health insurance was again by far the most important business line for private health insurers in 2020. Including other types of insurance such as compulsory long-term care insurance, daily benefits insurance and the other partial health insurance types, private health insurance undertakings insure approximately 44 million people.

#### **Investments**

The health insurers increased the carrying amount of their investment portfolio by 4.6% to approximately €316 billion in the year under review. Investments remained focused

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<sup>41</sup> See [www.bafin.de/dok/14015452](http://www.bafin.de/dok/14015452).

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 due in particular to high valuation reserves in fixed-income securities. As at 31 December 2020, net hidden reserves in investments amounted to around €63 billion, or roughly 20% of investments (previous year: 17%).

Preliminary figures put the average net investment return in the year under review at around 2.7%, a decline on the figure for the previous year (3.2%).

### **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 2020.

The remaining 40 health insurers were subject to Solvency II reporting requirements at the end of 2020. The majority of these health insurers use the standard formula to calculate the SCR. Four undertakings used a partial or full internal model. None of the undertakings used undertaking-specific parameters.

### **Transitional measures and volatility adjustment**

Two health insurers applied the volatility adjustment in accordance with section 82 of the Insurance Supervision Act and the transitional measure for technical provisions in accordance with section 352 of the Insurance Supervision Act in the year under review. One health insurer used the transitional measure for technical provisions only, while three undertakings employed the volatility adjustment as the sole measure. The health insurers did not apply the transitional discount curve, i.e. the transitional measure for risk-free interest rates in accordance with section 351 of the Insurance Supervision Act. Section 353 (2) of the Insurance Supervision Act requires that undertakings that apply a transitional measure and report a shortfall without that measure must submit a remediation plan. 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 SCR coverage as at 31 December 2020 and all quarterly reporting dates in 2020. Figure 7 on page 78 shows the SCR coverage ratios for the sector.

The SCR coverage ratio for private health insurers amounted to 474% as at 31 December 2019. This represents a year-end value, while the values shown in Figure 7 on page 78 are from intra-year reporting. The average SCR coverage ratio for the sector declined relatively sharply in the first quarter of 2020, due in particular to the substantial drop in fair values on the capital markets at the beginning of the coronavirus crisis, before recovering again over the course of the year.

The sector SCR for all private health insurers amounted to €7.2 billion as at 31 December 2020, based on the quarterly reporting. The health insurers were primarily exposed to market risk. This was responsible for around 74% of the capital requirements for users of the standard formula as at the close of the previous year. Around 47% of the capital requirements as at that date related to the underwriting risk for health insurance.

The eligible own funds for all health insurers amounted to approximately €31.0 billion as at 31 December 2020 according to the quarterly reporting. The health insurers reported the majority of their own funds in the reconciliation reserve. The proportion at the end of the previous year was approximately two-thirds. The surplus funds were another major component of own funds, accounting for just under one-third. Other components of own funds, such as share capital and the associated issuing premium, were comparatively unimportant.

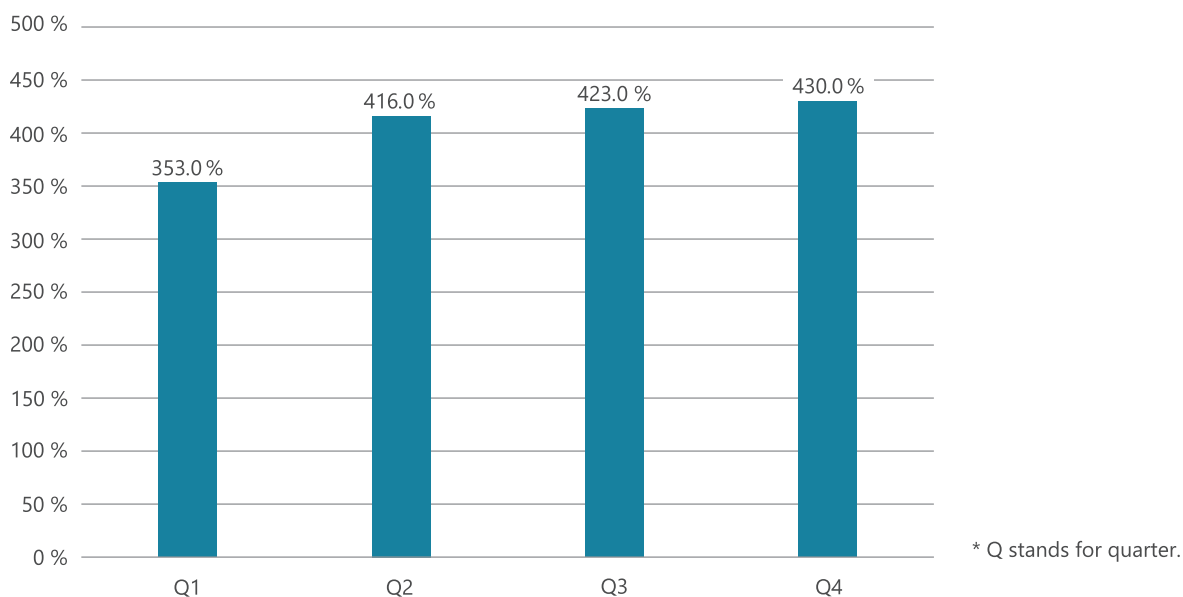
### **Projections**

BaFin also made a forecast for health insurers in 2020 in order to simulate the effects of adverse capital market developments on their performance and financial stability (see info box on page 78).

A total of 39 insurers participated in the projections. Only seven undertakings were exempted from taking part by BaFin. These are insurers offering non-SLT health insurance. These undertakings do not have to establish a provision for increasing age or generate a specific technical interest rate.

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 the risk attaching to new investments and reinvestments continues to arise in a low interest rate scenario, and

**Figure 7: SCR coverage ratios**



that investment returns decline. It follows that the technical interest rate must be gradually reduced by making premium adjustments.

**ACIR and technical interest rate**

The health insurers base their calculations of the technical interest rate on the actuarial corporate interest rate (ACIR) (see info box on page 79).

The figures for the ACIR calculated in the 2020 financial year are below the maximum technical interest rate of 3.5% stipulated in the German Health Insurance Supervision Regulation (*Krankenversicherungsaufsichtsverordnung*) throughout the sector. They continued to fall in comparison to

previous years due to the ongoing low interest rate environment. In most cases, therefore, insurers will have to make further reductions in the technical interest rates used for their premium rates. The ACIR guidelines contain a procedure for this, 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 entity under consideration.

Around 84% of insureds are affected by the premium adjustments for comprehensive health insurance that are pending in 2021. The average premium adjustment for the sector is approximately 10.1%. The health insurers

**At a glance**

**Health insurance projections**

The projection performed as at the 30 September 2020 reference date focussed on the medium-term impact of the low interest rate levels on the health insurers. To assess this, BaFin collected data on the forecast financial performance in accordance with the Commercial Code for the 2020 financial year and the following four years, using a variety of different unfavourable capital market scenarios in each case.

In one scenario, BaFin assumed that new investments and reinvestments were made solely in fixed-interest investments with a return on new investments of 0.5%. In a second scenario, the health insurers were able to simulate new investments and reinvestments on the basis of their individual corporate planning, assuming no changes in interest rates.

## Actuarial corporate interest rate

The business model for SLT (“similar to life techniques”) health insurance is based on premium rates that have to be reviewed annually for appropriateness. This involves examining all the assumptions on which the premium calculation is based – and especially those relating to changes in the net return on investments. Insurers estimate this trend and the safety margin that must also be factored into these assumptions on the basis of

the actuarial corporate interest rate (ACIR), which is produced by the German Association of Actuaries (*Deutsche Aktuarvereinigung – DAV*). Insurers must report their ACIR to BaFin each year. The ACIR determines whether they are also required to lower the technical interest rate for existing tariffs if they have to adjust their premiums.

have used a total of €2.6 billion of the provisions for bonuses to limit the increases in premiums.

### Property and casualty insurers

#### Business trends

Property and casualty insurers recorded a 3.8% year-on-year increase in gross premiums written in the direct insurance business in 2020 to €86.5 billion (previous year: €83.3 billion).

Gross expenditures for claims relating to the year under review fell by 3.3% to €24.7 billion (previous year: €25.5 billion). Gross expenditures for claims relating to prior years rose by 8.3% to €22.3 billion. Provisions recognised for individual claims relating to the year under review amounted to €22.3 billion, compared with €22.6 billion in the previous year; provisions recognised for individual claims relating to prior years amounted in total to €72.0 billion, compared with €69.5 billion in the previous year.

#### Motor vehicle insurance

Motor vehicle insurance was by far the largest insurance class in 2020, with gross premiums written amounting to €29.7 billion. This represented growth of 2.8% over the previous year. The increase was primarily due to a slight rise in the number of policies. Gross expenditures for claims relating to the year under review fell by a clear 11.0% year-on-year, due to reduced vehicle usage during the coronavirus pandemic. Expenditures for claims relating to previous years increased by 8.6%. In line with this, gross provisions recognised for individual claims relating to the year under review also fell, declining by 12.2%. Conversely, gross provisions recognised for individual claims relating to prior years rose by 5.9%.

### General liability insurance

Property and casualty insurers collected premiums of €11.6 billion (+5.5%) for general liability insurance. Claims relating to the year under review were up 1.8% year-on-year, at €1 billion. Claims relating to prior years led to expenditures by property and casualty insurers of €3.8 billion. Gross provisions for individual claims, which are particularly important in this insurance class, rose by 4.3% in the case of outstanding claims relating to the year under review, to €3.4 billion. Gross provisions for outstanding individual claims relating to prior years rose by a marginal 0.3% to €22.8 billion.

### Fire insurance

Insurers recorded gross fire insurance premiums written of €3.1 billion (+14.2%). Gross expenditures for claims relating to the year under review rose by 5.5% to €551.0 million.

### Residential buildings and contents insurance

Insurers generated premium income for comprehensive residential buildings insurance and comprehensive contents insurance of €11.9 billion (+5.6%). Expenditures for claims relating to the year under review remained almost unchanged, at €3.4 billion. Gross provisions recognised for individual claims relating to the year under review decreased by 6.9%. Expenditures for claims relating to previous years increased by 9.3%. Provisions for claims relating to previous years rose by 13.3%.

### Accident insurance

Premium income for general accident insurance amounted to €6.7 billion, 0.4% above the prior-year level. Gross expenditures for claims relating to the year under review fell by 10.6% to €411.2 million. €2.3 billion was reserved for outstanding claims relating to the year under review, 3.1% less than in the previous year.

## 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.

The average coverage ratio for German property and casualty insurers subject to Solvency I amounted to 515% at the end of 2019<sup>42</sup>.

## Solvency II

89% of property and casualty insurers were supervised in accordance with Solvency II as at 31 December 2019. 91% of all property and casualty insurers subject to reporting obligations under Solvency II used the standard formula to determine their solvency capital requirement (SCR). 14 insurance undertakings calculated the SCR on the basis of an internal model while 4 used a partial internal model. 11 insurers took up the statutory option of incorporating undertaking-specific parameters into the calculation of the SCR. 7 of them were legal expenses insurers.

All property and casualty insurers – with the exception of one very small specialist insurer – were able to report adequate SCR coverage as at 31 December 2020. The SCR coverage ratio for the sector as a whole amounted to 276.5% (see Figure 8 on page 81).

The SCR for the property and casualty insurers subject to interim reporting obligations was €44.8 billion in 2020. The minimum capital requirement (MCR) for the sector as a whole amounted to €14.6 billion. The most important risk drivers by far for property and casualty insurance were market risk and underwriting risk for non-life insurance. These accounted for 66% and 48% of the basic SCR respectively. Underwriting risk for health insurance (7%) and counterparty default risk (4%) were much less significant. The diversification effect, which reduces capital requirements, amounted to 25%, while the loss-absorbing effects of deferred taxes represented 18% of the basic solvency capital requirement.

Those German property and casualty insurers falling within the scope of Solvency II had eligible own funds for SCR coverage totalling €124.0 billion as at 31 December 2020. Around 96.5% of this figure was attributable to the highest category of own funds (Tier 1). Tier 2 own funds accounted for 3.1% and

Tier 3 own funds for 0.4%. The property and casualty insurers report the majority of eligible own funds in the reconciliation reserve. This accounted for approximately 89% of basic own funds as at 31 December 2020.

The relatively unchanged coverage ratio – compared to the life insurance sector, for example – mainly reflects the facts that property and casualty insurers do not issue long-term guarantees and that the average term of their investments is shorter. These undertakings are therefore considerably less sensitive, and react with much less volatility, to capital market movements.

## Reinsurers

Claims resulting from natural disasters in 2020 were once again in excess of the long-term average. Natural disasters are estimated to have caused total worldwide economic losses of US\$210 billion in 2020, with US\$82 billion of this figure being insured. The largest losses for the insurance industry occurred in the USA.<sup>43</sup> An extremely active hurricane season, a large number of tornadoes in the Midwest and extensive forest fires in California lifted the USA's share of global insurance losses to 82% (long-term average: roughly 60%). In Europe, by contrast, the level of claims from natural disasters made in 2020 was extremely moderate, impacting the insurance industry by approximately €3.6 billion.

Although the 2021 renewals round saw marked price increases across the market for the first time in a long time; average premium increases were less than 10% and hence considerably lower than had been expected in some cases. In Europe, in fact, average price increases were merely in low single-digit territory due to the low level of claims expenditures due to natural disasters. The only areas where double-digit increases were observed were in those insurance classes and regions impacted by losses, and on the retrocession market.

The fact that the market hardened less than had been expected is probably due to the persistent capital overhang. The comparatively high level of interest rates and the fact that underwriting risks are independent of other financial market risks continue to offer a significant incentive to invest in the reinsurance market. Brokers Aon Benfield<sup>44</sup> estimate that the supply of capital has now been restored to pre-COVID-19 pandemic levels after declining during the year. In addition, the catastrophe bond market was in full swing in 2020.

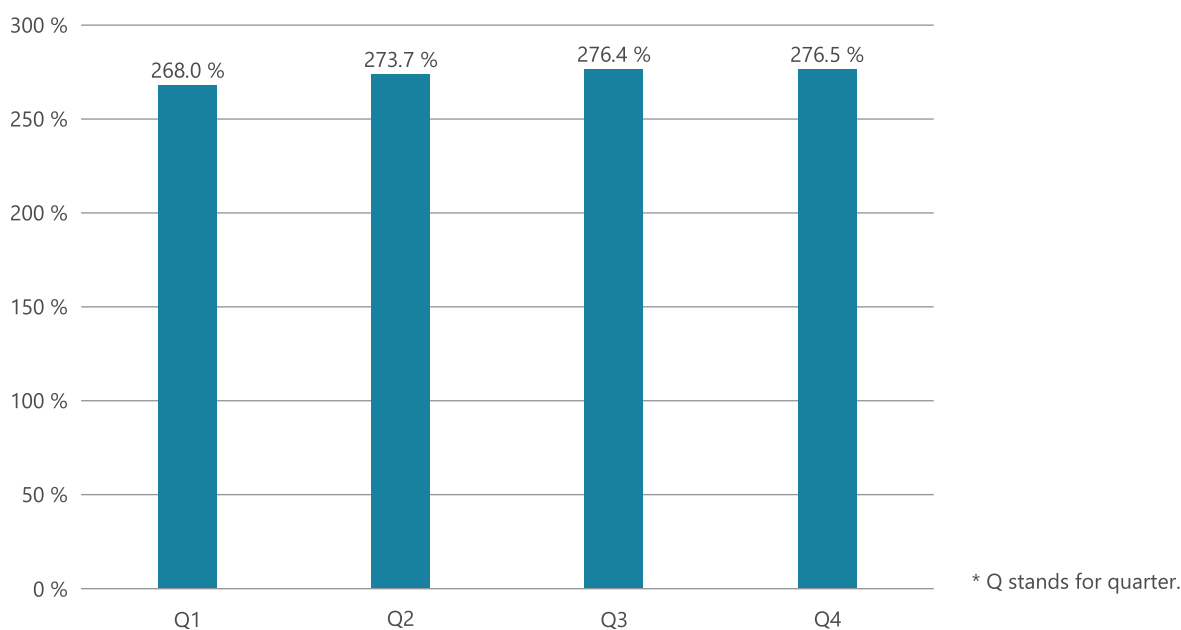
<sup>42</sup> The information relates to the 2019 financial year, since projections are not prepared for property and casualty insurers.

<sup>43</sup> Munich Re: Press release, 7 January 2021.

<sup>44</sup> Aon Benfield: Reinsurance Market Outlook January 2021.



**Figure 8: SCR coverage ratios**



The issue volume had never been higher than in 2020: new catastrophe bond issuance in the period up to the end of the year amounted to US\$16.4 billion<sup>45</sup>. Total catastrophe bonds in circulation had reached a record high of US\$46.4 billion by 31 December 2020.

It is not at all clear how long the reinsurance market will continue to harden. Natural disasters are playing a much smaller role compared to such phases in the past. In particular, the substantial uncertainty regarding the consequences of the COVID-19 pandemic and the ultimate level of claims expenditures are likely to play a key role here. Other factors such as persistent low interest rates and the impact of climate change are also tending to push up prices. However in many cases the supply of capital is decisive. To this extent, disciplined underwriting by reinsurers is critical to further developments, especially in cases in which claims from natural disasters are only moderate.

### Solvency II

Of the 30 German reinsurance undertakings subject to supervision by BaFin in 2020, 29 were required to comply with the Solvency II reporting obligations. These had own funds of around €247.5 billion as at 31 December 2019 (previous year: €212.6 billion). At the same date, the solvency capital requirement amounted to approximately €87.3 billion (previous

year: €64.1 billion). The significant rise in the capital requirement mainly reflects changes in the internal model for a major reinsurer that also acts as the holding company for a large insurance group. This resulted in an average SCR coverage ratio of around 283% (previous year: 331%). Average MCR coverage amounted to 849% as at the reporting date (previous year: 957%).

The range of coverage ratios within the reinsurance sector is considerable, especially with respect to the MCR. As at 31 December 2019, reinsurers reported SCR coverage ratios of between around 132% and 559%, and MCR coverage ratios of between 117% and 2,234%. None of the reinsurance undertakings reported inadequate capital coverage as at 31 December 2019.

### Heterogeneous market

The wide range of 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 a number of reinsurance undertakings that also perform the function of a holding company for an insurance group or a financial conglomerate. In such cases, reinsurance activities are frequently subordinate to the holding company function and this is reflected, among other things, in more than adequate capital resources from the reinsurance perspective. Even though reinsurance undertakings represent only 5.5% of all insurers in terms of numbers, they nevertheless account for around 47% of all own funds.

<sup>45</sup> ARTEMIS: Q4 2020 Catastrophe Bond & ILS Market Report.

According to the quarterly reports submitted, reinsurance undertakings' own funds rose to an overall total of €257.0 billion as at the 31 December 2020 reporting date, while the solvency capital requirement also increased, to €95.7 billion. The coverage ratio amounted to approximately 268%.<sup>46</sup>

## **Pensionskassen**

### **Business trends**

Like life insurers, the *Pensionskassen* were also required to submit projections in 2020. The results show that the total premium income generated by *Pensionskassen* in 2020 declined year-on-year. Premiums earned totalled approximately €6.5 billion in the year under review, a year-on-year decrease of around 5.4%. In 2019, they had declined by 5.2%.

Premium income for the stock corporations formed since 2002, which offer their services to all employers, fell by around 3.9% compared with the prior year, to €2.3 billion. In the case of the mutual insurance associations funded largely by employers, premium income shrank by roughly 6.1% to approximately €4.2 billion.

### **Investments**

The aggregate investment portfolios of the *Pensionskassen* supervised by BaFin grew by 5.2% in 2020 to approximately €186.1 billion (previous year: €176.9 billion). The dominant investment types are still "investment units, bearer bonds and other fixed-income securities", plus "registered bonds, notes receivable and loans".

The sector's hidden reserves grew to around €33.2 billion (previous year: €29.6 billion) according to preliminary figures. This corresponds to roughly 17.8% of the aggregate investments (previous year: 16.7%). Hidden liabilities are relatively insignificant, at 0.3% overall.

### **Projections and impact of the low interest rate environment**

In its projections as at the 30 September 2020 reference date, BaFin requested the *Pensionskassen* to estimate their results for the financial year under four equities 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 certain *Pensionskassen* – including those with premium rates to which the German Premium Reserve Regulation (*Deckungsrückstellungsverordnung*) applies and which are required to build up a *Zinszusatzreserve*, plus those *Pensionskassen* subject to more intensive supervision – the projections were extended even further to cover the following 14 financial years.

As the analysis of the projections showed, the coverage ratio for the SCR for the 2020 financial year was lower than the prior-year level. In general, the undertakings were able to comply with the solvency requirements, which are not based on Solvency II but on the specific rules set out in the IORP II Directive. In BaFin's opinion, therefore, the sector's short-term risk-bearing capacity seems to be assured as before. Based on the projections, the *Pensionskassen's* overall net return on investment was approximately 3.3% in 2020 (previous year: 3.8%).

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 individual *Pensionskassen* should have to strengthen their biometric actuarial assumptions or reduce the technical interest rate, they will find it increasingly difficult 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 projections for 2020: in almost all cases, *Pensionskassen* recognised additional reserves so as to strengthen the actuarial assumptions used to calculate their premium reserves.

BaFin is continuing to monitor and support the *Pensionskassen* closely, to ensure that these can maintain and strengthen their risk-bearing capacity as far as possible even given persistent low interest rates. *Pensionskassen* that have been particularly badly affected by the low interest rate environment are subject to 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 concerned.

However, it is becoming clear that certain *Pensionskassen* will require additional funds if the low interest rate environment persists. For *Pensionskassen* in the form of mutual insurance associations, it would

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<sup>46</sup> Further information and figures for the reinsurance business can be found in BaFin's 2019/2020 statistics on reinsurance undertakings, which are available on BaFin's website.

be appropriate for their sponsoring undertakings to make funds available. *Pensionskassen* in the form of stock corporations would turn to their shareholders. If the necessary support is not received, *Pensionskassen* may no longer be able to meet their obligations to beneficiaries in full.

If an employer grants occupational retirement benefits to its employees and appoints a *Pensionskasse* for this purpose, it has an obligation under the Occupational Pensions Act to pay the benefits granted itself in the worst case. This gives the beneficiaries and pensioners additional security.

### Solvency

The projections reveal that the solvency margin ratio set out in the German Capital Resources Regulation (*Kapitalausstattungs-Verordnung*) applicable to the *Pensionskassen* declined year-on-year to an average of 138% as at the 2020 reporting date. According to the estimates, two *Pensionskassen* were unable to comply with the solvency requirements as at 31 December 2020.

### Pensionsfonds

#### Business trends

*Pensionsfonds* recorded gross premium income totalling €5.0 billion in 2020, compared with €2.6 billion in the previous year. The fluctuations in premium income are attributable in particular to the fact that, depending on the type of commitment agreed, *Pensionsfonds* often involve the payment of single premiums.

The total number of beneficiaries rose in the year under review to 1,171,314 compared with 1,112,677 in the previous year. Of these, 707,571 were vested employees who are members of defined contribution pension plans, while 96,125 were vested employees who are members of defined benefit pension plans. Benefits of €2,706 million were paid to 375,036 people drawing them.

#### Investments

Investments for the account and at the risk of *Pensionsfonds* grew from €3,161 million to €3,475 million in the year under review. The largest share of the portfolio (55%) consisted of contracts with life insurance undertakings. Net unrealised gains in the investments made by *Pensionsfonds* totalled €381.4 million as at the 31 December 2020 reporting date (previous year: €267.8 million).

Assets administered for the account and at the risk of employees and employers grew from €45.5 billion to €51.1 billion in the year under review. Roughly 91% of

these investments, which are measured at market value in accordance with section 341 (4) of the Commercial Code, consisted of investment units.

### Projections and low interest rate environment

BaFin prepared projections in 2020 for 32 *Pensionsfonds* (see info box). The particular focus was on the expected profit for the year, the expected solvency and the expected valuation reserves at the end of the current financial year.

#### At a glance

### Projections for *Pensionsfonds*

The scenarios defined by BaFin for the *Pensionsfonds* projections were the capital market situation as at the 30 September 2020 reference date and a negative equities scenario involving a 24% drop in prices. In addition, BaFin required scenarios to be calculated that combined each of the two above-mentioned scenarios with a 200 basis point increase in the interest rate term structure.

The evaluation of the projections indicated that the 32 *Pensionsfonds* included in them would be able to withstand the four defined scenarios from a financial perspective. The obligations recognised by the *Pensionsfonds* in their financial statements are largely not guaranteed by the *Pensionsfonds*, while the guarantees are covered by congruent reinsurance in some cases. The technical provisions for the account and at the risk of employees and employers are recognised retrospectively in line 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, assuming no change in the capital market situation, supplementary contributions would have become due for nine *Pensionsfonds* as at 31 December 2020.

BaFin also considers it necessary to address the potential medium- and long-term ramifications for the *Pensionsfonds* of an even longer low interest rate period. In the course of the projection exercise, the *Pensionsfonds* were again also asked to estimate their

expenses for the *Zinszusatzreserve* for the following four financial years. 18 out of the 21 *Pensionsfonds* that operate insurance-based business have so far been required to establish a *Zinszusatzreserve*. Funding of these 18 *Pensionsfonds* is currently guaranteed through congruent reinsurance cover, or through current income or surpluses. In addition, the *Pensionsfonds* were asked to state the probable coverage of the solvency capital requirement under the Regulation on the Supervision of *Pensionsfonds* for the next four financial years.

### **Solvency**

According to the preliminary figures, all of the *Pensionsfonds* had sufficient own funds. They therefore complied with BaFin's solvency requirements. In the case of around two-thirds of the *Pensionsfonds*, the level of own funds required by supervisory law corresponded to the minimum capital requirement of €3 million for stock corporations and €2.25 million for mutual *Pensionsfonds*. The individual SCR for these *Pensionsfonds* is less than the minimum capital requirement. This is due either to the relatively low volume of business or to the type of business concerned.



## 3 Securities trading and the investment business

### 3.1 Monitoring of market transparency and integrity

If BaFin receives – external or internal – information on market abuse, it first conducts an analysis (see 3.1.1) to

establish whether this information contains sufficient evidence of market abuse. If so, BaFin launches a formal investigation (see 3.1.2). Where this investigation corroborates the evidence that prohibitions on market abuse have been breached, BaFin either files a complaint with the public prosecutor's office, or the division responsible for prosecuting administrative offences will deal with the matter (see 3.1.2).

**Table 14: Market abuse analyses in 2020**

	<b>New suspicious transaction and order reports</b>	<b>Analyses completed</b>	<b>Analyses yielding sufficient evidence</b>
2020			
<b>Total</b>	<b>2,625</b>	<b>1,857</b>	<b>22</b>
Market manipulation	1,547	1,143	9
Insider trading	1,069	689	13
Mixed cases	9	25	0
Reference year 2019			
<b>Total</b>	<b>2,471</b>	<b>3,767</b>	<b>25</b>
Market manipulation	1,557	2,635	10
Insider trading	888	1,081	15
Mixed cases	26	51	0

### 3.1.1 Market abuse analyses

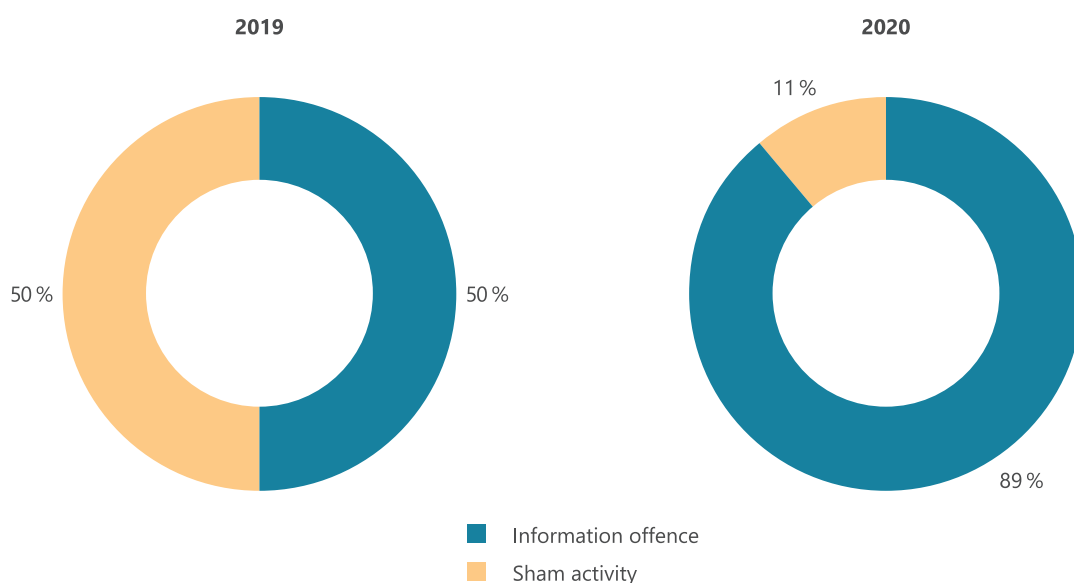
In 2020, BaFin produced substantially fewer market abuse analyses than in the previous year (see Table 14 on page 85). The large number of analyses in 2019 is due to the fact that the even more strongly risk-based approach that BaFin adopted with effect from that year allowed it to finalise numerous earlier cases, which were then included in the statistics for 2019. In 2020,

the number of suspicious transaction and order reports remained at the previous year's high level.

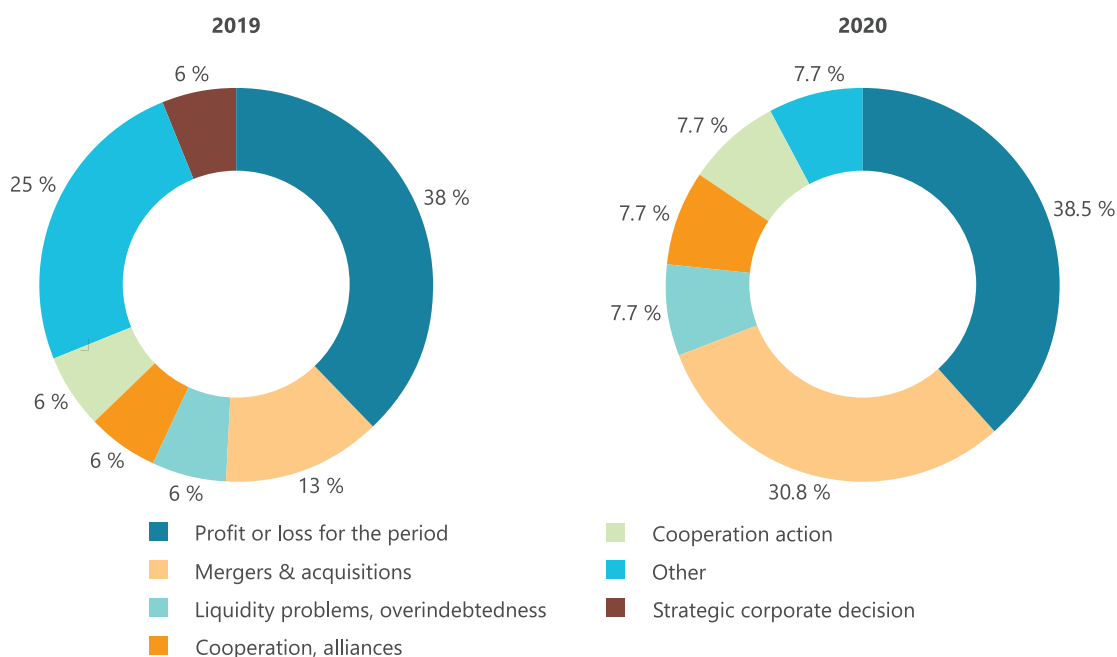
#### 3.1.1.1 Market manipulation

9 analyses conducted by BaFin in 2020 found sufficient evidence of market manipulation. Figure 9 shows the categories to which the individual cases were allocated in the year under review and the previous year.

**Figure 9: Breakdown of market manipulation evidence**



**Figure 10: Breakdown of insider trading evidence**



### 3.1.1.2 Insider trading

13 analyses conducted in 2020 found sufficient evidence of insider trading. Figure 10 on page 86 shows the percentage breakdown across the different categories of inside information in the year under review and the previous year.

### 3.1.2 Market abuse investigations

#### 3.1.2.1 Market manipulation

##### 3.1.2.1.1 Developments in 2020

BaFin's risk-based approach is not restricted to its analysis of market manipulation, but also applies to the resulting investigations. Since it concentrates on breaches with greater relevance, BaFin launched fewer new investigations in 2020 and also filed fewer criminal complaints than in the previous year (see Table 15 and Table 16).

**Table 15: Market manipulation investigations**

Period	New investigations	Investigation results						Ongoing investigations	
		Investigations discontinued	Referred abroad	Investigations referred to public prosecutors' offices or BaFin's Administrative Fines Division					Total (cases)
				Public prosecutors' offices		Administrative Fines Division			
				Cases	Individuals	Cases	Individuals		
2018	149	84		77	124	4	4	<b>81</b>	<b>277</b>
2019	96	130	3	27	45	0	0	<b>27</b>	<b>213</b>
2020	56	49	0	21	32	0	0	<b>21</b>	<b>199</b>

\* The number of referrals to BaFin's Administrative Fines Division and the number of administrative fine proceedings initiated by BaFin (see 3.6) differ because different processes are involved.

**Table 16: 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
		in accordance with sections 152 (2) and 170 (2) of the Code of Criminal Procedure	in accordance with section 153 of the Code of Criminal Procedure	in accordance with sections 154 and 154a of the Code of Criminal Procedure	in accordance with section 154f of the Code of Criminal Procedure		
2018	<b>268</b>	138	31	16	14	43	5
2019	<b>177</b>	109	12	11	2	22	0
2020	<b>206</b>	126	14	8	6	17	0

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	Convictions following full trial	Acquittals	Investigations discontinued	Final administrative fines
2018	0	6	7	3	3	7
2019	3	5	4	0	4	5
2020	17	2	10	1	4	1

\* The figures relate to rulings from previous years of which BaFin only became aware in the years specified in the left-hand column.

### International cooperation

In 2020, BaFin again worked together with foreign supervisory authorities on many investigations (see Table 17). It primarily shared information with supervisory authorities in other EU Member States, such as authorities in Austria and France, but also with the United Kingdom, which had already formally left the European Union (EU) at the beginning of the year. As regards countries outside the EU, BaFin received assistance for its investigations into market manipulation in particular from the Canadian and Swiss supervisory authorities.

**Table 17: Requests for international administrative assistance regarding market manipulation**

Period	Requests made	Requests received	Total
2018	75 (to 22 countries)	31 (from 12 countries)	<b>106</b>
2019	36 (to 18 countries)	29 (from 7 countries)	<b>65</b>
2020	34 (to 18 countries)	30 (from 12 countries)	<b>64</b>

#### 3.1.2.1.2 Selected focus areas for investigations

##### Curcas Oil N.V.

Anyone publishing an opinion on a financial instrument, be it in traditional or electronic media, may not do so for reasons of personal gain, i.e. in order to influence prices. Any conflicts of interest that exist when buy or sell recommendations are made must be disclosed appropriately. If several people jointly commit an offence, section 25 (2) of the German Criminal Code (*Strafgesetzbuch*) states that the actions of each of them are attributable to all of them.

Facts of the case: The accused, who had no previous convictions, had listed the shares of Curcas Oil N.V. on the regulated unofficial market of the Frankfurt Stock Exchange. He himself held some of Curcas Oil's shares via a company domiciled in the Caribbean state of St. Vincent and the Grenadines, which he controlled as the sole beneficial owner. In order to sell his shares as profitably as possible, he used intermediaries to commission the market letter "Tiger & Dragon", among others, to advertise the Curcas Oil shares. He paid a turnover-dependent commission of 30% for this. The market letter distributed e-mails with specific buy recommendations for the stock, but without disclosing the conflict of interest. The accused took advantage of the artificially generated demand to sell his shareholding at a profit.

Punishment: The Munich I Regional Court (*Landgericht*) – Commercial Crime Division – deemed a prison sentence of three years and six months to be appropriate to the crime and the accused's degree of culpability. At the same time, it passed a ruling seizing and forfeiting a total of €5.9 million as an equivalent sum of money. The judgement is final.

##### Various EUREX futures products

If, in the case of market manipulation using phantom orders (see info box), the public prosecutors discontinue an investigation under section 170 (2) of the German Code of Criminal Procedure (*Strafprozessordnung*) because, while they can prove a manipulative act within the meaning of section 20a of the German Securities Trading Act (*Wertpapierhandelsgesetz*), old version, they cannot prove its effect on the exchange or market price of the financial instrument concerned, it is possible to nevertheless pursue the manipulation as an administrative offence.

##### Definition

#### Phantom orders

A phantom order is when a trading participant places a buy or sell order with the intention of cancelling it before execution. The order is placed with the aim of misrepresenting the order situation to other market participants. Phantom orders falsely give the impression that there is interest in trading the stock. This could lead to other market participants gaining the wrong impression of the supply and demand situation. Consequently, phantom orders are prohibited as a form of market manipulation.

In line with this, the public prosecutors' office in Frankfurt am Main – which specialises in white-collar crime – discontinued the investigation that had been launched following a criminal complaint filed by BaFin over trade-based market manipulation: it seemed unlikely that it would be possible to prove the necessary impact on prices as defined section 38 (2) of the Securities Trading Act, old version ("successful manipulation"). The discontinuation of the investigation against the accused related only to his alleged criminal conduct. Consequently, since BaFin was the competent administrative authority, it was free to pursue the surviving allegation of market manipulation as an administrative offence.



Facts of the case: The accused – in his capacity as an organ authorised to represent a legal entity – had placed a large number of large-volume buy and sell orders in Euro Bund futures (FGBLs), BOBL futures contracts (FGBMs), DAX futures, EURO-STOXX-50 futures and Euro-OAT futures on the EUREX futures exchange. Shortly afterwards, he placed orders on the opposite side of the order book in each case that represented his true interest in trading. As soon as the orders on the opposite side of the order book had been executed, the suspect cancelled the large orders. The accused’s trading behaviour was part of a systematic strategy. Although the large orders that he placed accounted for up to 78% of total volumes on the relevant order book pages, their rapid deletion meant that they were not executed in up to 99% of cases. This order behaviour made it possible to obscure the true market situation.

Administrative fine: BaFin imposed five individual administrative fines of €40,000 each on the company. The administrative order imposing the fines is final.

**Banpu PCL Reg. Shares and Astaldi S.p.A.**

Facts of the case: The accused issued offsetting buy and sell orders in two financial instruments in three cases, having coordinated the nominal amounts, trading limits and choice of trading venue for these transactions. The accused’s intention with this order behaviour was to deliberately create exchange trades in which he simultaneously traded against himself as buyer and seller. One trade made by the accused, which was worth €33,680, amounted in otherwise illiquid trading to 100% of the daily turnover in the instruments. However, the transactions did not result in any change to his beneficial ownership of the instruments. In addition, the orders feigned a market situation that did not exist in reality.

Punishment: In response to an application by the public prosecutor’s office in Hanover, the Neustadt am Rübenerge Local Court (*Amtsgericht*) imposed a total administrative fine of 50 daily units of €200 per day, reflecting individual fines of 40 and 30 daily units. As a result, the total fine amounted to €10,000.

**3.1.2.2 Insider trading**

**3.1.2.2.1 Developments in 2020**

BaFin continued to pursue its risk-based supervisory approach to insider trading surveillance in 2020. As a result, the figures for the year saw a further decline. BaFin concentrated on highly relevant breaches and therefore launched fewer new investigations year-on-year (see Table 18 and Table 19 on page 90). However, it filed more criminal complaints relating to suspected insider trading. The number of ongoing investigations declined from 58 to 47.

**International cooperation**

International administrative assistance is an indispensable tool in insider trading surveillance. In 2020, BaFin requested administrative assistance from foreign supervisory authorities in 13 cases (previous year: 15 cases) (see Table 20 on page 90). Conversely, BaFin received requests for international assistance in 11 cases. In the previous year, BaFin received 22 requests for assistance.

**Table 18: Insider trading investigations**

Period	New investigations	Investigation results						Ongoing investigations
		Investigations discontinued	Investigations referred to public prosecutors’ offices or BaFin Administrative Fines Division				Total (cases)	
			Public prosecutors’ offices		Administrative Fines Division			
			Cases	Individuals	Cases	Individuals		
2018	71	48	19	63	1	4	20	75
2019	31	38	10	26			10	58
2020	19	13	15	36	2	2	17	47

**Table 19: Completed insider trading proceedings**

Period	Total	Investigations discontinued	Investigations discontinued as part of out-of-court settlements	Final court judgements			Administrative fine proceedings discontinued
				Court rulings	Convictions following summary proceedings	Convictions following full trial	
2018	45	42	2		1		
2019	58	29	17	6		1	5
2020	19	13	3				3

**Table 20: Requests for international administrative assistance in insider trading investigations**

Period	Requests made	Requests received	Total
2018	38	18	56
2019	15	22	37
2020	13	11	24

### 3.1.2.2.2 Selected focus areas for investigations

In 2020, the courts and public prosecutors' offices again informed BaFin about the outcome of insider trading proceedings. Although most of the cases for which BaFin had filed a complaint were discontinued, some accused had to make large payments as part of out-of-court settlements. The largest settlement was €2 million.

#### Gerry Weber International AG

At 1:18 p.m. on 25 January 2019, Gerry Weber International AG published an ad hoc disclosure in which the company announced that the talks with its finance partners had broken down and that application had therefore been made to the competent court, the Bielefeld Local Court (*Amtsgericht*), for an order for temporary debtor-in-possession proceedings under section 270a of the German Insolvency Code (*Insolvenzordnung*).

Trades by four trading participants had been so conspicuous that the suspicion of insider trading arose and BaFin filed a criminal complaint with the public prosecutors in Braunschweig. After extensive investigations had been made and a number of properties searched, the proceedings are to be

discontinued as part of an out-of-court settlement in accordance with section 153a of the Code of Criminal Procedure.

The largest settlement reached as part of these proceedings was €2 million in the case of one of the accused. This was the largest out-of-court settlement in the whole of 2020 for suspected insider trading. Settlements involving payments of between €5,000 and €30,000 were reached in the case of the other three accused.

According to the public prosecutors, the first payments have already been received. If all the payments are received by the relevant deadlines, the proceedings can be finally discontinued in May 2021. If this is not the case, a public prosecution will be brought.

### 3.1.2.3 Ad hoc disclosures and managers' transactions

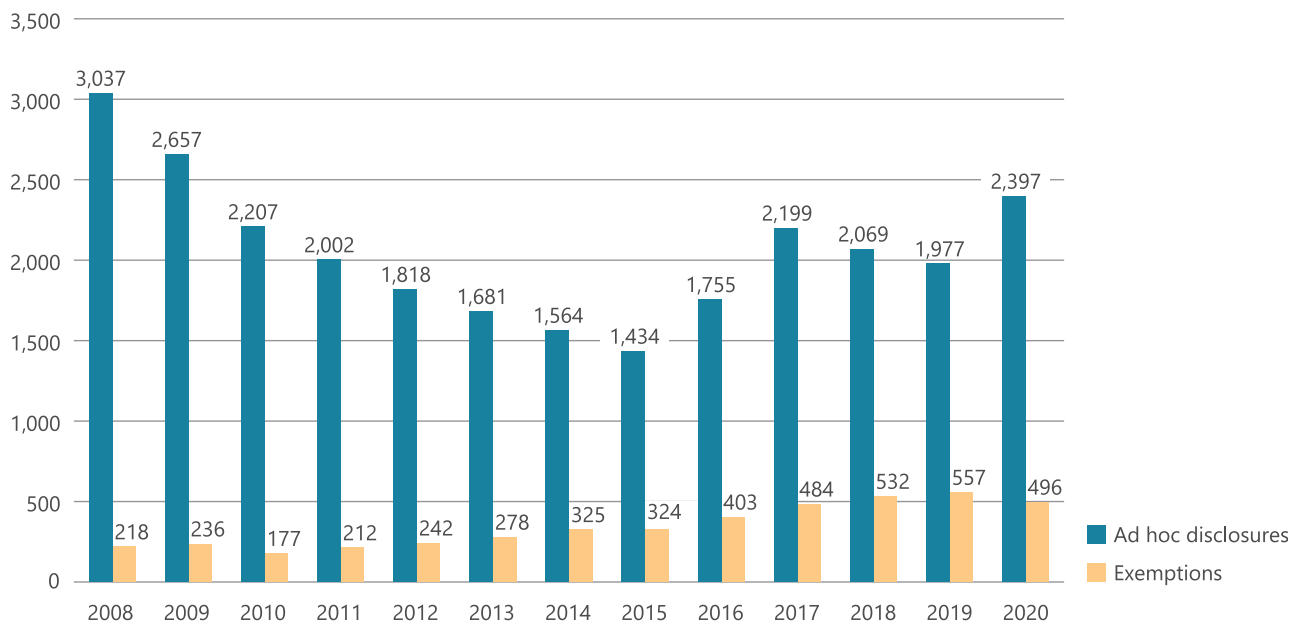
#### 3.1.2.3.1 Ad hoc disclosures

In 2020, issuers published a total of 2,397 ad hoc disclosures (previous year: 1,977 disclosures; see Figure 11 on page 91). In addition, BaFin received 496 delay decisions (previous year: 557 delay decisions). This means there was a sharp increase in the number of ad hoc disclosures year-on-year. The background was the coronavirus pandemic, which led to a relatively large number of ad hoc disclosures in accordance with Article 17 of the Market Abuse Regulation (MAR) having to be published.

In line with this, the number of ad hoc disclosures relating to companies' financial results (2019: 396 disclosures; 2020: 586 disclosures), forecasts (2019: 305 disclosures; 2020: 530 disclosures) and

**Figure 11: Ad hoc disclosures and exemptions**

As at 7 January 2021



dividends (2019: 76 disclosures; 2020: 156 disclosures) saw particularly clear rises. A justified interest in delay as defined in Article 17(4) of the MAR only exists here in very rare cases, which explains the drop in delay notifications. In addition, the number of ad hoc disclosures relating to mergers, acquisitions and contracts, which are often associated with delay decisions, declined significantly (2019: 170 disclosures; 2020: 130 disclosures).

A number of basic questions needed to be addressed in 2020 in relation to how issuers should deal with the effects of the COVID-19 pandemic and resulting ad hoc disclosure obligations. For example, clarification was needed on when a potential change to forecasts resulting from the pandemic constitutes inside information subject to a disclosure requirement. Another question was whether any specific aspects have to be taken into account when assessing whether financial figures constitute inside information. BaFin swiftly made associated questions of interpretation and application available as frequently asked questions (FAQs) on its website.<sup>47</sup>

**Guidelines on ad hoc disclosure requirements and possibilities for delaying disclosure**

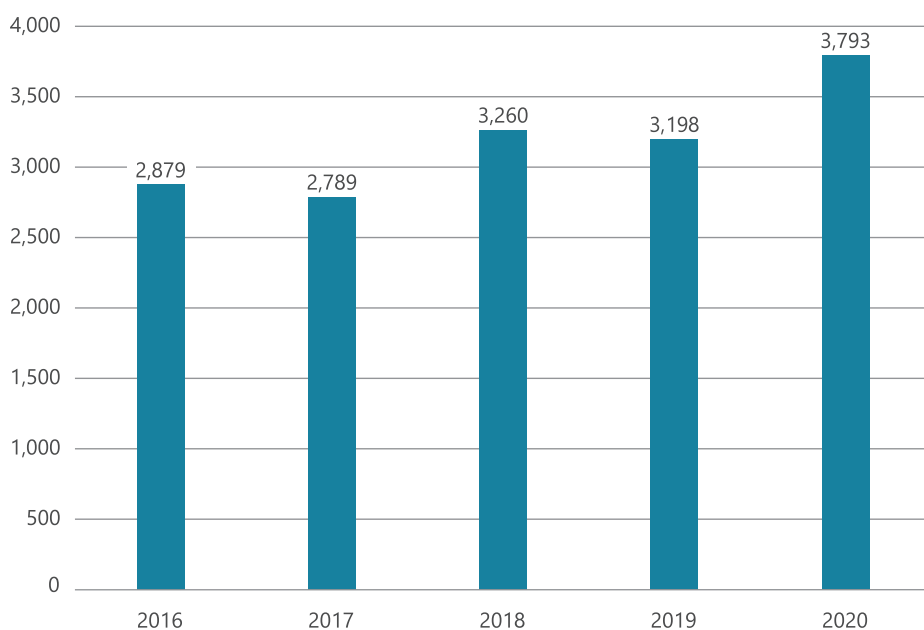
At the end of 2020, BaFin conducted a consultation process for its “Guidelines for determining general criteria for ad hoc disclosure obligations and options to delay disclosure for credit and financial institutions in relation to prudential action and resolution” as an annex to its Issuer Guidelines, Module C, Requirements based on the Market Abuse Regulation (MAR). The draft guidelines supplement the Issuer Guidelines and are addressed solely to credit and financial institutions. They are designed to help institutions identify potential inside information and deal with it appropriately in everything from organisational issues down to recovery and resolution.

**3.1.2.3.2 Managers’ transactions**

In 2020, BaFin received 3,793 managers’ transactions notifications (see Figure 12 on page 92). Background: Managers – e.g. members of management or supervisory boards – of issuers that have been admitted to a regulated market, multilateral trading facility (MTF) or organised trading facility (OTF) must notify BaFin of any transactions in that issuer’s shares or debt instruments or in associated derivatives or other associated financial instruments. The same applies to persons closely associated with them.

<sup>47</sup> www.bafin.de/dok/13849780, see also chapter I.1 for the measures taken by BaFin in relation to the coronavirus pandemic.

**Figure 12: Managers' transactions notifications**



### 3.1.3 Monitoring of short selling

#### 3.1.3.1. Prohibitions

The EU Short Selling Regulation bans uncovered short selling of shares and certain sovereign debt instruments. This also applies to entering into credit default swaps (CDSs) relating to sovereign issuers other than for hedging purposes and to the creation of such CDSs.

BaFin investigated 135 potential cases in 2020, which had been triggered by suspicious transaction and order reports or evidence available to BaFin itself. Table 21 on page 93 shows the results of the investigations. Most of the investigations discontinued by BaFin related to voluntary self-reports of minor infringements caused by human error such as customer misunderstandings during order placement.

#### 3.1.3.2 Transparency requirements and notifications by market makers

Holders of net short positions or third parties engaged by the holder notify BaFin of these positions using the MVP Portal, BaFin's reporting and publishing platform. At the end of 2020, 1,534 undertakings and 2 private individuals had registered for this procedure. As in previous years, most of the parties subject to the notification requirement came from the United States and the United Kingdom. Table 22 on page 93 provides a summary of the notifications received

by BaFin and of the net short positions published in the Federal Gazette (*Bundesanzeiger*). The number of disclosures rose significantly at the start of the coronavirus crisis<sup>48</sup> in 2020 due to a decision<sup>49</sup> by the European Securities and Markets Authority (ESMA) on 16 March 2020, which required net short positions in all shares admitted to trading on an EU regulated market to be reported as from a threshold of 0.1% of the issued share capital. ESMA extended the measure as from 17 June 2020<sup>50</sup>, 18 September 2020<sup>51</sup> and again as from 16 December 2020<sup>52</sup> by three months in each case.

Table 23 on page 93 provides a summary of the investigations launched into breaches of the transparency requirements. The number of notifications of net short positions submitted is high, and that of investigations launched seems low by comparison. This is because BaFin pursues a risk-based approach in the

48 See also chapter I.1.

49 ESMA Decision of 16 March 2020, [https://www.esma.europa.eu/sites/default/files/library/esma70-155-9546\\_esma\\_decision\\_-\\_article\\_28\\_ssr\\_reporting\\_threshold.pdf](https://www.esma.europa.eu/sites/default/files/library/esma70-155-9546_esma_decision_-_article_28_ssr_reporting_threshold.pdf).

50 ESMA Decision of 10 March 2020, [https://www.esma.europa.eu/sites/default/files/library/esma\\_decision\\_-\\_renewal\\_article\\_28\\_ssr\\_reporting\\_threshold\\_en.pdf](https://www.esma.europa.eu/sites/default/files/library/esma_decision_-_renewal_article_28_ssr_reporting_threshold_en.pdf).

51 ESMA, Decision of 16 September 2020, [https://www.esma.europa.eu/sites/default/files/library/esma70-155-11072\\_-\\_decision\\_-\\_renewal\\_article\\_28\\_ssr\\_reporting\\_threshold\\_-\\_september\\_2020.pdf](https://www.esma.europa.eu/sites/default/files/library/esma70-155-11072_-_decision_-_renewal_article_28_ssr_reporting_threshold_-_september_2020.pdf).

52 ESMA, Decision of 16 December 2020, [https://www.esma.europa.eu/system/files\\_force/library/decision\\_renewal\\_of\\_16\\_december\\_2020\\_on\\_art.28\\_ssr\\_reporting\\_threshold\\_de\\_0.pdf?download=1](https://www.esma.europa.eu/system/files_force/library/decision_renewal_of_16_december_2020_on_art.28_ssr_reporting_threshold_de_0.pdf?download=1).

**Table 21: Investigations of prohibited short sales**

Period	New investigations	Investigation results			Investigations	Ongoing investigations**
		Investigations discontinued	Referred to another EU authority*	Referred to Administrative Fines Division		
2018	55	53	44	0	71	18
2019	72	47	7	0	97	43
2020	106	81	14	0	135	54

\* Referred to the competent authority in accordance with Article 35 of the EU Short Selling Regulation.

\*\* As at 31 December.

**Table 22: Notifications and disclosures of net short positions**

Period	Notifications regarding shares	Disclosure required in the Federal Gazette	Number of shares affected	Notifications regarding debt securities	
				issued by the federal government	issued by the federal states
2018	16,417	4,764	489	124	0
2019	14,976	4,656	371	93	2
2020	24,981	4,604	558	70	0

Notifications broken down by indices in 2020*			
DAX	MDAX	SDAX	TecDAX
4,012	11,258	5,142	3,562

\* The sum of the individual figures is higher than the total number of notifications because some issuers are represented in two indices.

**Table 23: Investigations of transparency requirements**

Period	New investigations	Investigation results		Investigations	Ongoing investigations*
		Investigations discontinued	Referred to Administrative Fines Division		
2018	18	17	0	23	7
2019	4	3	0	11	8
2020	5	1	1	13	11

\* As at 31 December.

case of these investigations as well. It focuses on highly relevant cases, both when monitoring the notifications and in the resulting investigations.

Table 24 on page 94 provides a summary of market makers and primary dealers that made use of the exemptions from the prohibitions on short selling and from the transparency requirements in 2020.

**Table 24: Notifications by market makers and primary dealers in 2020**

	Market makers	Primary dealers
Total number of companies	54	35
of which based in Germany	48	9
of which based abroad	6*	26**
Total number of notifications in 2020	2,027	4
Total number of notifications since September 2012	11,841	44

\* Non-EU third country.

\*\* Domiciled outside Germany.

### 3.1.4 Supervision of financial market infrastructures: central counterparties and central securities depositories

#### 3.1.4.1 Authorisation procedure for central securities depositories under Article 16 of the CSDR

In January 2020, BaFin authorised Clearstream Banking AG under Article 16 of the EU Central Securities Depositories Regulation (CSDR) to perform core services and non-banking type ancillary services. As a result, Clearstream Banking AG is permitted to operate a securities settlement system and perform central account management and notary services in relation to initial securities issues, among other things.

Delegated Regulation (EU) 2018/1229 sets out in more detail the settlement requirements that depositories have to meet under the CSDR. In view of the COVID-19 pandemic, ESMA recommended to the European Commission that the Delegated Regulation should not take effect until February 2022. The consent of the European Parliament and Council to this was still outstanding as of the end of 2020.

#### 3.1.4.2 CCP Brexit

On 28 September 2020, ESMA declared that it would recognise the British central counterparties (CCPs) ICE Clear Europe Limited, LCH Limited and LME Clear Limited as third-country CCPs in accordance with the provisions of the European Market Infrastructure Regulation (EMIR) with effect from 1 January 2021. ESMA took this decision to prevent the end of the transitional period that had been agreed between the United Kingdom and the European Union in connection with Brexit<sup>53</sup> and that expired on 31 December 2020, from impeding European market participants' access to clearing services offered by British CCPs. An abrupt restriction of access to British CCPs would have been problematic from a financial stability perspective, among other things. The European Commission stated that it was in favour of successively transferring trading to the EU in the period up to the expiration of the recognition on 30 June 2022. During this period, ESMA will also examine whether one of the CCPs in the UK is of such systemic importance for the EU that its clearing services should not be offered by a CCP outside the EU. The Bank of England's Temporary Recognition Regime is designed to allow CCPs from the EU to perform their services in the United Kingdom until at least 2023.

#### 3.1.5 Supervision of OTC derivative transactions and compliance with position limits

EMIR requires financial and non-financial counterparties with volumes of OTC derivatives in excess of certain thresholds to 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 58 requests to this effect in 2020. Details are listed in Table 25 on page 95.

In parallel, companies that have been subject to the clearing obligation for OTC derivatives since 2016 can request an exemption from this obligation for intragroup transactions. 11 such requests were submitted in 2020, compared with 19 requests in the previous year.

<sup>53</sup> See also chapter I.3.

**Table 25: Notifications and requests**

	Notifications/ requests 2019	Notifications/ requests 2020
Total number of notifications/requests	72	58
One counterparty domiciled in another EU member state (notification)	31	19
One counterparty domiciled in a third country (request)	41	39

**Market surveillance by BaFin**

The clearing and collateralisation requirements for OTC derivatives are subject to market surveillance by BaFin. In the case of financial counterparties – such as insurers, securities services providers, banks and funds – BaFin follows a risk-based approach. Where the volume of derivatives entered into in the case of non-financial counterparties exceeds certain thresholds, these counterparties must demonstrate under section 32 of the Securities Trading Act that they comply with the material EMIR requirements. To do this, they must submit a certificate to this effect that has been issued by an auditor.

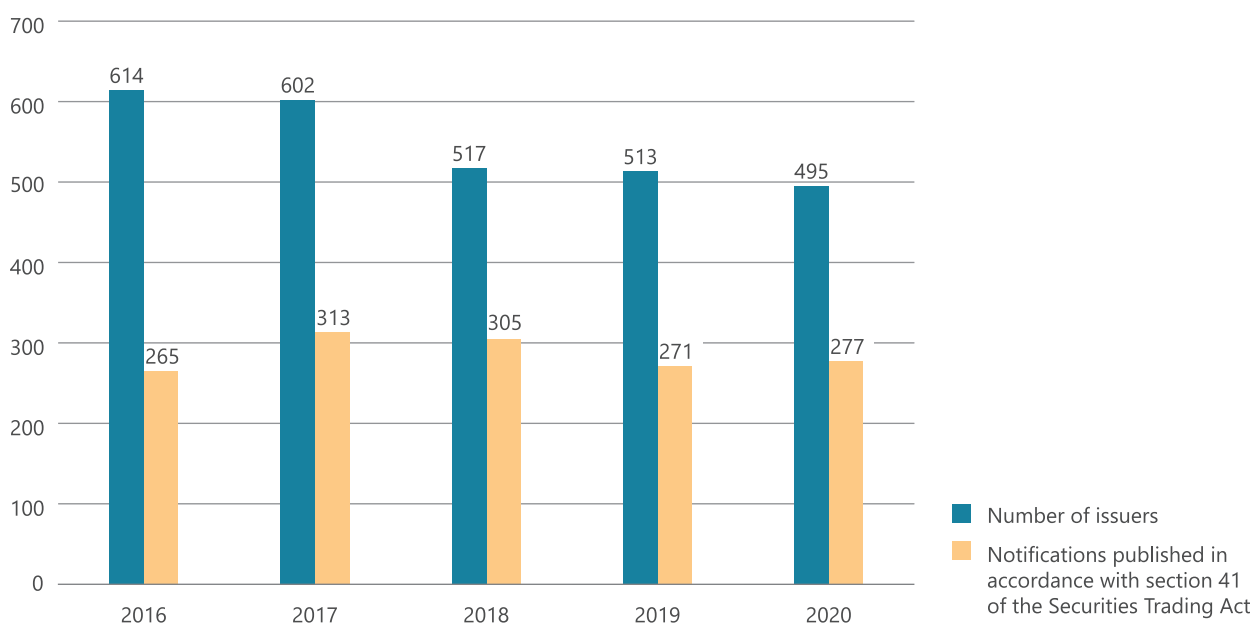
**Position limits for commodities derivatives**

Since 2018, the Markets in Financial Instruments Directive II (MiFID II) has required supervisory authorities to set position limits for commodities derivatives, and trading venues and investment firms to submit corresponding position reports to them. In 2020, BaFin imposed four individual position limits in commodity derivatives by way of general administrative acts. These related to modifications to existing position limits relating to electricity as the underlying. In 2019, 24 general administrative acts had been issued. The background to the modifications was a change in the methodology used to calculate the number of open contract positions underlying the position limits as part of a pan-European harmonisation effort by ESMA.

**One sustained breach of the reporting requirements**

In 2020, one institution domiciled in Denmark that was covered by the reporting requirement failed to comply with it on a sustained basis. BaFin is working on the case together with the Danish supervisory authority Finanstilsynet. In addition, BaFin found in six cases that position limits had been exceeded. These mainly related to energy contracts. When BaFin intervened, the providers rectified the exceedances at short notice. In addition, BaFin received a total of 35 requests for hedging exemptions in 2020.

**Figure 13: Number of issuers admitted to an organised market**



### 3.1.6 Voting rights

The number of issuers whose shares were admitted for trading on an organised market declined to 495 in 2020 (previous year: 513 issuers, see Figure 13 on page 95). These undertakings published a total of 277 notifications (previous year: 271 notifications) on changes in the total number of their voting rights (section 41 of the Securities Trading Act).

The total number of notifications of changes in the percentage of voting rights rose from 3,840 in 2019 to 4,482 in 2020 (see Figure 14). The percentage breakdown across group notifications, voluntary group notifications (voluntary notifications on existing shareholdings by a group when thresholds are reached or crossed at the level of a subsidiary) and other disclosures remained constant year-on-year.

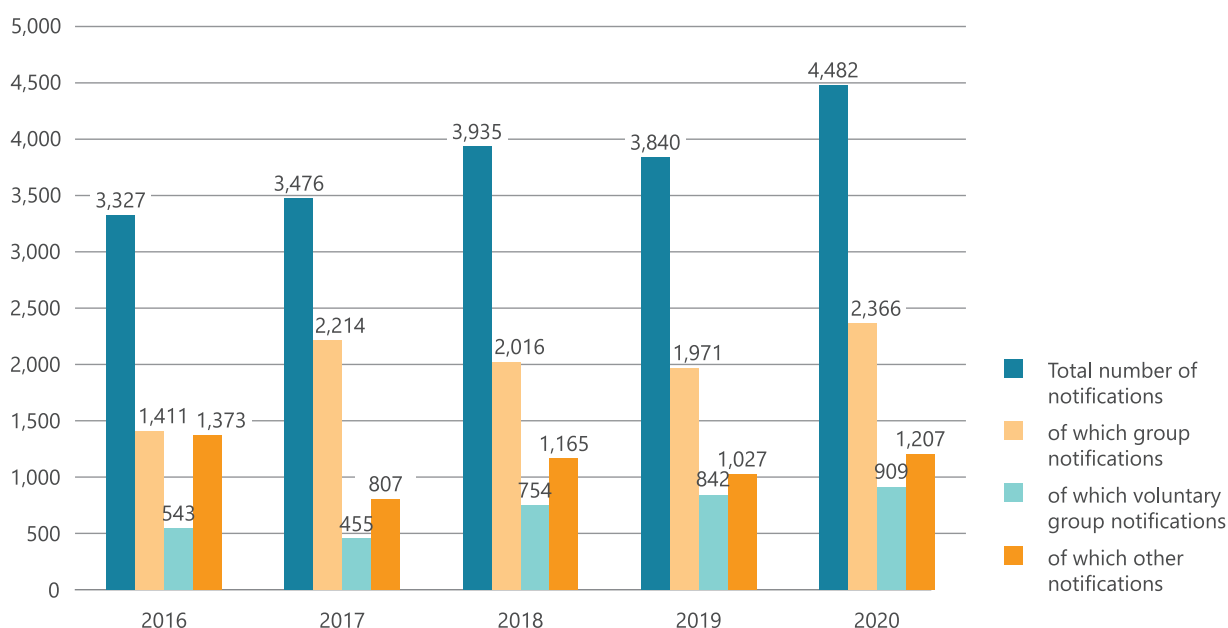
A majority (2,944) of the notifications (previous year: 2,410 notifications) related to changes in voting rights (sections 33 and 34 of the Securities Trading Act). This was followed by 968 (previous year: 886) notifications on existing shareholdings, 295 (previous year: 270) notifications relating to changes in holdings of financial instruments (section 38 of the Securities Trading Act) and 369 (previous year: 319) notifications relating to aggregated voting rights and holdings of financial instruments (section 39 of the Securities Trading Act).

## 3.2 Prospectuses

### 3.2.1 Recovery package

European lawmakers are planning to introduce limited-term changes to the EU Prospectus Regulation to provide temporary relief in the area of securities prospectus law and hence to support the economy during the difficult period caused by the COVID-19 pandemic. One key change is a new, radically shortened prospectus format for equities issues by issuers who have already been admitted to trading on a regulated market or an EU growth market for at least 18 months. This Recovery Prospectus is to be limited to a maximum of 30 pages – plus a summary of a maximum of two pages. The prospectus should also contain information on the specific impact of the COVID-19 pandemic on the issuer and whether the issuer is receiving government support. In addition, the competent authorities should examine the prospectus within 7 instead of 10 working days, as was previously the case. What is more, existing exceptions for non-equity securities that can be issued by a credit institution under certain circumstances are to be extended temporarily. The plan here is to increase the relevant threshold from €75 million to €150 million.

**Figure 14: Total number of voting rights notifications**





### 3.2.2 Securities prospectuses

The number of prospectuses approved rose slightly by 3.4%, notwithstanding the COVID-19 pandemic. The legal basis is the new EU Prospectus Regulation,<sup>54</sup> which entered into force in mid-2019.

#### Initial public offerings

The volatility in initial public offerings (IPOs) for the regulated market that was seen last year continued: 6 of the 11 prospectuses submitted were withdrawn in the course of the process, in many cases shortly before approval was granted. One of the reasons in most cases was that the issuers considered the market situation to be too uncertain in view of the coronavirus pandemic. Overall, they also saw a greater need to consult with BaFin.

#### Refusals of approval and more referrals

Outside of the regulated market, BaFin refused approval for prospectuses under the EU Prospectus Regulation for the first time and referred almost twice the number of suspicious cases to the Consumer Protection Division VBS 7 compared with 2019. The latter then initiated a greater number of product intervention procedures than in the previous year.

#### More securities information sheets

BaFin also approved a significantly larger number of securities information sheets in 2020. Total issuance of securities for which information sheets were produced also rose by 146% in 2020 to €293 million.

#### Security token offerings

The trend towards tokens representing rights similar to securities (security token offerings or STOs) is continuing. However, BaFin also refused to approve the prospectus for a public token offering for the first time in 2020.

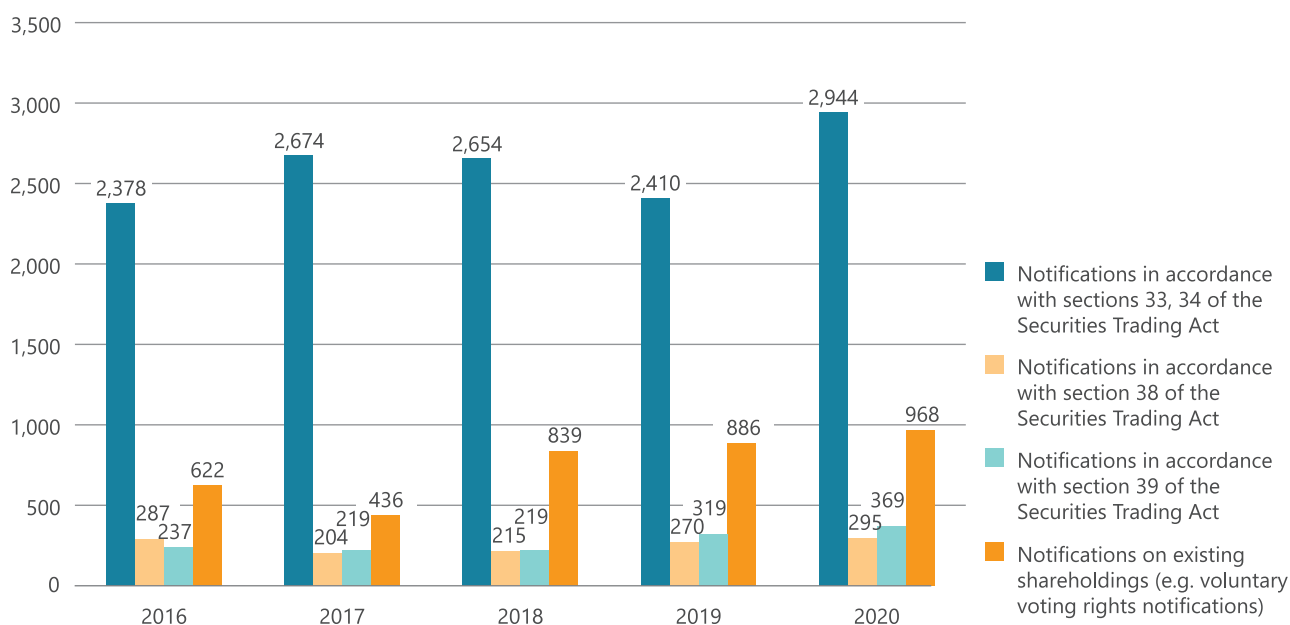
**Table 26: Number of approvals in 2020 and 2019**

Product	2020	2019
Prospectuses (of which IPOs)	301 (5)	291 (4)
Registration documents (of which URDs)*	32 (1)	41 (0)
Securities information sheets approved	95	55
STO prospectuses (securities information sheets)	3 (23)	3 (2)
Withdrawn (of which IPOs) (of which securities information sheets)	53 (6) (26)	52 (10) (13)
Approval refused (of which securities information sheets)	3 (1)	0 (0)

\* "URD" stands for "Universal Registration Document".

<sup>54</sup> See BaFin's 2019 Annual Report, page 103.

**Figure 15: Breakdown of voting rights notifications by notification criterion**



### 3.2.3 Non-securities investment prospectuses

In 2020, BaFin received a total of 51 non-securities investment prospectuses for examination (see Figure 16). For market-related reasons, this represented another year-on-year decrease: in 2019, 55 prospectuses were submitted. However, the drop was lower than in previous years. Among other things, this can be attributed to market reaction to the amended requirements of the German Renewable Energy Sources Act (*Erneuerbare-Energien-Gesetz*). The fact that the “wind power” category (15 submissions) has replaced “other” as the largest target investment group (see Figure 17 on page 99) supports this interpretation. Examples of projects falling under the general “other” category include tidal power plants and energy storage media. Non-securities investments taking the form of limited partnership interests (see Figure 18 on page 99) topped the list of type of participation in 2020 with 15 submissions.

BaFin approved 44 non-securities investment prospectuses (previous year: 35 prospectuses). A total of eight processes were discontinued in 2020 because the offerors withdrew their applications. BaFin did not refuse to approve any prospectuses in the year under review.

#### Supplements to non-securities investment prospectuses

In 2020, BaFin received a total of 10 applications for the approval of supplements under the German Capital Investment Act (*Vermögensanlagengesetz*), a decrease compared with the 18 applications received in the previous year. 10 supplements were approved (previous year: 21 applications). The obligation to submit

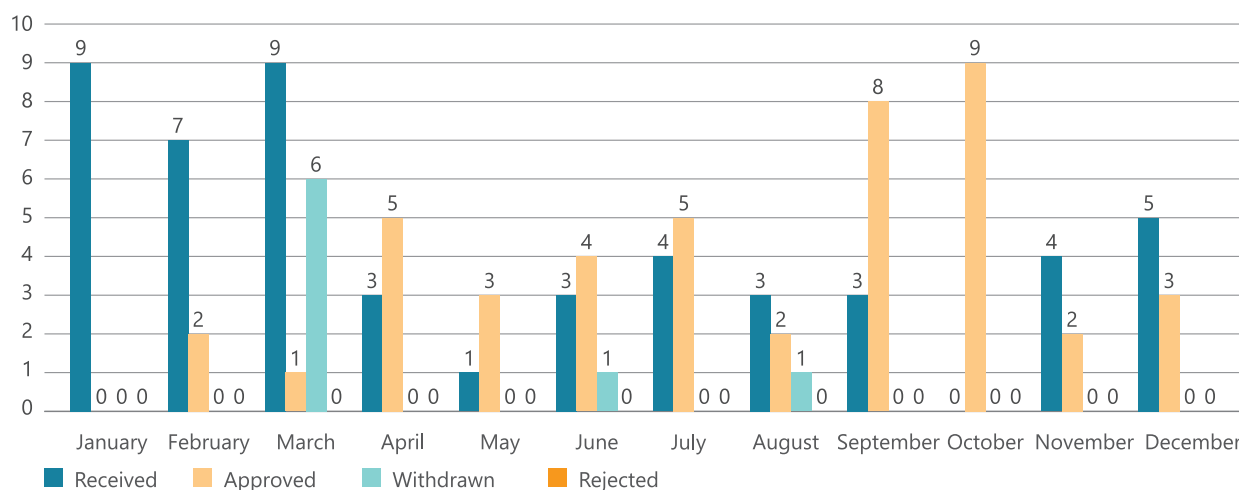
a supplement arises, for example, when the issuer publishes a new set of annual financial statements. If in this case the issuer does not provide the required supplement to the prospectus, the latter automatically becomes invalid. In 2020, BaFin compared the published annual financial statements with the supplements submitted in order to check that all issuers had complied with this obligation. In one case this had not happened and BaFin was forced to take action.

#### Capital investment information sheets without a prospectus

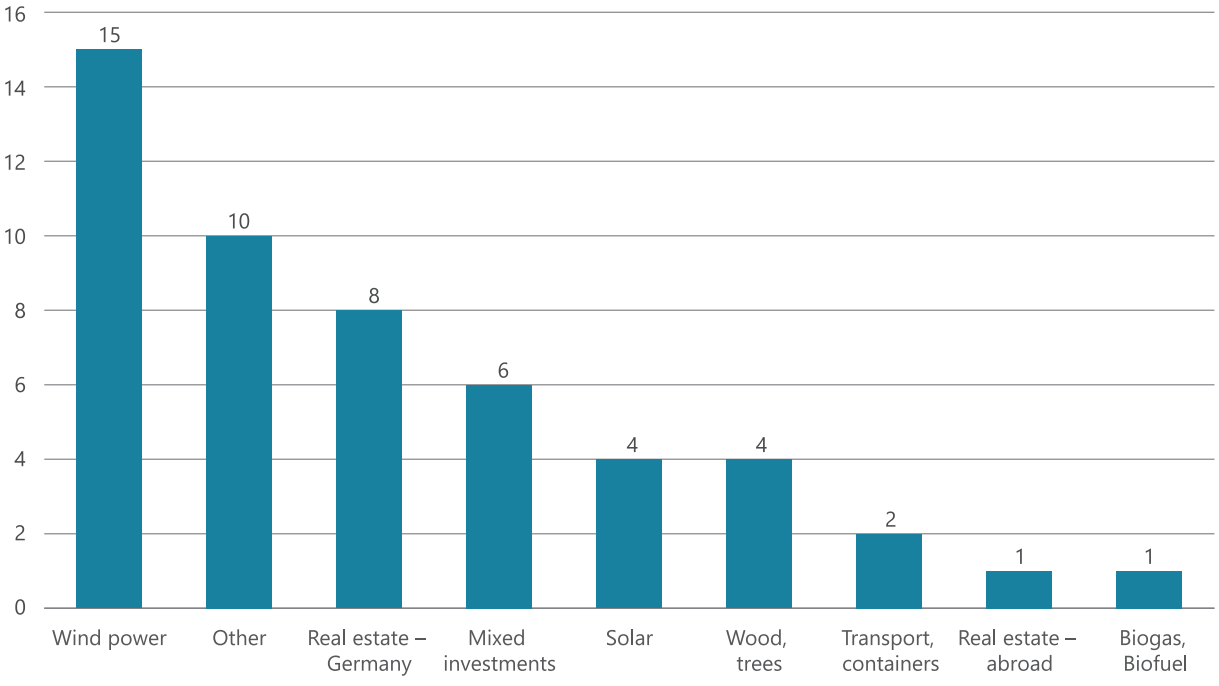
The rising trend in the number of capital investment information sheets without a prospectus as part of crowdfunding processes continued, with 678 documents being received in the year under review (previous year: 587 documents received). BaFin approved the publication of 520 capital investment information sheets without a prospectus. Another 41 such applications were withdrawn in the same period.

Real estate in Germany accounted for the most capital investment information sheets without a prospectus in 2020, followed by the “other” category (see Figure 19 on page 100). The “other” target investment category, which BaFin uses in the absence of another more suitable category, often relates to investments in a company’s normal business activity. The companies’ business purposes vary extremely widely, ranging from fish farming and drinking water plants down to a variety of e-vehicles. Of the possible types of participation, qualified subordinated loans were once again the clear leader, with 508 submissions (see Figure 20 on page 101).

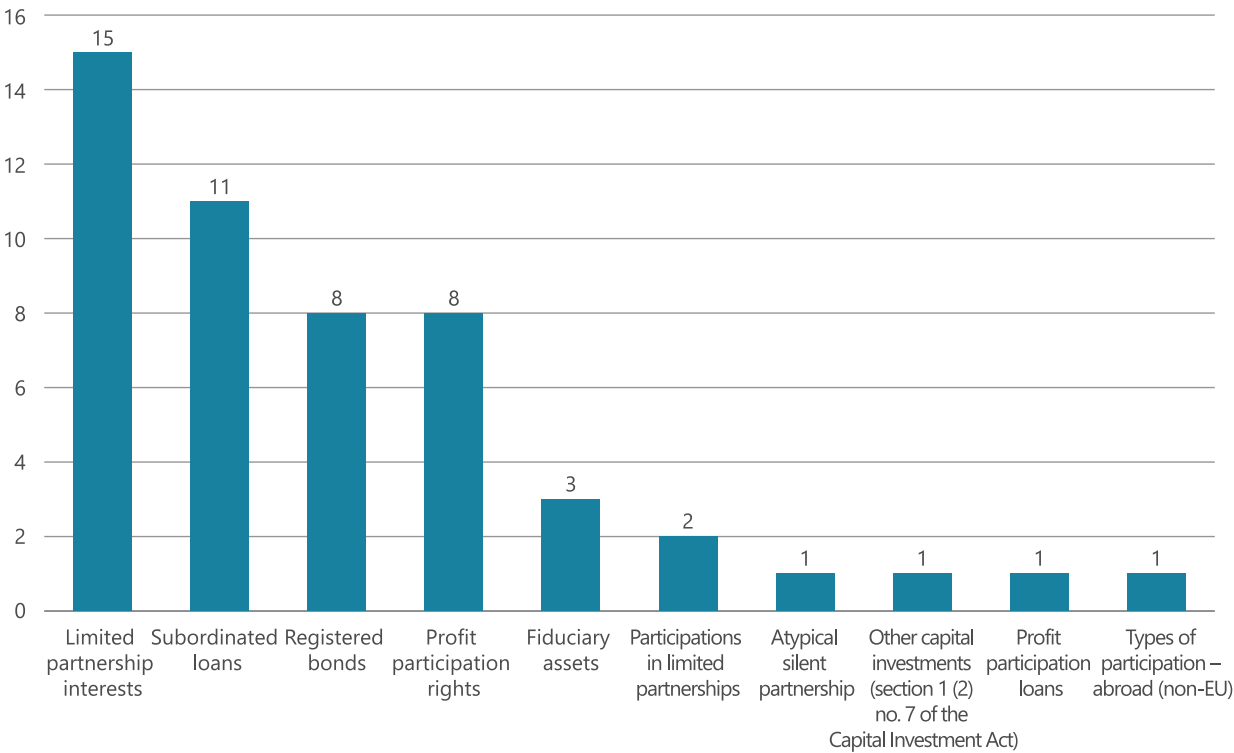
Figure 16: Prospectuses received, approved, withdrawn and rejected



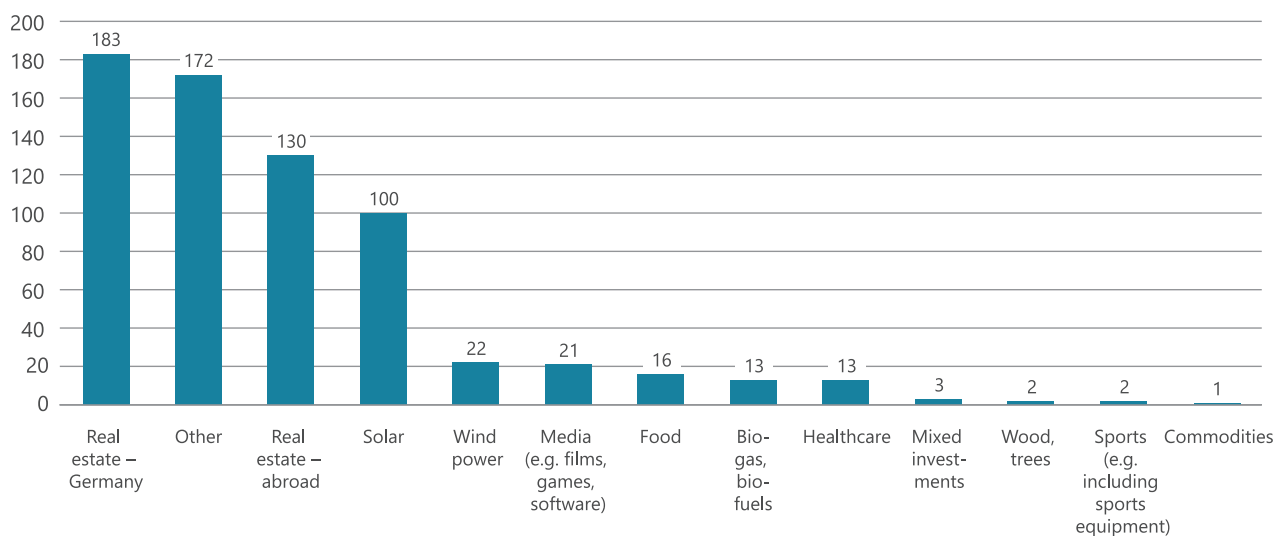
**Figure 17: Prospectuses by target investment (in order of number of prospectuses received)**



**Figure 18: Prospectuses by type of participation (in order of number of prospectuses received)**



**Figure 19: Capital investment information sheets without prospectus by target investment\***



\* In order of the number of capital investment information sheets without a prospectus received.

### 3.2.4 Market supervision of offers of securities and capital investments to the public

In 2020, BaFin conducted a total of 218 market surveillance proceedings for possible violations of the Capital Investment Act, the German Securities Prospectus Act (*Wertpapierprospektgesetz*) and the EU Prospectus Regulation (previous year: 151 proceedings). The total number of proceedings initiated in 2020 as a result was 160 (previous year: 144 proceedings). The clear increase in this number is due on the one hand to increased market surveillance by BaFin and on the other to a greater number of tip-offs from the public.

#### Prohibitions

BaFin's Division for Supervision of Non-Securities Investment Products and Offers of Securities prohibited 3 offers of capital investments to the public in 2020 (previous year: 5 cases) and 10 public offers of securities (previous year: 8 prohibitions) for breaching the requirement to draw up a prospectus/capital investment information sheet without a prospectus. In the case of non-securities investments, the prohibitions mainly related to direct investments. The investments in securities primarily related to share offers. Two of BaFin's prohibitions under the Capital Investment Act and one under the Securities Prospectus Act were confirmed in full by the courts.

#### Information published on BaFin's website

The rulings in the above-mentioned cases also confirmed in full the announcements made by BaFin about them. All in all, BaFin published 20 cases of

irregularities and the measures it took on its website (previous year: 20 cases). The announcements generated keen interest among the public, and particularly in Internet forums. This is to be welcomed from a consumer protection perspective.

#### Special audit of accounting

In the year under review, BaFin had concrete indications for the first time of a breach of accounting standards. It therefore ordered a special audit under the Capital Investment Act.

#### Marketing violations

10 out of the total of 33 proceedings relating to marketing violations (previous year: 21 proceedings) related to violations of the Securities Prospectus Act.

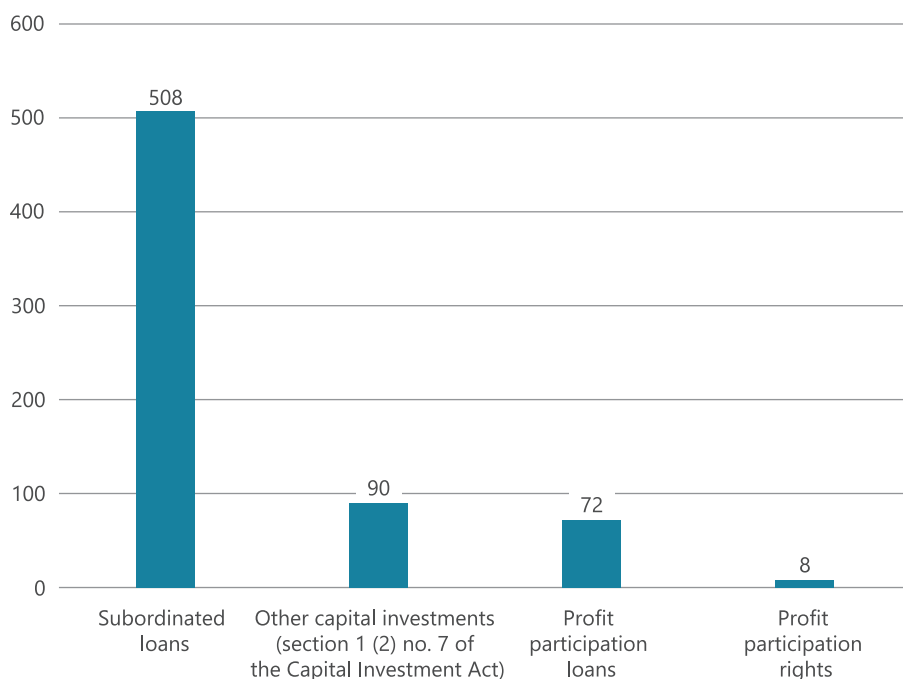
### 3.3 Takeovers

BaFin's Securities Supervision monitors offers to the public to acquire securities admitted to trading on a regulated market. It examines the offer documents for completeness and evident contraventions of the German Securities Acquisition and Takeover Act (*Wertpapiererwerbs- und Übernahmegesetz*). If necessary, BaFin can prohibit an offer (see Figure 21 on page 101).

#### Mandatory offer to shareholders of Travel24.com AG

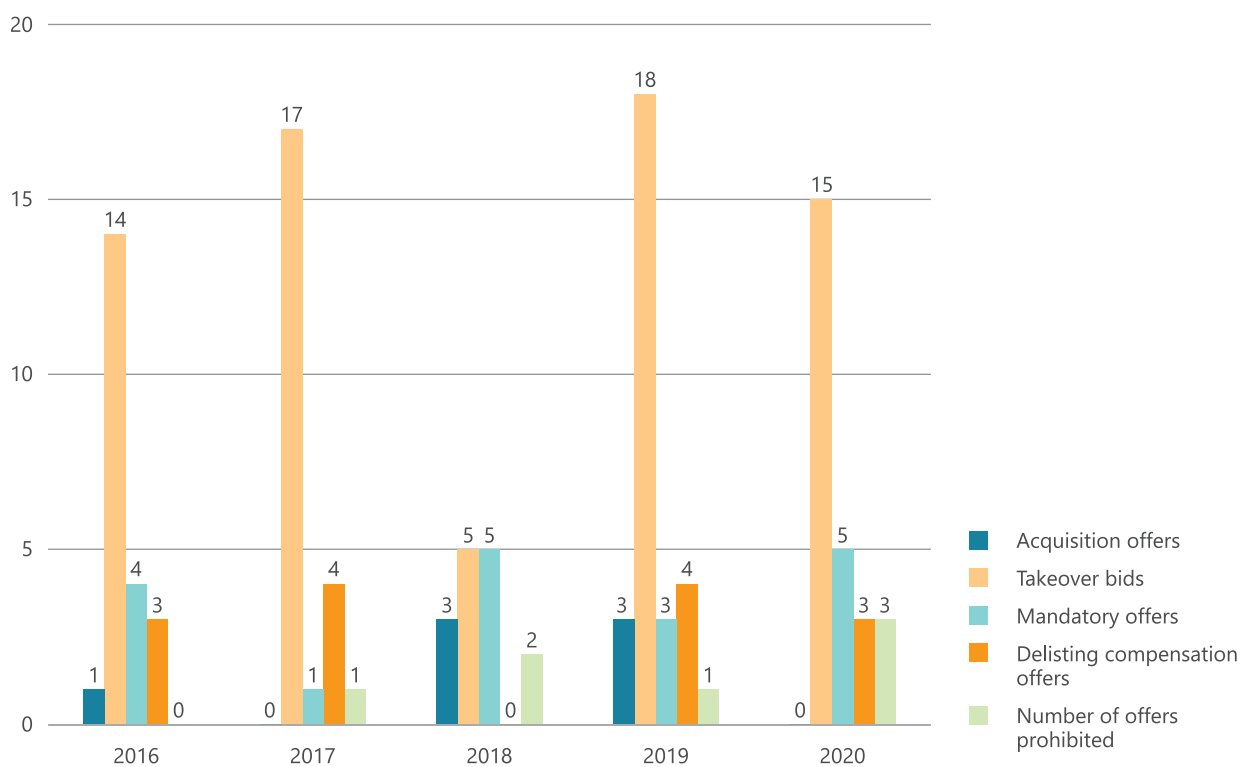
Particularly relevant from a supervisory law perspective was the joint mandatory offer made on 25 November 2020 by VICUS Group AG and three natural persons, as a bidding consortium, to the shareholders of Travel24.com AG. This mandatory offer

**Figure 20: Capital investment information sheets without prospectus by type of participation\***



\* In order of the number of capital investment information sheets without a prospectus received.

**Figure 21: "Offer procedures"**



ended proceedings for non-compliance with statutory provisions stretching back several years in the course of which BaFin had issued a number of requests for information and the submission of documentation. In addition, BaFin had threatened coercive fines of more than €350,000 and ultimately imposed them in the amount of €150,000. Both an application for exemption by VICUS Group AG and its objection to the enforcement of the mandatory offer required by BaFin were unsuccessful.

One of the reasons for requiring the mandatory offer was that the bidders had obtained control over Travel24.com AG for the first time on 28 September 2017 by way of a power of attorney for the general meeting. One of the bidders had previously acquired shares of Travel24.com AG at a price of €5.69 per share. Therefore, in line with the rulings of the Federal Court of Justice,<sup>55</sup> this was the minimum price that had to be used even though the price of Travel24.com AG's shares had fallen in the meantime to as low as €1.21 per share. Three years' interest was also payable in addition to the minimum consideration, since the bidders had failed to discharge their obligations under takeover law within the prescribed period. As a result, the bidders had to offer the Travel24.com AG shareholders a purchase price of €6.41 per share. This price exceeded all the highest prices for the stock in the five years preceding the publication of the mandatory offer.

#### **Prohibition of takeover bid by Heidelberger Beteiligungsholding AG**

On 6 March 2020, BaFin prohibited the takeover bid made by Heidelberger Beteiligungsholding AG to the shareholders of Biofrontera AG. Heidelberger Beteiligungsholding AG proposed not to pay any cash consideration for the shares of Biofrontera AG. Instead, it wanted to grant the latter's shareholders one share in Heidelberger Beteiligungsholding AG for every 17 shares in Biofrontera AG. However, shares offered as consideration in an exchange offer must not only be admitted to trading on a regulated market but must also be "liquid" (section 31 (2) sentence 1 of the Securities Acquisition and Takeover Act). No definition of "liquid" from a takeover law perspective is given in the act.

The primary purpose of the provision is to enable the shareholders of a target company who accept a takeover bid to resell the shares offered as compensation in the exchange offer, and more specifically on acceptable terms and in a timely manner via the stock exchange

in exchange for payment in euros. However, stock exchange trading of the shares in Heidelberger Beteiligungsholding AG had only been marginal in the past. The forecast that BaFin was required to make in accordance with section 31 (2) sentence 1 of the Securities Acquisition and Takeover Act revealed that liquid share trading was unlikely to develop soon even following settlement of the takeover offer. As a result BaFin was obliged to prohibit the takeover bid, since it did not include any lawful consideration. The bidder lodged an appeal against this decision. The competent court – the Frankfurt am Main Higher Regional Court – had not ruled on the case at the end of December 2020.

#### **Exemption procedures**

In certain circumstances, BaFin can exempt a legal entity from the obligation to make an offer that it would otherwise have to fulfil in accordance with the Securities Acquisition and Takeover Act. The lawmakers have provided two alternatives for this: exemption in accordance with section 37 of the Securities Acquisition and Takeover Act and non-consideration of voting rights in accordance with section 36 of the Securities Acquisition and Takeover Act (see Figure 22 on page 103).

#### **Rescue of TUI AG**

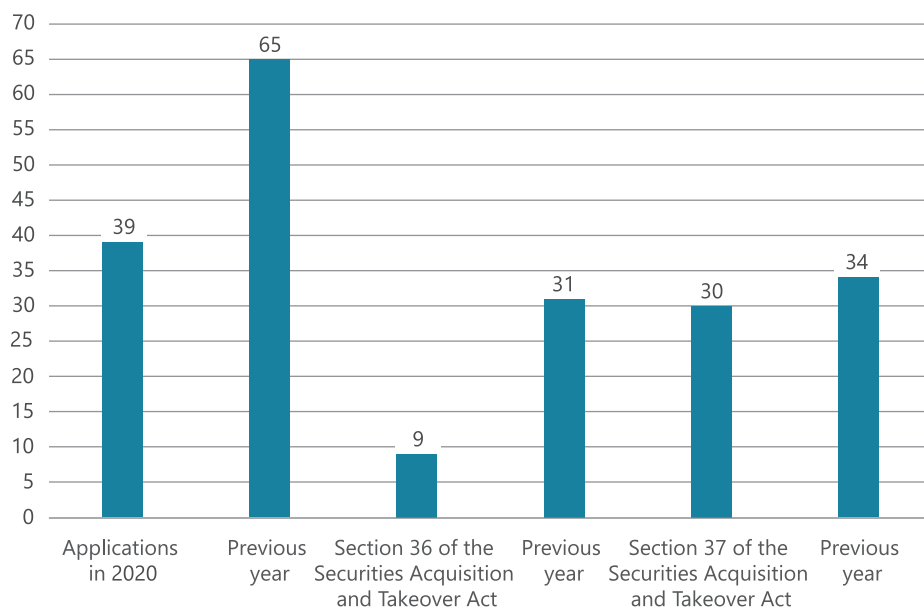
In December 2020, BaFin exempted the former majority shareholder of TUI AG, Unifirm Limited, from its obligations under takeover law resulting from the acquisition of control over the company. The exemption was made due to the rescue of TUI AG by the German Economic Stabilisation Fund (*Wirtschaftsstabilisierungsfonds*). TUI AG had got into economic difficulties as a result of the COVID-19 pandemic. One special feature of this procedure was that BaFin classified the acquisition of control as a side effect of a rescue scenario.

BaFin found that a rescue scenario did in fact exist in view of the statutory framework setting out the preconditions for recapitalisation measures by the Fund. The Fund had agreed with TUI AG on further government support at the beginning of December 2020, but had also made these dependent on Unifirm Limited making a financial contribution. In weighing up its discretionary decision, BaFin relied in particular on the lawmakers' assessments in relation to section 14 (1) and (2) of the German Economic Stabilisation Acceleration Act (*Wirtschaftsstabilisierungsbeschleunigungsgesetz*).

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<sup>55</sup> BGH judgement of 29 July 2014 – II ZR 353/12.

**Figure 22: Exemption procedures**



### 3.4 Financial reporting enforcement

#### Monitoring of financial reporting

As at 1 July 2020, 545 companies from 8 countries were subject to the two-tier enforcement procedure by BaFin and the German Financial Reporting Enforcement Panel (*Deutsche Prüfstelle für Rechnungslegung – FREP*). This compares with a total of 549 companies from 7 countries in 2019. Table 27 shows the enforcement procedures completed by BaFin in 2020.<sup>56</sup>

<sup>56</sup> See chapter I.2 for information on Wirecard.

#### Publication of financial reports

In 2020, BaFin performed approximately 890 examinations (previous year: 915 examinations) to establish whether issuers had published their online annual and half-yearly financial reports on time. In 14 cases (previous year: 12 cases) it found indications of violations, which it pursued further in administrative fine proceedings.

As in the previous year, BaFin continued in 2020 to monitor the publication of notifications intended to provide information on when and where issuers make their financial reports available online. In 17 cases (previous year: 29 cases), issuers with registered offices in Germany failed to draw attention to the publication

**Table 27: Completed enforcement procedures**

	Errors found: yes	Errors found: no	Errors published: yes	Errors published: no
Company accepts FREP's* findings	8	n/a**	8	0
Company does not accept FREP's findings	1	2	1	0
Company refuses to cooperate with FREP	0	1	0	0
BaFin has material doubts as to the accuracy of the FREP's findings/procedure	0	0	0	0
BaFin has assumed responsibility for the examination (banks, insurance undertakings)	0	0	0	0
<b>Total</b>	<b>9</b>	<b>3</b>	<b>9</b>	<b>0</b>

\* "FREP" stands for the "Financial Reporting Enforcement Panel".

\*\* n/a: not applicable.

of financial reports. All 17 of these cases related to annual financial reports rather than half-yearly financial reports. Not only had the issuers failed to draw attention to the publication of annual reports, but they had also failed to publish the annual 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 the 17 cases where the relevant notification had not been published.

BaFin also verified whether the published half-yearly financial reports contained all the minimum components required by law. In one case during the year under review, it found that the responsibility statements (*Bilanzzeit*) were missing. This prompted BaFin to pursue the case in question further in administrative fine proceedings.

BaFin launched a total of 5 administrative procedures to enforce the financial reporting requirements, compared with 10 such procedures in 2019. 16 proceedings were still pending from previous years, and 7 proceedings were concluded by BaFin in 2020. Most of the pending proceedings are at the enforcement stage. BaFin threatened coercive fines in three cases during the year under review. In one case it imposed a coercive fine of up to €172,500 and initiated enforcement measures.

In 2020, BaFin published the measures it had taken in relation to eight companies plus the associated notes in accordance with section 124 of the German Securities Trading Act (*Wertpapierhandelsgesetz*). In the previous year, it published such information on 13 companies.

## 3.5 Supervision of the investment business

### 3.5.1 Asset management companies

In 2020, 20 (previous year: 9) German asset management companies (*Kapitalverwaltungsgesellschaften*) were granted authorisations to manage investment funds, or BaFin extended their existing authorisations. A total of 3 companies surrendered their authorisation, compared with 4 in the previous year. This brought to 143 the number of companies in Germany that were authorised in accordance with the German Investment Code (*Kapitalanlagegesetzbuch*) at the end of 2020 (previous year: 143 companies). In addition, 48 asset management companies registered in accordance with section 44 of the Investment Code; 49 companies had requested registration in 2019. 21 companies surrendered their registration. As a result, the total number of asset management companies registered at the end of 2020 stood at 431 (previous year: 404 companies).

In 12 cases, asset management companies established a branch in another EU member state or offered cross-border services (previous year: 15 cases). Conversely, 37 companies from other EU countries notified BaFin that they had established a branch or started providing cross-border services in Germany (previous year: 126 companies).

### Risk-based supervision

During the year under review, BaFin performed a total of 118 supervisory visits and annual interviews on site, compared with 110 in 2019. In addition, it accompanied 5 financial statement audits and special audits at asset management companies, depositaries and trustees (previous year: 8 audits accompanied).

As in the previous year, the supervisory and annual interviews conducted in 2020 focused in particular on how to deal with negative interest rates and issues around Brexit, such as investments in the United Kingdom. Other core topics included, among other things, sustainable investments, the resolution of real estate funds and the transfer of their assets to the depositary, digitalisation and implementation of the German Supervisory Requirements for IT in Asset Management Companies (*Kapitalverwaltungsaufsichtliche Anforderungen an die IT – KAIT*). The supervisory and annual interviews conducted in 2020 also focused on the COVID-19 pandemic.

### 3.5.2 Investment funds

The German investment market continued to grow in 2020 (see Table 28 on page 105). Both special and retail funds recorded cash inflows (see Table 29 on page 105).

All in all, BaFin approved 164 new retail investment funds in accordance with the Investment Code in the year under review, including 125 undertakings for collective investment in transferable securities (UCITS)<sup>57</sup>, 7 open-ended retail AIFs and 32 closed-ended retail AIFs. In 2019, BaFin had authorised 161 retail investment funds in accordance with the Investment Code, including 126 UCITS, 6 open-ended retail AIFs and 29 closed-ended retail AIFs.

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<sup>57</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.



### 3.5.2.1 Open-ended real estate funds and hedge funds

At the end of 2020, 66 asset management companies were authorised to manage open-ended real estate funds (previous year: 64). BaFin granted approvals to 3 companies in 2020.

A total of 18 asset management companies managed open-ended real estate funds for retail investors as at the end of the year. 41 companies limited their activities to the management of open-ended real estate special funds in 2020. 7 companies did not make use of their authorisations and have not yet established any open-ended real estate funds.

2 open-ended real estate funds for retail investors were issued in the course of 2020 and 1 was liquidated, bringing the total number of these funds to 58 (previous year: 57 funds). The total fund volume for this market segment was €118.27 billion as at the end of the year (previous year: €109.85 billion).

Gross cash inflows into open-ended real estate funds for retail investors amounted to €10.9 billion in the year under review. Gross cash inflows into open-ended real estate special funds amounted to €16.5 billion (previous year: €20.25 billion). Fund assets held by open-ended real estate special funds amounted to €133.6 billion at

the end of 2020, compared with €121.12 billion in the previous year. Clearly even the coronavirus pandemic did not stop net cash inflows in 2020.

As in the previous year, 21 open-ended real estate funds for retail investors were in liquidation at the end of the year under review, after one company had given notice to terminate management of an additional such fund in September 2020. The aggregate fund volume amounted to €1.65 billion (previous year: €1.92 billion). The management rights for all of these funds have already been transferred to the depositaries.

#### Hedge funds

There were 12 hedge funds in Germany at the end of 2020 (previous year: 13 hedge funds). Their total volume under management was €4.5 billion (previous year: €3.98 billion). As in 2019, there were no domestic funds of hedge funds on the German market.

### 3.5.2.2 Foreign investment funds

In 2020, 10,409 EU UCITS were authorised for marketing in Germany (previous year: 10,550 funds). A total of 849 new notifications were received by BaFin from companies wanting to market EU UCITS in Germany, compared with 886 new notifications in 2019. As in previous years, most of the notifications – 443 in total – came from Luxembourg in 2020. In addition, BaFin

**Table 28: Open-ended investment funds**

	2020		2019	
	Number	Assets	Number	Assets
Total	7,214	€2,550.9 billion	6,898	€2,391.4 billion
Retail funds	2,926	€571.9 billion	2,726	€548.3 billion
Special AIFs	4,288	€1,979.0 billion	4,172	€1,843.1 billion

\* Alternative Investment Funds.

**Table 29: Cash flows**

	2020	2019
Aggregate net cash inflows	€116.7 billion	€133.6 billion
Aggregate gross cash inflows	€438.3 billion	€357.1 billion
Gross cash inflows into retail investment funds	€128.8 billion	€106.0 billion
Gross cash inflows into special AIFs	€309.5 billion	€251.1 billion
Aggregate cash outflows	€321.6 billion	€223.5 billion

received 303 notifications from Ireland, 45 from France and 25 from Austria. Marketing of 990 EU UCITS was discontinued.

In addition, 3,075 EU AIFs and 527 foreign AIFs from third countries were authorised to market units or shares in Germany (previous year: 2,715 EU AIFs and 445 foreign AIFs from third countries). Of this number, 2,233 originated in Luxembourg, 41 in the United Kingdom, 289 in Ireland, 146 in the Cayman Islands, 153 in the United States, 232 in France, 108 in the Netherlands and 37 in Switzerland. A total of 997 AIFs (previous year: 847) started marketing in Germany in 2020, of which 745 were from Luxembourg, 47 from the United Kingdom, 53 from Ireland, 41 from the United States and 25 from the Cayman Islands. Conversely, 791 EU AIFs and foreign AIFs ceased marketing, including 253 from Luxembourg, 295 from the United Kingdom and 82 from Ireland.

### 3.6 Administrative fine proceedings

Total administrative fines imposed by BaFin in 2020 amounted to €8.5 million. BaFin initiated 107 new administrative fine proceedings due to infringements of capital markets law<sup>58</sup>, while 517 proceedings were still pending as at the beginning of the year. 292 proceedings were concluded, 172 of them by imposing administrative fines. This translates into a prosecution ratio of approximately 59%. BaFin discontinued a further 120 procedures, 99 of them for discretionary reasons<sup>59</sup> (see Table 30).

58 This includes violations of the Securities Trading Act, the Securities Acquisition and Takeover Act, the Capital Investment Act, the Securities Prospectus Act, Regulation (EU) No 1286/2014 (PRIIPs Regulation), Regulation (EU) No 236/2012 (EU Short Selling Regulation), Regulation (EU) No 600/2014 (MiFIR) and Regulation (EU) No 596/2014 (MAR). See chapter III.7.

59 See chapter III.7.

**Table 30: Administrative fine proceedings – Securities Supervision**

	Proceedings pending at the beginning of 2020	New proceedings initiated in 2020	Proceedings completed by imposing an administrative fine	Highest individual administrative fine imposed (€)	Proceedings discontinued for factual or legal reasons	Proceedings discontinued for discretionary reasons	Proceedings pending at the end of 2020
Reporting requirements	0	0	0	0	0	0	0
Ad hoc disclosures	71	16	9	1,275,000	5	9	64
Managers' transactions	3	6	0	0	1	0	8
Market manipulation	8	0	1	40,000	2	2	3
Notification and publication requirements	249	35	125	744,000	7	47	105
Duties to provide information to securities holders	0	0	0	0	0	0	0
Short selling	4	0	1	24,000	0	3	0
Financial reporting requirements	133	34	33	504,000	1	29	104
Prospectuses	19	0	2	4,900	5	1	11
Company takeovers	16	6	0	0	0	2	20
Conduct of business rules and organisational and transparency requirements	3	1	0	0	0	1	3
Other	11	9	1	7,000	0	5	14



## 4 Consumer protection

### 4.1 Complaints and enquiries

Customers of supervised institutions and undertakings can complain about these to BaFin.

#### 4.1.1 Credit institutions and financial services providers

In 2020, BaFin processed even more submissions relating to credit and financial services institutions than in previous years. Whereas the figure for 2019 totalled 8,525, 2020 saw a total of 9,547 submissions: 138 general queries and 9,409 complaints. 881 complaints were successful. In 22 cases, BaFin issued statements to the Petitions Committee of the Bundestag (the lower house of the German parliament).

**Table 31: Complaints by group of institutions**

Group of institutions	Total number of submissions
Private banks	5,617
Savings banks	997
Public sector banks	618
Cooperative banks	944
Mortgage banks	7
<i>Bausparkassen</i>	265
Financial services providers (e.g. leasing and factoring undertakings)	224
Foreign banks	737

Once again, submissions in 2020 covered the entire range of products and services offered by credit institutions. The main categories of complaint concerned payments processing, lending and the management of current and garnishment protection accounts. The impact of the COVID-19 pandemic<sup>60</sup> could also be felt. For example, older people in particular complained of having difficulty in doing business with the banks, since

<sup>60</sup> See chapter I.1.

branches and local offices were temporarily closed. At the same time, so many customers used direct or online banking that this impacted service or led to delays. Problems in migrating internal IT systems at banks also led to criticism, with customers complaining of disruptions to online banking services and payments systems – in some cases lasting several days.

#### Fees for contactless payments

The COVID-19 pandemic led to greater use being made of contactless payment options, which in turn led to complaints to BaFin. Consumers objected to the fees charged, which they particularly noticed when frequently using their cards, also to pay extremely small amounts. According to the institutions, using the cards should be free of charge. This was indeed the case as far as using the card as a means of payment was concerned. The costs were incurred elsewhere: depending on the account model selected, they arose from fees for individual account movements or for sending the requisite mTANs. All credit institutions have to publish their fees in their schedule of prices and services. Consumers are therefore advised to inspect this.

#### Interest rate adjustment clauses

Another core issue that triggered a large number of complaints was the interest on long-term premium-aided savings agreements (*Prämiensparverträge*) with variable interest payments. Detailed information on this topic is provided in subsection 4.4.

## 4.1.2 Insurance undertakings

In 2020, BaFin handled a total of 8,216 submissions relating to insurance undertakings (previous year: 7,851 submissions). 34.98% (previous year: 37.2%) of these submissions ended in success for the parties making them.

7,969 submissions (previous year: 7,637 submissions) were attributable to the insurance classes mentioned in Table 32 “Submissions received by insurance class since 2015”. This figure included 7,588 complaints, 345 general enquiries and 36 petitions that reached BaFin via the Bundestag or the Federal Ministry of Finance (*Bundesfinanzministerium*).

There are many different reasons why consumers complain to BaFin. The most common causes in 2020 are given in Table 33.

**Table 33: Most frequent reasons for complaints in 2020**

Reason	Number
Claims handling/delays	1,458
Issues relating to coverage	909
Sum insured	811

#### Discretionary bonus, premiums adjustments and COVID-19

In many queries, BaFin was asked to examine the sum insured under life insurance policies. This mainly related to problems with discretionary bonuses. As in previous years, the “permanent right to object” led to queries. In addition, policyholders asked for information on whether and in what amount acquisition and distribution costs would become due again on Riester pension

**Table 32: Submissions received by insurance class since 2015**

Year	Life	Motor	Health	Accident	Liability	Legal expenses	Building/ contents	Other classes	Miscellaneous*	Total
2020	1,723	2,021	1,607	209	389	567	617	836	247	<b>8,216</b>
2019	1,549	1,958	1,420	245	452	776	605	632	214	<b>7,851</b>
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>

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

insurance policies if the state allowance changes during the savings phase but the overall premium remains the same, so that the client's own contribution rises or falls as a result.

Premiums adjustments were one main reason for complaints about private health insurers. These related both to comprehensive health insurance and to private long-term care insurance. A large number of policyholders also complained about decisions on benefits taken by their health insurers.

BaFin received a large number of queries relating to the COVID-19 pandemic in 2020, particularly in the area of property and casualty insurance. A variety of complaints were submitted about delays in processing insurance claims and decisions on benefits. Travel insurance and business shutdown insurance were particularly frequently affected. Among other things, complaints were made that travel insurers refused to pay cancellation costs for trips. Complaints about business shutdown insurance related to insurers refusing to pay out, citing the applicable terms and conditions.

#### 4.1.3 Securities business

In 2020, BaFin received a total of 2,325 complaints relating to securities transactions (previous year: 615 complaints) and 376 written enquiries (previous year: 296 enquiries) from investors.

The main focus was on administration and customer service and delayed or inadequate order execution. A particularly large number of complaints related to switching securities accounts. A large number of customers complained that certain institutions took an unusually long time to transfer them. However, system crashes at individual brokers, which were caused by the market turbulence at the start of the coronavirus crisis and which led to it only being possible to execute orders after a delay, or in some cases not at all, also led to complaints. All in all, investors traded more than ever before in 2020. This is likely to be a further reason why the number of complaints increased.

The number of complaints about undertakings from Cyprus with cross-border activities also rose again in the year under review. They related to transactions involving financial contracts for difference (CFDs).<sup>61</sup> BaFin informed the Cyprus Securities and Exchange Commission (CySEC) – the country's competent supervisory authority

– about the complaints. As the home supervisor, the latter is responsible for taking measures against the undertakings concerned. Customers frequently suffer massive losses with CFDs due to the leverage involved. The leverage limit introduced by BaFin's product intervention measure in July 2019<sup>62</sup> only offers limited protection here, since the risk of loss continues to exist, albeit to a lesser extent. Some investors do not even want this limited protection and have themselves reclassified as professional clients, since the leverage limit does not apply to this group. In addition, many investors are not put off CFD trading by the mandatory risk warning from CFD brokers that more than 80% of investor accounts frequently suffer losses.

#### 4.1.4 Investment and asset management companies

BaFin also received a total of 142 complaints and queries relating to investment and asset management companies in 2020. Among other things, these related to asset management companies' publication requirements and management decisions, and investment fund distribution. The complaints and inquiries relating to open-ended real estate funds mainly related to the liquidation of open-ended real estate funds for retail investors.

BaFin investigated the information provided, obtained statements from the supervised companies where appropriate and explained the legal framework to complainants. Only in a few cases was it necessary for BaFin to take more far-reaching measures.

#### 4.1.5 Consumer helpline

Members of the public can call BaFin's consumer helpline at +49 (0) 800 2 100 500. As in the past, many of them made use of this in 2020: advisers dealt with 23,777 telephone queries (previous year: 20,391 queries) about the financial market, specific consumer protection issues and problems with banks, insurance undertakings or financial services providers. Of these calls, 24.32% related to the insurance sector and 56.01% to the banking sector. 11.99% of calls concerned securities supervision.

Many callers requested information about the different ways of submitting complaints to BaFin. The helpline agents told them about the competent authorities and provided them with information on the status of

61 [www.bafin.de/dok/15223170](http://www.bafin.de/dok/15223170).

62 [www.bafin.de/dok/12770180](http://www.bafin.de/dok/12770180).

ongoing complaint procedures. Many callers also asked for information about possible mediation procedures.

## 4.2 Product interventions

BaFin did not take any product intervention measures in 2020. Nevertheless, it still used its powers to strengthen consumer protection during the year.

### Investigations of financial instruments

For example, BaFin investigated a large double-digit number of financial instruments in the year under review to establish whether they gave rise to significant consumer protection concerns. Analyses were performed, among other things, on bearer bonds, certificates, token-based securities, and subordinated bonds and loans.

Such analyses frequently lead to questions about the issuers, the financial instruments themselves or the issuing procedure. Among other things, BaFin contacted the issuers in order to clarify these questions. In some cases it also used its rights to obtain information, which allow it to oblige anyone to provide information and forward documents. BaFin contacted the issuers whenever the analyses led to significant concerns regarding investor protection. It is legally obliged to do so before planning to take product intervention measures. It must give the issuers concerned an opportunity to state their position.

Investor protection issues in relation to which BaFin contacted the issuers included the following:

- highly complex terms and conditions for products, and overall investment constructs,
- a lack of transparency regarding product design or the product information provided to investors,
- illiquidity, i.e. difficulty in reselling the investment,
- economic difficulties at the product issuer, leading to a danger that they may not be able to meet investors' claims when the investment falls due – and hence in many cases also
- a poor risk-return profile for the financial instruments being offered.

The issuers contacted reacted in a wide variety of ways to BaFin's comments about the financial instruments concerned. Many sought ways to improve investor protection by modifying the financial instrument concerned. For example, they simplified complex terms and conditions for products, or at least explained them better. Alternatively, they abolished contractual clauses that put investors at a disadvantage. Other issuers chose

other ways of addressing BaFin's investor protection concerns. For example, a number restricted their offerings to professional clients: BaFin's investigations normally focus on retail customers.

However, some issuers abandoned the issuing procedure as a whole. Potential reasons for this could have been that their plans would no longer have been economically feasible once they had complied with BaFin's requirements, or would have been too risky for them. From BaFin's point of view, this generally does away with the need for a product intervention measure.

The issuers' readiness to enter into discussion and make compromises is probably also due to the fact that they have to bear the cost of any product intervention measures themselves, and that the latter are also published. BaFin charges a good €12,000 in fees for product intervention measures. In addition, it is obliged to make all such measures public.

All in all, the investor protection concerns voiced by BaFin were resolved in 2020 by the issuers in question either modifying their offerings sufficiently or completely abandoning their plans to issue the instruments. In this way, BaFin's product intervention powers again assisted with collective consumer protection in 2020 without BaFin having to have recourse to prohibitions or restrictions.

## 4.3 Market surveys

### 4.3.1 BaFin participates in global study on consumer financial education

In 2020, BaFin evaluated a survey of more than 1,000 representative adults in Germany that it had commissioned to learn more about their knowledge, behaviour and attitudes to financial issues.<sup>63</sup> Topics such as financial innovations and financial resilience also played a role. BaFin uses such representative surveys to obtain important information and input for its work, and in particular for consumer education.

The survey provided BaFin with the following insights:

- Roughly one-fifth of adults answered all the questions about finance – from compound interest through inflation down to risk diversification – correctly. Men did slightly better than women on their financial knowledge.

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<sup>63</sup> [www.bafin.de/dok/14063038](http://www.bafin.de/dok/14063038) (only available in German).

- When it comes to selecting financial products, one-quarter of consumers only obtain information from one provider before making their purchase. One-third tends to ignore the small print as long as there are no problems.
- Although the deposit guarantees under the German Deposit Guarantee Act (*Einlagensicherungsgesetz*) protect consumer bank deposits of up to €100,000, half of respondents doubt that their money would be safe at a bank if it were to become insolvent.
- Sustainability aspects have been playing a role in the financial sector for some time now. Almost 80% of consumers want banks to examine undertakings' ethical guidelines before offering them banking services. Roughly 60% say they prefer financial firms with high ethical standards.
- Investments in crypto tokens and initial coin offerings (ICOs) were not an issue for consumers at the time of the survey (summer 2019).
- However, one question took on new prominence during the COVID-19 pandemic: what would happen if they were to lose their main source of income? According to the information they provided, 18% of consumers are especially dependent on their main source of income and could not meet their cost of living for even one month without it. A further quarter could get by for more than one month, but less than three months.

The survey was BaFin's contribution to a global study coordinated by the OECD International Network on Financial Education (INFE), of which BaFin is a member.

BaFin commissioned two market research institutes to conduct the survey. The results of the study have been published on the BaFin website. Researchers can obtain anonymised survey microdata from the Deutsche Bundesbank's Research Data and Service Centre (RDSC).<sup>64</sup>

### 4.3.2 Payment protection insurance for consumer loans

In September 2020, BaFin published the results of its second market survey on payment protection insurance on its website. The review began in 2019 and the evaluation of the results was completed in the summer of 2020.<sup>65</sup> Payment protection insurance serves to meet claims under loans and hire purchase

agreements if the debtor dies, becomes unemployed or unable to work, or cannot meet their obligations for other reasons.

An initial market survey by BaFin on payment protection insurance in 2017 revealed extensive deficits.<sup>66</sup> This prompted lawmakers to add legal requirements designed to ensure greater advice, information and transparency for payment protection insurance policies to the German Insurance Contract Act (*Versicherungsvertragsgesetz*). The new rules entered into force on 23 February 2018 as part of the transposition into national law of the Insurance Distribution Directive (IDD).

#### Second market survey in 2019/2020

BaFin's second market survey also addressed the topic of payment protection insurance. The objective was to capture new trends and to investigate insurers' behaviour given the changes to the statutory provisions in the German Insurance Contract Act. The survey did not cover payment protection insurance for mortgage loans or *Bauspar* loans.

The transposition of the IDD into German law led in particular to improvements to genuine group insurance contracts. The providers' responses show that the insurers have largely implemented the requirements relating to duties to provide information and that individual insurers migrated their contract structures from genuine group insurance contracts to individual contracts. However, there were deficits with respect to revoking payment protection insurance. The new section 7d of the German Insurance Contract Act sets out that anyone who takes out payment protection insurance must be informed again of their right of revocation one week after they have submitted the contractual agreement. Equally, they must also be supplied with another copy of the product information sheet. Many providers enclose a welcome letter along with the documents intended for their customers. The survey showed that many of these letters are not written in a consumer-friendly manner.

It also revealed the high rejection rates at individual insurance undertakings. The most common reason why insurers refused to provide cover was the risk of unemployment. In the case of unemployment insurance, the rejection rates for genuine group insurance contracts were generally between 35% and 55%. In the case of individual insurance contracts, peak rejection rates were up to 66%. BaFin will continue to address this issue.

<sup>64</sup> <https://www.bundesbank.de/en/bundesbank/research/rdsc/research-data-and-service-centre-rdsc--617900>.

<sup>65</sup> [www.bafin.de/dok/14647474](http://www.bafin.de/dok/14647474) (only available in German).

<sup>66</sup> See the 2017 Annual Report, page 38.

In the case of premiums and commission payments and models, BaFin did not see any significant changes across the market as a whole. The commission paid by insurance undertakings to the credit institutions was extremely high in some cases: The 2017 market survey also came to the same conclusion.

#### **Online survey on payment protection insurance**

An online survey that was also performed in 2019 by a market research institute commissioned by BaFin focused on consumers who had taken out payment protection insurance in connection with consumer credit. BaFin published the results of this study as well in September 2020.<sup>67</sup> It revealed that 55% of respondents had the impression that they would either not have been given any loan at all or would have been given one with a higher interest rate if they had not taken out payment protection insurance. Roughly 70% of them also had the wrong idea of the risks insured against.

### **4.3.3 Investigation of certificate distribution**

Before offering financial instruments such as certificates to their customers, distributors must check whether the instruments' manufacturers have correctly identified the target market, i.e. the potential investors. If this is the case, they are allowed to take over the target market. It is important that this check is made. Consequently, all distributors must have their own product approval processes for third-party products. This is required by the product governance regime set out in the European Markets in Financial Instruments Directive II (MiFID II).

BaFin examined for 2019 and 2020 whether distributors are complying with these governance requirements and whether the latter have the protective effect desired by the lawmakers.<sup>68</sup> BaFin surveyed 40 distributors that sell, distribute, offer, recommend or market products: 10 savings banks, 10 cooperative banks and 20 private and foreign banks.

To do this, BaFin randomly selected certificates that were distributed in the 2019 calendar year and in the first quarter of 2020. It transpired that almost two-thirds of the distributors polled took over the target market without any changes from the certificate manufacturer (the designer).

When determining the target market, manufacturers and distributors apply the Common Minimum Standard

for determining a target market for securities agreed by the German Banking Industry Committee (GBIC), the German Investment Funds Association (BVI) and the German Derivatives Association (DDV). This standard has established itself in the period since 2017. It facilitates communication between designers and distributors on the basis of uniform target market criteria, both before and after a financial product has been launched on the market.

#### **65% took over the target market unchanged**

The market survey revealed that 65% of distributors polled applied the manufacturers' target market designation without making any changes. This is not necessarily wrong; distributors can reach the same conclusion as designers. However, if distributors simply use the target market without conducting their own assessment, they delegate their own responsibility to the designers. In this case they will not notice if the designers' target market designation is implausible. Yet it is the distributors themselves who are closest to their customers and who know their needs best.

By contrast, 35% of distributors changed the target market in individual cases – usually by further narrowing its scope. They sometimes also corrected the designers' classifications where these were not plausible in light of the Common Minimum Standard.

If the target market is defined too broadly, investors may be offered certificates that are not aligned with their needs. Although most of the designers complied with the agreed Minimum Standard, in some cases this was applied without thinking. For example, individual designers sometimes identified clients with only basic knowledge and limited experience as the target market for relatively complex underlyings or certificates. Other manufacturers even approved certificates on leveraged indices for investors who have neither knowledge nor experience of how factor certificates work or what the risks involved with them are.

#### **Target market incorrectly determined in 6% of cases**

In 6% of the certificates investigated, the distributors should have adjusted the target market categories but failed to do so. In other words, they treated different products in the same way by defining uniform target markets for groups of certificates that differ greatly in terms of their complexity and risk content.

<sup>67</sup> [www.bafin.de/dok/14647474](http://www.bafin.de/dok/14647474) (only available in German).

<sup>68</sup> [www.bafin.de/dok/15175020](http://www.bafin.de/dok/15175020).



In view of the findings of its market survey, BaFin is drawing the attention of all distributors – and not just the 40 included in the survey – to their obligations. Under the German Securities Trading Act (*Wertpapierhandelsgesetz*), distributors are subject to extensive obligations as part of the product approval process. These obligations are specified in more detail in section 12 of the German Investment Services Rules of Conduct Regulation (*Wertpapierdienstleistungs-Verhaltens- und Organisationsverordnung*) and special section (BT) 5 of the Minimum Requirements for the Compliance Function and Additional Requirements Governing Rules of Conduct, Organisation and Transparency for Investment Services Enterprises (*Mindestanforderungen an die Compliance-Funktion und die weiteren Verhaltens-, Organisations- und Transparenzpflichten – MaComp*).

This means that even if designers and distributors use the same standards, distributors are by no means relieved of their due diligence obligations. In addition, the target market standard set out by the DK, BVI and DDV is only a minimum standard. If it does not provide conclusive results, it may be necessary to further refine the target market. Blind reliance on the minimum standard does not guarantee compliance with the regulatory obligations in all cases.

BaFin has published additional questions and answers<sup>69</sup> on the interpretation of distributors' obligations. It will ensure, as part of its operational supervision, that distributors comply with these obligations.

#### 4.3.4 Coordinated supervisory action by ESMA on suitability assessments

In 2020, the European Securities and Markets Authority (ESMA) again launched a coordinated supervisory action (CSA) by the supervisory authorities in the EU Member States. Following on from the pilot project on "appropriateness assessment" in 2019, ESMA selected the topic of "suitability assessment" for 2020. The participating supervisory authorities, including BaFin, conducted the survey independently within the framework set out by ESMA.

For this project, BaFin surveyed financial services institutions, private banks, savings banks and cooperative banks. The number of institutions surveyed and the response period were adapted in light of the coronavirus pandemic. The survey was performed using

a questionnaire that was sent to the institutions. The market survey covered almost all areas of the suitability assessment. The latter is not a new MiFID II requirement but rather was already required under MiFID I in cases in which investment advice was given or financial portfolio management was performed. In line with this, the implementation status was found to be largely good. However, there is room for improvement in some areas, for example as regards obtaining customer details.

ESMA does not publish the findings of the CSA. However, it did state that it would probably check whether it needed to modify its guidelines regarding certain aspects of suitability. If necessary, ESMA will also publish new Q&As on the topics of suitability assessment and the suitability reports.

The CSA is performed annually. For 2021, the issue of product governance has been selected.

#### 4.4 Interest rate adjustment clauses for premium-aided savings plans

Premium-aided savings plans bearing variable rates of interest were again a core consumer concern in 2020. In addition to the question of whether credit institutions are in fact permitted to terminate such plans prematurely, the focus was on the interest rate adjustment clauses they contain: in Germany, there are thousands of premium-aided savings plans whose interest rate arrangements do not comply with the legal requirements in practice. BaFin continued to monitor this extremely closely in the year under review.

The topic has also been a matter for the civil courts for some time. In 2004 and 2010, the Federal Court of Justice (*Bundesgerichtshof*) passed a number of rulings<sup>70</sup> in which it formulated general requirements for drafting such clauses. These specify that provisions failing to meet these requirements are automatically invalid. Most recently the Dresden Higher Regional Court (*Oberlandesgericht*)<sup>71</sup> answered a number of important questions regarding the concrete wording of interest rate adjustment clauses but left others open. Now the Federal Court of Justice is being called upon to decide again. It was not clear at the end of 2020 when such a judgement could be expected.

<sup>70</sup> Judgements of the Federal Court of Justice of 17 February 2004 – case ref. XI ZR 140/03; 13 April 2010 – case ref. XI ZR 197/09; 21 December 2010 – case ref. XI ZR 52/08 and 14 March 2017 – case ref. XI ZR 508/15.

<sup>71</sup> OLG Dresden, judgement dated 22 April 2020, case ref.: 5 MK 1/19 and judgement dated 17 June 2020, case ref.: 5 MK 1/20.

<sup>69</sup> [www.bafin.de/dok/10849298](http://www.bafin.de/dok/10849298). (only available in German).

According to the information at BaFin's disposal, many credit institutions have reacted to the above-mentioned rulings by the Federal Court of Justice and amended the interest rate adjustment clauses in their savings plans. However, this was generally done unilaterally and without the customers involved being informed or having an opportunity to be involved. In addition, in BaFin's opinion it can be expected that the interest rate adjustment mechanisms subsequently used by the institutions also do not comply in full or at least in part with the Federal Court of Justice's requirements. For example, in many cases neither the reference interest rates used nor the adjustment intervals meet the requirements set out in the rulings.

BaFin is of the opinion that this must be clarified as a matter of principle in the interests of all affected savers, and that this unlawful situation must be remedied without having to have recourse to the law in each individual case.

In February 2020, BaFin made clear in an article for BaFinJournal<sup>72</sup> what it expects from the institutions concerned: they should contact their customers proactively and inform them that the interest rate adjustment clauses in long-term savings plans bearing variable rates of interest are invalid. In addition, BaFin attempted, in a round table meeting on 25 November 2020 with representatives of banks and consumer protection organisations, to agree a solution in the interests of all savers affected. However, the attempt failed due to the resistance of the institutions involved.

BaFin therefore decided at the end of 2020 to use a general administrative act to oblige the institutions concerned to inform their customers that the interest rate adjustment clauses used are invalid. Section 4 (1a) sentence 2 of the German Act Establishing the Federal Financial Supervisory Authority (*Finanzdienstleistungsaufsichtsgesetz*) invests BaFin with the authority to take such a measure to remedy deficiencies related to consumer protection at the institutions and undertakings that they supervise. The consultation procedure for the planned general administrative act had not begun at the end of 2020. The institutions have the opportunity during such procedures to state their position on the proposed measures.

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72 [www.bafin.de/dok/13851978](http://www.bafin.de/dok/13851978).



## 5 Money laundering prevention

### 5.1 Application guidance on the German Money Laundering Act (*Geldwäschegesetz*) for insurers

In January 2020, BaFin published its “Interpretation and Application Guidance in relation to the German Money Laundering Act (*Geldwäschegesetz*) – Special section for

insurance undertakings” (BT-AuA/VU). This addresses questions relating to the implementation of the Money Laundering Act for an individual supervisory sector for the first time. The goal is to help insurers implement the act by providing a clear definition of what constitutes a loan, the requirements governing occupational retirement provision contracts and the duties to regularly update information on clients with existing insurance policies. Interpretation and application guidance for other financial market sectors were under development at the end of 2020.

## 5.2 FATF evaluation

Since 2020, the Financial Action Task Force – FATF for short – has been evaluating Germany as part of its regular country assessments (see info box). One of the focus areas is the financial sector. BaFin performed the preparatory work for this part of the evaluation in 2020. In particular, it addressed the on-site visit by the FATF assessment team that had been scheduled for 2021.

The approval of the mutual evaluation report by the FATF Plenary marks the completion of the evaluation of Germany. The FATF performs what are known as mutual evaluation processes to assess the measures adopted by member states to combat money laundering, terrorist financing and proliferation financing.

### At a glance

#### Financial Action Task Force

Germany is a founding member of the Financial Action Task Force (FATF), which was established in 1989. The FATF is the most important international body for combating and preventing money laundering and terrorist financing. It sets standards and issues recommendations for these areas (“International Standards on Combating Money Laundering and the Financing of Terrorism & Proliferation – The FATF Recommendations”).

The FATF uses a mutual evaluation process to continuously monitor whether its member states implement these standards and how they combat the risks and threats associated with money laundering, terrorist financing and proliferation financing. As part of this process, it sends assessment teams to visit the different countries. Germany was last assessed in 2010 during the third round of mutual evaluations. At the time, the evaluation focused on the binding legal measures taken by Germany and other member jurisdictions to implement the FATF’s Standards and Recommendations. The current fourth round of evaluations focuses on how effectively the countries are implementing the FATF Standards and whether the FATF objectives are being met.

## 5.3 Cooperation in the Anti Financial Crime Alliance

The Anti Financial Crime Alliance (AFCA) has become a key pillar of the fight against money laundering and terrorist financing within a very short space of time (see info box). A total of five working groups have now been established under the umbrella of the AFCA, which takes the form of a public-private partnership.

### At a glance

#### Joint efforts to combat money laundering

On 24 September 2019, BaFin, the Financial Intelligence Unit (*Zentralstelle für Finanztransaktionsuntersuchungen – FIU*), the Federal Criminal Police Office (*Bundes-kriminalamt*) and 14 banks launched the Anti Financial Crime Alliance (AFCA). Within this public-private partnership, the authorities and banks, led by the FIU, seek to strengthen and coordinate the fight against money laundering and terrorist financing. One precondition for successfully combating money laundering is the strategic exchange of information on an ongoing basis. The partners therefore use this joint institution to exchange findings and insights swiftly, securely and in detail.

They also contribute their own experience to the AFCA. The FIU is the central unit in Germany for all suspicious transaction reports. Banks are legally required to prevent the abuse of the financial system for money laundering and terrorist financing. In turn, BaFin monitors whether the banks actually do this and that they comply with the statutory anti-money laundering requirements. Last but not least, the role of the Federal Criminal Police Office is to ensure that money launderers and terrorist financiers can be prosecuted.

The AFCA is headed by a six-person board composed of representatives of the member banks and public authorities. BaFin Chief Executive Director Dr Thorsten Pötzsch represents BaFin on the board, which is chaired by FIU head Christof Schulte.

BaFin is co-head of AFCA Working Group 2 on “Risks and trends in the financial sector” together with Commerzbank AG. This is tasked with increasing the strategic exchange of information between public authorities and banks. The common goal is to identify patterns and phenomena that will help develop new money laundering typologies, and to generally improve the prevention of money laundering and terrorist financing.

In 2020, the members of the working group produced papers on indicators and advisory documents on, among other things, shell companies and the risks posed by the COVID-19 pandemic in relation to money laundering and terrorist financing.

#### 5.4 Inspection statistics and inspection priority areas for the Prevention of Money Laundering Directorate

BaFin conducted or shadowed a total of 77 inspections in the field of money laundering prevention in 2020 (prior year: 109 inspections) (see Table 34). However, due to the coronavirus pandemic these inspections had to take place remotely as from the second quarter onwards instead of taking the form of on-site visits, as is usually the case.

In the case of the inspections that BaFin performed itself, it focused firstly on the key areas of suspicious transaction reports, the money remittance business and crypto-assets but also on the risk analysis and monitoring operations, and the position of and work performed by the AML officer, in the institutions concerned.

BaFin discovered serious deficiencies with respect to risk analysis in some cases. Conversely, there were generally no serious deficiencies in the case of suspicious transaction reports and the money remittance business.

**Table 34: Money laundering inspections in 2020**

Type	Banking sector	Non-banking financial sector
Own inspections	33	8 (of which 6 agents)
Shadowing of audits of annual financial statements	14	10
Special audits by auditors	11	1

#### 5.5 Statistics on account information access procedures

Section 24c (1) of the German Banking Act (*Kreditwesengesetz*) requires credit institutions, asset management companies and payment institutions to maintain an electronic file in which they store certain account master data such as the account number, the name and date of birth of the account holders and persons authorised to draw on the account, and the dates on which the account was opened or closed. On request, BaFin provides information contained in this account information access file to the authorities listed in section 24c (3) of the Banking Act. It did so on 289,861 occasions in 2020 (see Table 35).

**Table 35: Account information access procedures in accordance with section 24c of the Banking Act**

Recipient	2020		2019	
	absolute	in %	absolute	in %
BaFin	235	0.08	752	0.4
Tax authorities	15,667	5.41	12,648	6.8
Police authorities	219,754	75.81	131,959	70.7
Public prosecutors	39,375	13.58	29,982	16.1
Customs authorities	14,057	4.85	10,683	5.7
Other	773	0.27	551	0.3
<b>Total</b>	<b>289,861</b>		<b>186,575</b>	



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## 6 Unauthorised business activities

### 6.1 Fundamental aspects

#### 6.1.1 Regulation of crypto-assets – MiCA Regulation

The legal framework for issuing and trading crypto-assets will change significantly as a result of the comprehensive regulation of these digital legal assets planned by the European Commission. At the end of September 2020, the European Commission published its draft Markets in Crypto-Assets Regulation (MiCA)<sup>73</sup>. Key points of the new legislation include new duties for issuers of particularly relevant crypto-assets: asset-referenced tokens and e-money tokens have different reserves of legal tender, commodities or other crypto-assets. As a result, they promise stable values, which could make them interesting as alternative means of payment. Issuing these types of crypto-assets is only to

be permitted if they have previously passed through a successful approvals process.

In addition, the draft contains authorisation requirements for providers who want to supply services in connection with such crypto-assets. It covers activities corresponding to existing financial services such as the provision of advisory services relating to crypto-assets, exchanging them for legal tender, or custodial services.

If the European regulation is adopted as proposed, digital tokens will fall under two different regimes in future: tokens that are classified as financial instruments will continue to be governed by the German Banking Act (*Kreditwesengesetz*). By contrast, issuers of payment and utility tokens and service providers active in this segment will have to comply with the rules set out in the EU regulation going forward.<sup>74</sup>

<sup>73</sup> European Commission, Proposal for a regulation on markets in crypto-assets, and amending Directive (EU) 2019/1937.

<sup>74</sup> See chapter II.1 for further details on the European Commission's Digital Finance Package.

### 6.1.2 Draft law on electronic securities

In mid-December 2020, the Federal Cabinet resolved the draft law on electronic securities (*Geszentwurf zur Einführung elektronischer Wertpapiere*), which was submitted jointly by the Federal Ministry of Finance (*Bundesfinanzministerium – BMF*) and the Federal Ministry of Justice and Consumer Protection (*Bundesministerium der Justiz und für Verbraucherschutz – BMJV*).<sup>75</sup> The Federal Government’s aim with the new legislation is to open up German law to allow electronic securities that do not use the currently mandatory paper certificates. Instead, the latter will be replaced by a digital entry – either as a central register security in a register maintained by a central custodian or a custodian bank or in the form of a crypto-asset security maintained by a crypto-asset securities register based on distributed ledger technology. This makes it necessary to extend the scope of the German Banking Act (*Kreditwesengesetz*) to include a new activity requiring authorisation: crypto-asset securities register management. In future, BaFin would therefore approve and supervise both sorts of register managers.

### 6.1.3 Crowdfunding Regulation

The Regulation on European Crowdfunding Service Providers (known for short as the ECSP Regulation) entered into force on 9 November 2020.<sup>76</sup> This is part of the European Commission’s FinTech Action Plan.<sup>77</sup> The regulation is designed to remove existing barriers to cross-border crowdfunding and create a framework that ensures a high level of investor protection.

Crowdfunding is increasingly becoming established as an alternative form of finance for start-ups and small and medium-sized enterprises (SMEs). This is normally based on relatively small investment amounts. In this kind of brokerage, a crowdfunding service provider operates a public internet platform. This offers a way for companies needing finance and potential investors or lenders to find each other. Where the ECSP Regulation applies it is exclusive and takes precedence over national law.

<sup>75</sup> BMJV, *Gesetz zur Einführung von elektronischen Wertpapieren*, [https://www.bmjv.de/SharedDocs/Gesetzgebungsverfahren/DE/Einfuehrung\\_elektr\\_Wertpapiere.html](https://www.bmjv.de/SharedDocs/Gesetzgebungsverfahren/DE/Einfuehrung_elektr_Wertpapiere.html) (only available in German).

<sup>76</sup> OJ EU L 347 dated 20 October 2020.

<sup>77</sup> European Commission: FinTech Action Plan: For a more competitive and innovative European financial sector.

Since the regulation came into force, it is mandatory for crowdfunding brokers to have an ECSP licence; the application for this must be submitted to BaFin. BaFin is also responsible for prosecuting unauthorised business activities in this area.

## 6.2 Authorisation requirement

Anyone wishing to conduct banking business, e-money business, investment business or insurance business in Germany may do so only with authorisation from BaFin. Once a licence has been granted, the entity concerned is then automatically subject to BaFin’s supervision. The same applies to financial services and payment services (see info box on page 120).

In 2020, the number of new queries received by BaFin in relation to authorisation rose slightly to 1,113, up from 1,055 in 2019 (see Table 36). The focus was on fintech issues, the supply and trading of crypto-assets (locally stored digital financial instruments), crypto custody transactions, new payments services and queries in relation to the coronavirus pandemic.

**Table 36: New authorisation queries**

	2018	2019	2020
New authorisation queries	1,397	1,055	1,113

### Exemption from the authorisation requirement and ongoing supervision

In accordance with section 2 (4) of the German Banking Act (*Kreditwesengesetz*), BaFin can exempt undertakings from the authorisation requirement in the case of business that is limited in scope. This also exempts the service provider from having to comply with a statutory catalogue of provisions that they would have to meet during ongoing supervision. However, such an exemption is only possible for as long as the undertaking does not require supervision due to the nature of its business. In order to qualify for exemption, undertakings have to meet strict conditions and the business conducted must be atypical from a banking perspective. This will regularly be the case, for example, where such business is merely auxiliary or ancillary to the operator’s actual, i.e. core, business and does not have any economic importance in its own right.

Third-country undertakings may only be exempted from the authorisation requirement if qualified supervision is performed by the competent authority in the third-party country. This means that additional supervision by BaFin of business conducted in Germany is unnecessary,

At a glance

## Authorisation requirement

BaFin's responsibilities include examining the business conducted by new providers and new business models introduced at established undertakings to determine whether they have to be authorised under the supervisory legislation. Providers require prior authorisation for the following businesses:

- banking business or financial services under the German Banking Act (*Kreditwesengesetz*)
- insurance business under the German Insurance Supervision Act (*Versicherungsaufsichtsgesetz*)
- payment services or e-money business under the German Payment Services Supervision Act (*Zahlungsdienststeaufsichtsgesetz*)
- management of investment funds within the meaning of the German Investment Code (*Kapitalanlagegesetzbuch*)

If a provider has already commenced an activity that actually requires authorisation without having obtained the necessary licence from BaFin, the latter will enforce its right to withhold authorisation. In other words, it will ensure that the provider ceases to perform, and winds up, the unauthorised business without delay. BaFin will inform investors of this on its website, [www.bafin.de](http://www.bafin.de), and in BaFinJournal. Depending on the nature of the case, BaFin may also file a complaint with the prosecuting authorities against the operators responsible.

BaFin can only determine whether a planned business activity requires authorisation on a case-by-case basis. However, it has published Guidance Notices on its website that enable potential providers to make an initial self-assessment.

and avoids the effort involved in dual supervision. This is governed by section 2 (5) of the German Banking Act.

**Table 37: Exemption of institutions**

	2018	2019	2020
Exempted institutions	368	361	358
Newly exempted institutions	10	3	3

In practice, BaFin only grants such exemptions on application. However, it only makes use of this option in extremely rare cases – the normal situation is that authorisation is required for an activity classified by law as a banking business or financial service.

### 6.3 Investigation of unauthorised business activities

Any violation of the authorisation requirements also impacts the integrity of the entire financial system. Anyone who conducts business activities subject to the authorisation requirement without having obtained the required authorisation from BaFin is committing an offence (see info box on page 121).

As in the past, investigation of unauthorised business activities in 2020 mainly focused on digital business models such as online trading platforms and their money transfer companies, and on bitcoin ATMs. In addition, BaFin recorded an increasing number of cases of identity theft and attempts to recruit trust assistants.

#### Suspected violations hit new record level in 2020

2020 saw another rise in the number of suspected violations – from 1,318 cases in 2019 to 1,436 cases in 2020 – due both to an increased number of tip-offs and more intensive enforcement activities (see Table 38). BaFin took formal steps against unauthorised business activities in 176 cases – the largest number to date. Many providers discontinued their unauthorised business voluntarily after a hearing with BaFin on the issue.

**Table 38: Investigations of unauthorised business activities**

	2018	2019	2020
New suspected violations	1,281	1,318	1,436
Searches	23	17	6
Formal measures	87	150	176



At a glance

## How BaFin investigates unauthorised business

In keeping with its public risk prevention mandate, BaFin is tasked with investigating businesses operating without the necessary authorisation. In such cases it enforces the authorisation requirement in order to prevent damage to the integrity of the financial market, regardless of any subsequent criminal proceedings. BaFin devotes substantial resources to this, and lawmakers have provided it with a wide range of investigative instruments. For example, it is entitled to search both business and private premises, and persons.

These powers are inevitably limited if perpetrators are operating from other countries. In such cases, however, BaFin can have recourse to domestic telecommunications networks, website providers and banks (e.g. in order to freeze accounts or cash). In addition, BaFin is constantly expanding its cross-border collaboration with foreign authorities.

BaFin publishes the measures it takes on its website and in BaFinJournal in order to warn investors.

Irrespective of any formal measures taken, BaFin issued 16 warnings in 2020 (previous year: 43) on its website and in BaFinJournal about undertakings that had contacted German customers anonymously or under a false identity by e-mail or telephone, or online. As is usual in such cases, the providers contacting customers were located abroad. They claimed untruthfully that they were supervised by BaFin, or created that impression, in order to lull customers into a false sense of security.

### Objections and court proceedings

Affected parties can file objections to formal measures imposed by BaFin.

**Table 39: Objection proceedings**

	2018	2019	2020
New objection proceedings	48	34	45
Formal objection notices	34	22	15
Withdrawn/otherwise discontinued	19	16	4

The measures imposed by BaFin are immediately enforceable by law and objections do not have suspensory effect. The only option open to the parties for which the formal measures are intended is to bring a summary application before the Frankfurt am Main Administrative Court (*Verwaltungsgericht*) for an order that the legal remedy should have a suspensory effect.

**Table 40: Summary proceedings – first instance**

	2018	2019	2020
New summary proceedings	8	8	16
Application dismissed	7	11	7
Order for suspensory effect	0	0	1

If BaFin ultimately rejects the objection brought against a formal measure, the party for which the measure is intended can bring a legal action before the Frankfurt am Main Administrative Court.

**Table 41: Legal proceedings – first instance**

	2018	2019	2020
New legal proceedings	16	10	19
Judgement in favour of BaFin	2	7	9
Action allowed	1	0	0
Action withdrawn/otherwise discontinued	10	5	3

On appeal, the Hesse Higher Administrative Court (*Verwaltungsgerichtshof*) completed 7 appeal proceedings in 2020 (previous year: 2) and 2 (previous year: 3) interim relief proceedings.

## 6.4 Bitcoin ATMs

Crypto ATMs in Germany must be authorised by BaFin. However, some providers set up these machines without having such a licence. BaFin is increasingly taking action against such operators – among other reasons due to the possibility of money laundering. In addition, criminals use bitcoin ATMs to render the proceeds of crime untraceable.

## 6.5 Money transfer companies

In 2020, BaFin again issued a large number of prohibition and liquidation orders against money transfer companies acting for fraudulent trading platforms. The objective is generally to permanently stop the operators of such illegal money transfer companies and to return any sums secured. In addition, BaFin uncovered new methods being used by perpetrators in an attempt to conceal the flows of funds generated using fraudulent trading platforms<sup>78</sup>: for example, perpetrators more frequently misused accounts belonging to private individuals or exchanged money before forwarding it in the form of crypto-assets.

## 6.6 Platforms

Fraudulent trading platforms remained a focus of the prohibition and liquidation orders issued in relation to unauthorised business in 2020. The fact that criminal transactions are becoming more and more professional from a technical perspective, and that perpetrators are constantly developing new ways of transferring money, is making investigations more difficult. BaFin is stepping up its close cooperation with national and international competent investigating authorities.

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<sup>78</sup> See 6.6.



## 7 Sanctions

In 2020, BaFin initiated a total of 220 administrative fine proceedings<sup>79</sup> (see info box).<sup>80</sup> The proceedings were brought against natural persons, payment agents, credit institutions, insurance undertakings, payment institutions and finance leasing and/or factoring institutions<sup>81</sup>, and, where applicable, also against the persons responsible for these companies. They were triggered by violations of provisions of the following German acts that are punishable by administrative fines:

- Money Laundering Act (*Geldwäschegesetz*)
- Banking Act (*Kreditwesengesetz*)
- Insurance Supervision Act (*Versicherungsaufsichtsgesetz*)
- Capital Investment Act (*Vermögensanlagegesetz*)
- Securities Trading Act (*Wertpapierhandelsgesetz*)
- Securities Prospectus Act (*Wertpapierprospektgesetz*)
- Payment Services Supervision Act (*Zahlungsdienstleistungsaufsichtsgesetz*)

<sup>79</sup> Proceedings in accordance with the German Act on Breaches of Administrative Regulations (*Ordnungswidrigkeitengesetz*).

<sup>80</sup> For information on the distinction between sanctions and measures, see info box and the 2016 Annual Report (page 55 ff.).

<sup>81</sup> Section 1 (1a) sentence 2 nos. 9 and 10 of the Banking Act.

### Definition

#### Measures or sanctions?

BaFin has a large number of measures at its disposal to protect the integrity of the financial market and collective consumer interests; these are defined in various specialised pieces of legislation. This suite of measures enables BaFin to take action against both legal entities (i.e. undertakings) and natural persons. In addition to taking classic supervisory law measures, BaFin can also pursue breaches of the law by imposing administrative fines.

The two options for taking action differ in terms of their objectives. Supervisory measures are intended to avert threats. They should be seen as preventive administrative actions that do not necessarily have to be prompted by a legal violation. Administrative fines, by contrast, are sanctions, i.e. repressive administrative acts. The term “repressive” is used because the law on breaches of administrative regulations aims to sanction breaches that have been established by imposing fines. Another purpose is to persuade perpetrators to comply with the legal provisions in future.

## Total volume of administrative fines

Administrative fines totalling **€8,499,000** were imposed across all of BaFin's sectors in 2020 (see info box).

### At a glance

## Administrative fines imposed by BaFin

BaFin imposed administrative fines totalling **€8,499,000** in 2020.

- Administrative fines totalling **€399,000** were attributable to Banking Supervision, Prevention of Money Laundering and Insurance Supervision.
- The Securities Supervision/Asset Management Sector imposed administrative fines totalling **€8,500,000**.

## New administrative fine proceedings initiated by BaFin

BaFin initiated 220 administrative fine proceedings in 2020.

- 116 of these were attributable to Banking Supervision, Prevention of Money Laundering and Insurance Supervision.<sup>82</sup>
- 107 proceedings<sup>83</sup> were attributable to the Securities Supervision/Asset Management Sector.

## Administrative fine proceedings initiated by Securities Supervision

In 2020, BaFin's Securities Supervision/Asset Management Sector imposed administrative fines totalling €8.5 million<sup>84</sup> for violations of capital markets law<sup>85</sup> (see info box). 107 new administrative fine proceedings were initiated<sup>86</sup>, while 517 proceedings

were still pending from the previous year. The Sector concluded a total of 292 proceedings, imposing administrative fines in 172 cases. This translates into a prosecution ratio of approximately 59%.<sup>87</sup>

## Administrative fine proceedings initiated by Banking and Insurance Supervision

In the area of the supervision of undertakings<sup>88</sup>, BaFin initiated 116<sup>89</sup> proceedings against legal entities in 2020 relating 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 fines. The legal entities against which proceedings were brought included credit institutions, insurance undertakings, payment institutions and finance leasing and/or factoring institutions. They were also directed against the management personnel of the undertakings concerned, such as managing directors and money laundering officers, as well as against other natural persons who are subject to professional supervision requirements.<sup>90</sup> BaFin issued 19 administrative orders imposing a fine in these proceedings and in other administrative fine proceedings that were still pending from previous years.

17 of these administrative orders imposing a fine became final in 2020, including 14 for which no appeal was lodged. 3 administrative orders imposing a fine became final in a preliminary hearing following an ordinary appeal. 2 other cases of administrative fine proceedings against a credit institution and a foreign financial services institution are awaiting a preliminary hearing after a participant appealed.

An appeal by an agent as defined by section 1 (9) of the Payment Services Supervision Act that was still pending from the previous year was the subject of a decision in the first instance by the Frankfurt am Main Local Court (*Amtsgericht*), which fully upheld on its merits the administrative order imposing a fine.

82 These proceedings were initiated by the Internal Administration and Legal Affairs Sector. The prevention of money laundering has been part of the Resolution Sector since the beginning of 2018.

83 This information refers to the figures stated in chapter III.3.3.6.

84 This total refers to the administrative fines stated in chapter III.3.3.6.

85 This covers violations of the Securities Trading Act, the Securities Acquisition and Takeover Act, the Capital Investment Act, the Securities Prospectus Act, Regulation (EU) No 1286/2014 on key information documents for packaged retail and insurance-based investment products (PRIIPs) (PRIIPs Regulation), Regulation (EU) No 236/2012 (EU Short Selling Regulation), Regulation (EU) No 600/2014 (Markets in Financial Instruments Regulation – MiFIR) and Regulation (EU) No 596/2014 (Market Abuse Regulation – MAR).

86 This information refers to the figures stated in chapter III.3.3.6.

87 The statistical data refers to the administrative fine proceedings stated in chapter III.3.3.6.

88 These proceedings were initiated by the Internal Administration and Legal Affairs Sector. See page 106 for a summary of administrative fine proceedings in the area of market supervision.

89 Proceedings in accordance with the Act on Breaches of Administrative Regulations.

90 Or against the persons responsible for these entities.

In the case of 3 administrative orders imposing a fine dating from 2018 that had been confirmed in 2020 in the first instance by the Frankfurt am Main Local Court, the party concerned and two interested parties lodged appeals; the Frankfurt am Main Higher Regional Court (*Oberlandesgericht*) will decide in these.

A total of 48 proceedings, some of which were pending from previous years, were discontinued in 2020, 18 of them for discretionary reasons.<sup>91</sup>

30 proceedings were terminated in other ways, for example by discontinuing proceedings in accordance with section 46 (1) of the German Act on Breaches of Administrative Regulations (*Ordnungswidrigkeitengesetz*), normally in conjunction with section 170 (2) of the German Code of Criminal Procedure (*Strafprozessordnung*). 5 proceedings were transferred to the public prosecutor's office in accordance with section 41 of the Act on Breaches of Administrative Regulations due to indications that a criminal offence had been committed, or were taken over by the public prosecutor in accordance with section 42 of the Act on Breaches of Administrative Regulations because there was a connection between investigations relating to a potential criminal act being pursued there and the administrative offence proceedings at BaFin.

### **Total volume of administrative fines**

In 2020, BaFin imposed a total of 39 individual administrative fines relating to violations of provisions of the Money Laundering Act, the Banking Act, the Insurance Supervision Act and the Payment Services Supervision Act; these amounted to €399,000 in total. The fines were imposed on credit institutions, insurance undertakings and finance leasing and/or factoring institutions and – depending on the specific facts of the case – also against the persons responsible for these companies or against third parties engaged to perform tasks.

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<sup>91</sup> Section 47 (1) of the Act on Breaches of Administrative Regulations.



## 8 Contact point for whistleblowers

The Whistleblower Directive<sup>92</sup> entered into force in the European Union (EU) in December 2019. It protects persons who report breaches of Union law, and EU Member States must transpose it into national law by the end of 2021. BaFin actively prepared for this in 2020 as a member of international working groups and by helping to design the national legislation. A project team at the European Central Bank (ECB), of which BaFin was a member, identified potential challenges that the supervisory authorities in the Member States are likely to face when implementing the Directive, and illustrated potential solutions.

Public perceptions of whistleblowers have changed. Whereas they were previously more likely to be seen as informers, the general public now recognises how important they are for throwing light on irregularities. This can be seen from the fact that both public interest

in the work of BaFin's contact point for whistleblowers and the number of reports submitted are continuously increasing.

In line with this, the number of reports received rose substantially again in 2020 to total 1,319, up from 925 in the previous year.

More than 59% of whistleblowers used the electronic whistleblowing system that BaFin introduced on 1 January 2017. Roughly 33% of the notifications were submitted by e-mail, while 6% were received by post. Phones were used to provide information in approximately 1% of cases. As in the previous year, less than 1% of whistleblowers paid personal visits.

A total of 53% of the submissions concerned alleged violations by supervised institutions. BaFin follows up on the reports and takes measures where necessary to stop the breaches. 36% of notifications related to potentially unauthorised business activities, which BaFin also investigates. 4% related to alleged money laundering activities and 6% concerned complaints relating to consumer protection issues. The remaining notifications related to matters for which BaFin is not the competent authority or that did not contain any identifiable facts.

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<sup>92</sup> Regulation (EU) 2019/1937 of the European Parliament and of the Council of 23 October 2019 on the protection of persons who report breaches of Union law, OJ L 305 dated 26 November 2019.



# IV

## Resolution





# 1 Fundamental aspects

## 1.1 MaBail-in

In the fourth quarter of 2020 BaFin, as the national resolution authority (NRA), conducted a consultation process for the first revision of its Circular regarding the Minimum Requirements for Implementing a Bail-in (*Mindestanforderungen zur Umsetzbarkeit eines Bail-in – MaBail-in*) (see info box). The revised version is intended to help further improve institutions' resolvability in the event of a bail-in. The Circular is addressed to institutions for which BaFin in its capacity as national resolution agency is responsible (see info box on page 131) and which are not candidates for insolvency proceedings (see info box on page 130).

Unlike the first version of the MaBail-in dated 4 July 2019, which focused only on liabilities up to and including the senior non-preferred insolvency class, the new version now includes all liabilities that are eligible for bail-in. This also applies to other liabilities that, although excluded by law from bail-ins, may

nevertheless include components eligible for bail-in as at the effective date of the resolution; one example here are secured liabilities.

### At a glance

#### **Bail-in: a legal perspective**

There are two elements to a bail-in under the German Recovery and Resolution Act (*Sanierungs- und Abwicklungsgesetz*):

- the write-down and conversion of relevant capital instruments in accordance with section 89 of the Recovery and Resolution Act and Article 21 of the SRM Regulation;<sup>1</sup>
- the bail-in of creditors in accordance with section 90 of the Recovery and Resolution Act and Article 27 of the SRM Regulation.

<sup>1</sup> "SRM" stands for "Single Resolution Mechanism".

The revised Circular permits institutions to limit the information to be provided to specific insolvency classes so as to enable them to handle this increased volume of information in a resource-effective manner. In exceptional cases, for example, it might be enough to provide information only on liabilities up to and including the senior non-preferred insolvency class, to the extent that the institution meets the relevant economic requirements for this. BaFin's new version of the MaBail-in will also require new data to be captured that can then be requested if a resolution process occurs.

## 1.2 Guidance Notice on external bail-in execution

BaFin also conducted a consultation process for its Guidance Notice on external bail-in execution in the fourth quarter of 2020. This is addressed to all institutions issuing securities in Germany and builds in terms of its content on the minimum requirements for bail-ins.

The first version of the Guidance Notice, which was published on 1 October 2019, focused on a base case scenario. For example, it only considered stock corporations with bearer shares, assumed bonds would only be denominated in euros and was restricted to the activities of the financial market infrastructures (FMIs) that were involved in its preparation: Clearstream Banking, WM Datenservice and the Frankfurt Stock Exchange. The second version of the Guidance Notice now extends the focus at both the procedural and the technical level to cover all legal organizational forms and all classes of shares, as well as taking foreign-currency bonds into account. Whereas the discontinuation and suspension of trading previously only covered the regulated market on the Frankfurt Stock Exchange, the new version of the Guidance Notice also covers the suspension of trading on regulated and non-regulated markets at regional exchanges, such as the Stuttgart Stock Exchange.

The first version of the Guidance Notice also assumed that the share conversion process at a stock corporation would not modify the class of shares involved. A notification of the features of the new shares by the resolution authority was all that was needed to admit the new shares of the same class to the regulated market. The "simplified listing application" in the new version now covers all other cases. Besides the class of shares, for instance, the institution's legal form or stock market listing can also change after resolution. Another new point is that, unlike the first version, the revision includes the option of suspending payments during the technical implementation phase (i.e. for a limited period).

### At a glance

#### **Different methods of resolution**

There are a number of ways in which institutions can be resolved in an orderly manner. In addition to bail-ins of shareholders and creditors, institutions can be sold to competitors. It is also possible to transfer them to a bridge institution or asset management company.

If resolution is not in the public interest, however, then normal insolvency proceedings rather than resolution proceedings are instituted once a proportionality test has been performed; this applies particularly in the case of smaller banks.

## Who is responsible?

### 1 Resolution in the banking union

European lawmakers created the Single Resolution Mechanism (SRM) for the eurozone on 1 January 2016 as Pillar Two of the banking union. Pillar One is the Single Supervisory Mechanism (SSM), which is headed by the European Central Bank (ECB).<sup>2</sup>

The SRM comprises the Single Resolution Board (SRB) and the national resolution authorities (NRAs) in the eurozone. BaFin has been the NRA for Germany since 2018. Before that, the Financial Market Stabilisation Agency (*Bundesanstalt für Finanzmarktstabilisierung*) performed this task. Responsibilities within the SRM are divided between the SRB and the NRAs.

#### BaFin's role as an NRA

In its capacity as an NRA, BaFin is responsible for those German institutions that are classified as less significant institutions (LSIs) in the SSM. This category also includes financial market infrastructures (FMIs) with banking licences and central counterparties (CCPs) with and without banking licences.

#### SRB

The SRB is responsible for

- significant institutions (SIs) within the SSM that are supervised by the ECB;
- cross-border LSIs; and
- LSIs for which responsibility is transferred to the SRB in certain circumstances.

The SRB has established Internal Resolution Teams (IRTs) for each institution or group of institutions for which it is responsible, with the SRB and the relevant competent NRAs working together jointly in these. In other words, the IRTs are similar to the Joint Supervisory Teams (JSTs) in the SSM. The core task of the IRTs is to enhance institutions' resolvability. They do this by developing and updating resolution plans. Among other things, they assess the impediments to a potential resolution and appropriate measures to remove them. In 2020, BaFin took part in 37 IRTs.

### 2 Resolution in the European Union and cooperation with third-country authorities

The SRB and the NRAs establish resolution colleges to coordinate collaboration between different resolution authorities in the banking union, in Europe and in third countries. The main purposes of these colleges are

- to exchange information
- to develop group resolution plans
- to assess specific institutions' resolvability
- to remove impediments to resolution
- to decide on group resolution schemes and
- to coordinate public communications

In 2020, BaFin took part in 20 resolution colleges.

Crisis Management Groups (CMGs) are set up for all institutions classified by the Financial Stability Board (FSB) as global systemically important banks (G-SIBs). 19 of the 30 institutions worldwide that were classified as G-SIBs in 2020 have operations in Germany. BaFin also headed a CMG on CCPs in 2020 and took part in seven others. All in all, therefore, BaFin collaborated in a total of 27 CMGs in 2020.

<sup>2</sup> See chapter III.1.2 for further information on the SSM.

### 1.3 MaValuation

In 2020 BaFin, in its capacity as an NRA, also conducted a consultation process for its “Minimum requirements for information systems to provide information for valuations in the context of resolution” (*Mindestanforderungen an Informationssysteme zur Bereitstellung von Informationen für Bewertungen im Rahmen einer Abwicklung – MaValuation*). The MaValuation specifies in detail the type of information that is needed for the valuations to be performed in the course of resolution. It answers the question of what information the institutions must provide for this purpose. It is based on the principle of proportionality and comprises a two-step approach: step I is looking mainly at existing internal and external standard reports and the institution’s documentation, while in step II BaFin will require a data model from the institutions. Step II is not included in the first version of the MaValuation.

Since the new version of the MaBail-in extends the data requested to include all liabilities eligible for bail-in, the MaValuation is becoming even more important. This is because valuers are no longer merely responsible for determining the losses, net asset values and recapitalisation requirements for the institution to be resolved. Depending on the specific case in question, they are now also, for example, required to establish bail-in values for structured and/or partially secured instruments, and to assess close-out amounts for derivatives and securities financing transactions.

### 1.4 General administrative act on eligible liabilities prolonged

On 26 June 2020, BaFin prolonged its general administrative act on granting permission for repurchases until 28 December 2020. It had published the original act on 26 June 2019. In it, BaFin sets out the details of a general permission for certain institutions to terminate, repay or repurchase eligible securities before these fall due.

At the end of December, BaFin then issued an identically worded general administrative act that is valid until 27 December 2021. The background to this are statutory amendments that entered into force as of 28 December 2020 and that affect the Recovery and Resolution Act, among other things. The amendments do not require any changes to be made to the general administrative act. BaFin reserves the right to prolong the general administrative act again in order to provide institutions with a proportionate repurchasing method in particular in the period until a regulatory technical standard (RTS) is issued.

## 2 Institutions for which the SRB is directly responsible

The Single Resolution Board (SRB) was directly responsible for 122<sup>3</sup> institutions<sup>4</sup> under the SRM in 2020 (see info box on page 131). This included 37 institutions or groups of institutions that are domiciled in Germany or have cross-border operations in the eurozone. BaFin took part in the IRTs formed for each institution or group of institutions.

Successfully overcoming crises requires resolution and supervisory authorities and other affected stakeholders to work together across borders effectively and on a basis of trust. The participants in the numerous SRM bodies successfully extended and improved their cooperation despite the COVID-19 pandemic.<sup>5</sup>

## 3 Institutions for which BaFin is responsible

At the end of 2020, BaFin was directly or indirectly responsible in its capacity as a NRA for resolution and resolution planning for 1,389 institutions and groups of institutions that are domiciled in Germany or have cross-border operations in the eurozone. It was directly responsible for 1,355 of these undertakings (see info box on page 131).

BaFin continued to make steady progress in 2020 and further improved the institutions’ resolvability.

3 See also the SRB website, <https://srb.europa.eu/en/content/banks-under-srbs-remit>.

4 See also the SRB Annual Report, [https://srb.europa.eu/sites/srbsite/files/srb\\_annual\\_report\\_2019.pdf](https://srb.europa.eu/sites/srbsite/files/srb_annual_report_2019.pdf).

5 See also chapter I.1.

# 4 Resolution planning

## 4.1 2020 resolution planning cycle

In the 2020 planning cycle (see info box), BaFin was closely involved, as a member of the relevant Internal Resolution Teams, in the resolution planning for the 17 institutions domiciled in Germany that fall under the direct responsibility of the SRB. In addition, BaFin collaborated on the resolution planning for 20 foreign groups of institutions for which the SRB was primarily responsible.

### At a glance

#### Resolution planning cycle

The resolution planning cycle generally starts on 1 April of one year and runs until 31 March of the following year.

During this period, the resolution strategy for and the resolvability of the relevant institutions is continually analysed and, where necessary, improved.

As part of the IRTs, BaFin worked to enhance the resolution planning (see info box on page 131). In particular, it focused on the progress made by individual institutions with respect to resolvability. Issues included improving data quality and availability and the internal processes and structures suited for use in crises, as well as the determination of (internal) MREL ratios. The minimum requirements for own funds and eligible liabilities (MREL) are a key resolution planning tool<sup>6</sup> and are designed to ensure banks' resolvability.

The 2020 planning cycle also focused for the first time on institutions whose significance has increased substantially as a result of Brexit, e.g. because they have expanded their business activities in Germany.

BaFin had primary responsibility in the 2020 planning cycle for 1,389 of the institutions and groups of institutions in Germany, both for the planning and for the implementation of resolution measures. These include less significant institutions, financial market infrastructures, subsidiaries of undertakings domiciled in

other EU member states and third countries (provided that these are non-SRB institutions), and investment firms.

#### Increased focus on resolution at institutions in Germany

In the meantime, progress has been made on anchoring the topic more strongly as a strategic focus at financial institutions and hence making it a priority for top management. By and large, senior managers at German banks have now recognised that they need to prepare their institutions extremely comprehensively for crisis scenarios. The unforeseen exogenous shock caused by the COVID-19 pandemic in 2020 underscored this again very vividly. In this situation, the resolution planning work performed since 2015 proved extremely helpful to the resilience of the financial system.

## 4.2 Ensuring resolvability and determining the MREL

An interactive process between the authorities involved and the individual institutions is needed in order to ensure the latter's resolvability. One of BaFin's main tasks is to document resolution planning by institutions domiciled in Germany. Resolution plans are documents that are not only standardised but also specifically tailored to reflect the particular features of the institution concerned, and that the authorities involved use in the case of resolution as a template for the steps to be taken.

Resolution planning focuses on developing individual resolution strategies that fit the business models concerned. When selecting the individual resolution strategy for an institution, BaFin always adopts the goal of avoiding the risk of contagion in the financial sector and the real economy. The resolution strategies selected are designed to continue critical functions, avoid negative impacts on financial stability and protect public funds and claims by customers and deposit holders.

In 2020 BaFin, as the supervisor directly or indirectly responsible, worked closely together with the institutions on implementing the individual resolution strategies: some institutions became significantly leaner during this process, e.g. by reducing their legal entities around the world. Another institution made extensive modifications from a company law perspective so as to ensure that the adopted resolution strategy could be implemented.

<sup>6</sup> See also 4.2 for details of the MREL.

Key elements of resolution planning include the minimum requirements for own funds and eligible liabilities (MREL) that BaFin sets for institutions using an administrative act; this also applies to those institutions for which the SRB is responsible.

The objective of resolution planning is to ensure resolvability by identifying potential impediments that could materially hinder the implementation of individual resolution strategies. Where significant impediments to resolvability exist, the institution must propose appropriate measures to remove them. Under European and national law, BaFin now has wide-ranging means of intervening to require institutions to remove substantial impediments to resolution, if necessary in the form of administrative acts.

The institutions are facing numerous challenges – the consequences of the coronavirus pandemic, global geopolitical uncertainty, digitalisation and related new players and financial market dependencies. Added to this is the associated pressure of having to constantly adapt and change their business models. In view of these problems, one task must be given a high priority: institutions must improve their resolvability (see info box) and hence enhance the financial system's ability to withstand crises.

At a glance

## Digital workshops on resolvability

In 2020, BaFin held digital resolvability workshops with the banks. These gave the latter important insights on how to identify and remove potential impediments to resolution.



V

# Inside BaFin





# 1 Who works for BaFin?

2,771 members of staff worked for BaFin at the end of 2020 (see Table 42). In a majority of cases, they had qualifications in law and administrative studies, economics, natural sciences and information technology. 69 employees were on long-term assignment to international institutions and supervisory authorities as at the 31 December reporting date. 36 of these had been seconded temporarily to the European Central Bank (ECB).

**Table 42: Employees**

As at 31 December 2020

Career level	Employees			of whom civil servants	of whom public service employees
	Total	Women	Men		
Higher civil service	1,376	569	807	1,236	140*
Higher intermediate civil service	850	383	467	693	157*
Intermediate/basic civil service	545	367	178	188	357
<b>Total</b>	<b>2,771</b>	<b>1,319</b>	<b>1,452</b>	<b>2,117</b>	<b>654*</b>
of whom in Bonn	1,929	916	1,013	1,500	429*
of whom in Frankfurt	842	403	439	617	225*
of whom candidates for the higher intermediate civil service/vocational trainees	35	17	18	13	22

\* Including those employees not covered by collective wage agreements.

**Table 43: Recruitment in 2020**

As at 31 December 2020

Career level	Qualifications						
	Total	Women	Men	Fully qualified lawyers	Economists	Mathematicians/statisticians	Other
<b>Higher civil service</b>	71	32	39	31	28	10	2
				<b>Business lawyers</b>	<b>Economists</b>	<b>Career training</b>	<b>Other</b>
<b>Higher intermediate civil service</b>	25	12	13	6	17	1	1
<b>Intermediate/basic civil service</b>	41	30	11				
<b>Candidates for the higher intermediate civil service/vocational trainees</b>	15	6	9				
<b>Total</b>	<b>137*</b>	<b>74*</b>	<b>63*</b>				

\* Excluding candidates for the higher intermediate civil service/vocational trainees.

BaFin recruited a total of 137 new members of staff in 2020 (see Table 43), 15 more than in the previous year. It will also advertise numerous open positions in 2021. One of the reasons for this is that lawmakers have entrusted it with performing new tasks.

Personnel management plays an extremely important role at BaFin. BaFin attracts and retains talented staff by offering employees attractive career prospects and wide-ranging areas of activity. Its responsibilities are complex and demanding, and many have an international dimension. What is more, the regulatory framework and the list of BaFin's responsibilities are constantly evolving. In addition, many members of staff work in interdisciplinary teams.

BaFin helps staff achieve a successful work-life balance, providing its own day care centres at both its locations. In addition, it permits teleworking<sup>1</sup> and enables staff to work from home<sup>2</sup>. BaFin radically expanded this offering following the outbreak of the coronavirus pandemic in order to protect its staff from infection and prevent COVID-19 from spreading.

### Expertise through CPD

In 2020, BaFin employees took part in 502 continuing professional development (CPD) events (previous year: 643 events). The total number of attendances recorded by BaFin during the year was 2,738 (previous year: 4,063). This means that, on average, each BaFin employee attended 1.9 days of CPD in 2020 (previous year: 2.7 days).

BaFin offers both recent graduates and experienced employees a wide range of CPD sessions. Joint training initiatives – above all with the Deutsche Bundesbank, the ECB and the European Supervisory Authorities (ESAs) – also promote closer collaboration and more effective international networking. In addition, BaFin is working to make its CPD formats even more flexible and to digitalise them.

BaFin's personnel development activities also systematically help its workforce to develop, both professionally and personally. Among other things, employees are offered specific induction programmes and have the opportunity to move to a higher career bracket, gain promotion or be deployed at an international level.

## 2 Budget

BaFin's Administrative Council approved a budget of €436.5 million for 2020. Planned expenditure for 2020 was therefore around €54.5 million higher than in 2019 (€382 million). This rise of approximately 14.3% was largely due to planned increases in personnel and IT expenditure.

Personnel expenses accounted for 64.3% of projected expenditure for 2020 (€280.8 million) and non-staff administrative expenses for 28.2% (€123.3 million). In the previous year, actual personnel expenses amounted to €246.1 million, while non-staff administrative expenses were €77 million. Capital expenditure totalled 5% of the 2020 budget (previous year: 4.4%). Cost reimbursements and grants accounted for 2.5% of the budget (previous year: 2%).

### Financing through cost allocations and fees

BaFin is independent of the federal budget and finances itself in full from its own income. The largest income item in the 2020 budget was composed of cost allocations levied on supervised undertakings – a statutory special levy with a financing function. The projected figure for this in 2020 totalled €414.5 million (previous year: €359.6 million). Otherwise, BaFin finances itself from administrative income such as fees. The projected figure for this item in 2020 was €22 million (previous year: €22.5 million).

The final cost allocation for 2019 was performed in the 2020 reporting period. Banks and other financial services providers accounted for 44.8% of total income from cost allocations in 2019. The insurance sector contributed 26.4% and the securities trading sector 21.6%. The share attributable to BaFin's activities as a National Resolution Authority amounted to 7.2%. The final cost allocation for 2020 will be performed in the course of 2021.

### Actual expenditure and income

BaFin's actual expenditure in 2020 was approximately €389.3 million (previous year: €345.3 million). Conversely, its income amounted to around €458.8 million (previous year: €386.5 million). BaFin's Administrative Council had not yet approved the 2020 annual financial statements at the time this Annual Report went to press.

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1 Option of working from home on predetermined dates, subject to certain conditions.

2 Option of working from home on flexible dates. BaFin specifies the maximum number of home office days per month.

### Separate enforcement budget

BaFin estimated the total cost of the separate enforcement budget to be €8.7 million in 2020 (previous year: €8.3 million). As in previous years, this included a planned cost reimbursement paid to the German Financial Reporting Enforcement Panel (*Deutsche Prüfstelle für Rechnungslegung*). This amounted to €6.2 million in 2020. In addition, the Federal Ministry of Finance (*Bundesministerium der Finanzen*) approved additional expenditure by BaFin for audits that became necessary but that were not contained in the separate enforcement budget. BaFin's actual expenditure on enforcement in 2020 was therefore approximately €9.1 million (previous year: €8.2 million). Income – including advance cost allocation payments for 2021 – totalled approximately €20.0 million (previous year: €15.7 million).

## 3 Compliance

### Rules on private financial transactions

BaFin has introduced stricter rules for employee transactions ahead of a planned change in the law. Since 16 October 2020, for example, employees in risk category A may no longer conduct any private transactions in shares or bonds issued by financial corporations that are domiciled or have branch offices in the European Union. They have also been forbidden to engage in transactions involving derivatives of such securities since that date. Risk category A covers all employees who have or could have knowledge of inside information by virtue of their official duties, i.e. due to the tasks they perform. This comprises 87% of all BaFin staff.

"I consider it extremely important that employees should avoid even the slightest appearance of a conflict of interests, and tightening the internal rules on employee transactions was and is therefore essential in view of the reporting about Wirecard", underscores Béatrice Freiwald, Chief Executive Director of Internal Administration and Legal Affairs. She also says that stricter rules are necessary to strengthen the compliance system overall, and not just because of events associated with Wirecard AG's insolvency.<sup>3</sup>

In a second step, lawmakers are planning to amend section 28 of the German Securities Trading Act

(*Wertpapierhandelsgesetz*). The draft German Financial Market Integrity Strengthening Act (*Gesetz zur Stärkung der Finanzmarktintegrität*) contains a proposal for this. As soon as the legislative process has been concluded, BaFin will adapt the internal rules governing its control system.

BaFin has had such an internal system, which it uses to monitor staff's private financial transactions, ever since it was founded. This is required by section 28 (previously section 16a) of the Securities Trading Act (see info box). The control mechanism comprises reporting requirements and a variety of different control options and is designed to ensure that employees who have (or could have) knowledge of inside information due to the tasks they perform in their work do not use this knowledge for private financial transactions. BaFin has appointed a Compliance Officer in accordance with section 28 of the Securities Trading Act who monitors private financial transactions and makes upgrades to the internal control system.

#### Definition

### "Section 28 of the Securities Trading Act – Monitoring the transactions of persons employed by BaFin

(1) BaFin must have adequate internal control mechanisms in place that are capable of preventing any infringement of the prohibitions under Article 14 of Regulation (EU) No 596/2014 by persons employed by BaFin.

(2) The supervisor or the person authorised by the supervisor can require BaFin employees to provide information and submit documents relating to transactions in financial instruments [...] that they have concluded for own account or for the account of or on behalf of a third party. [...] Employees who possess or may possess inside information in carrying out their official duties are obliged to notify, without undue delay, the supervisor or the person authorised by the supervisor in writing or electronically of any transactions in financial instruments [...] that they have concluded for own account or for the account of or on behalf of a third party. [...]"

<sup>3</sup> See also chapter I.2 for a further discussion of Wirecard.

### Special review of employee transactions

BaFin's Compliance Officer performed a special review to determine whether employees who had or could have had knowledge of inside information by virtue of their official duties, i.e. due to the tasks they perform in their work, illegally used this information for private transactions in financial instruments relating to Wirecard. Internal Audit assisted the Compliance Officer in this. In addition, BaFin commissioned a legal opinion and appointed an auditing firm to audit the special review. The review, which was launched in June 2020, had not been completed at the time of going to press.

## 4 Bodies and councils

BaFin is assisted and monitored in its work by a number of bodies and councils<sup>4</sup>.

- Administrative Council
- Advisory Board
- Insurance Advisory Council
- Securities Council
- Consumer Advisory Council

The Administrative Council monitors the management of BaFin and supports BaFin in the performance of its supervisory functions. It is also responsible for deciding on BaFin's budget.

The Advisory Board advises BaFin in the performance of its supervisory functions. In addition, it assists BaFin in the further development of its supervisory principles.

## 5 Communications

### 5.1 Press enquiries

BaFin received a particularly large number of enquiries from journalists in 2020.

#### Wirecard

The events relating to Wirecard AG were the dominant topic for the press in 2020. BaFin's media spokespersons answered approximately 1,500 media enquiries on this subject alone. The Aschheim-based company and former member of the DAX, which is now insolvent, is said to have manipulated its financial reporting for years. National and international media asked in particular why Wirecard AG – in contrast to the bank belonging to the group – was not under BaFin's supervision. Another common question was why BaFin did not examine the role played by the Financial Reporting Enforcement Panel more critically and why it did not take over the investigation of the company's financial reporting. Numerous other enquiries were also received in relation to the prohibition on short sales, to the content and status of market abuse investigations and to responsibilities with respect to anti-money laundering supervision.

#### COVID-19

Equally, a large number of enquiries were received in relation to the supervisory changes made by BaFin during the coronavirus pandemic.<sup>5</sup> BaFin's stance on distributing profits and dividends particularly interested journalists. However, a large number of enquiries were also received with respect to countercyclical capital buffers and on the cover for losses provided by business shutdown insurance.

#### Persistent low interest rates

Given the ongoing period of low interest rates, the media continued to look in detail at the situation of life insurers and *Pensionskassen* in 2020. Journalists were interested in the undertakings' financial situation and the supervisory measures planned or already taken, especially with respect to intensified supervision. In addition, a number of press enquiries related to the technical interest rate used by life insurers in their new business and to the future of the premium guarantee. The situation of the banks in the low interest rate environment was also the subject of a large number

<sup>4</sup> A complete list of the bodies and councils is available on BaFin's website at [www.bafin.de/dok/7859930](http://www.bafin.de/dok/7859930).

<sup>5</sup> See chapter I.1 for the measures taken by BaFin during the coronavirus pandemic.

of enquiries. For example, journalists were interested in how low interest rates were impacting the banks' economic position and how the banks were reacting to this.

### **Solvency II**

Another topic that generated considerable media interest was the ongoing review of the European Solvency II regime. The main focus here was on the measures relating to long-term guarantees (LTGs) and potential relief for insurers, e.g. as regards reporting.

### **PSD2**

A large number of journalists also requested information on the provisions of the Second Payment Services Directive (PSD2). Strong customer authentication in electronic payment transactions was a particularly popular subject. Information was also sought on the opening of account interfaces for third-party service providers, as well as on the current status of authorisation procedures for payment initiation service providers and registration procedures for account information service providers.

## **5.2 Events and trade fairs**

An extremely large number of trade fairs and stock exchange events in which BaFin would normally have taken part had to be cancelled due to the COVID-19 pandemic. The same applies to conferences and events normally organised by BaFin itself.

## **5.3 Publications**

As in previous years, BaFin issued a number of new publications on supervisory and consumer topics on its website, [www.bafin.de](http://www.bafin.de), in 2020. A few examples are given in the following.

### **BaFinJournal and BaFinPerspectives**

BaFinJournal provided regular information on current supervisory topics in 2020, as in the past. The monthly journal is published on [www.bafin.de](http://www.bafin.de). In addition, BaFin published another issue in its BaFinPerspectives series on 15 May 2020. In it, BaFin and the Federal Office for Information Security (*Bundesamt für Sicherheit in der Informationstechnik*) jointly addressed the issue of cybersecurity. The series is published on BaFin's website in German and English.

### **Brochures**

A large number of BaFin's brochures are aimed at consumers. In October 2020, BaFin published a brochure entitled "*Schule vorbei – Was junge Menschen über Geld wissen sollten*" ("School's out – what young people need to know about money") on its website. This is primarily aimed at young adults and explains what they need to take into account in their financial planning, including what products they definitely need and what risks they must expect.

### **Annual Report and statistics**

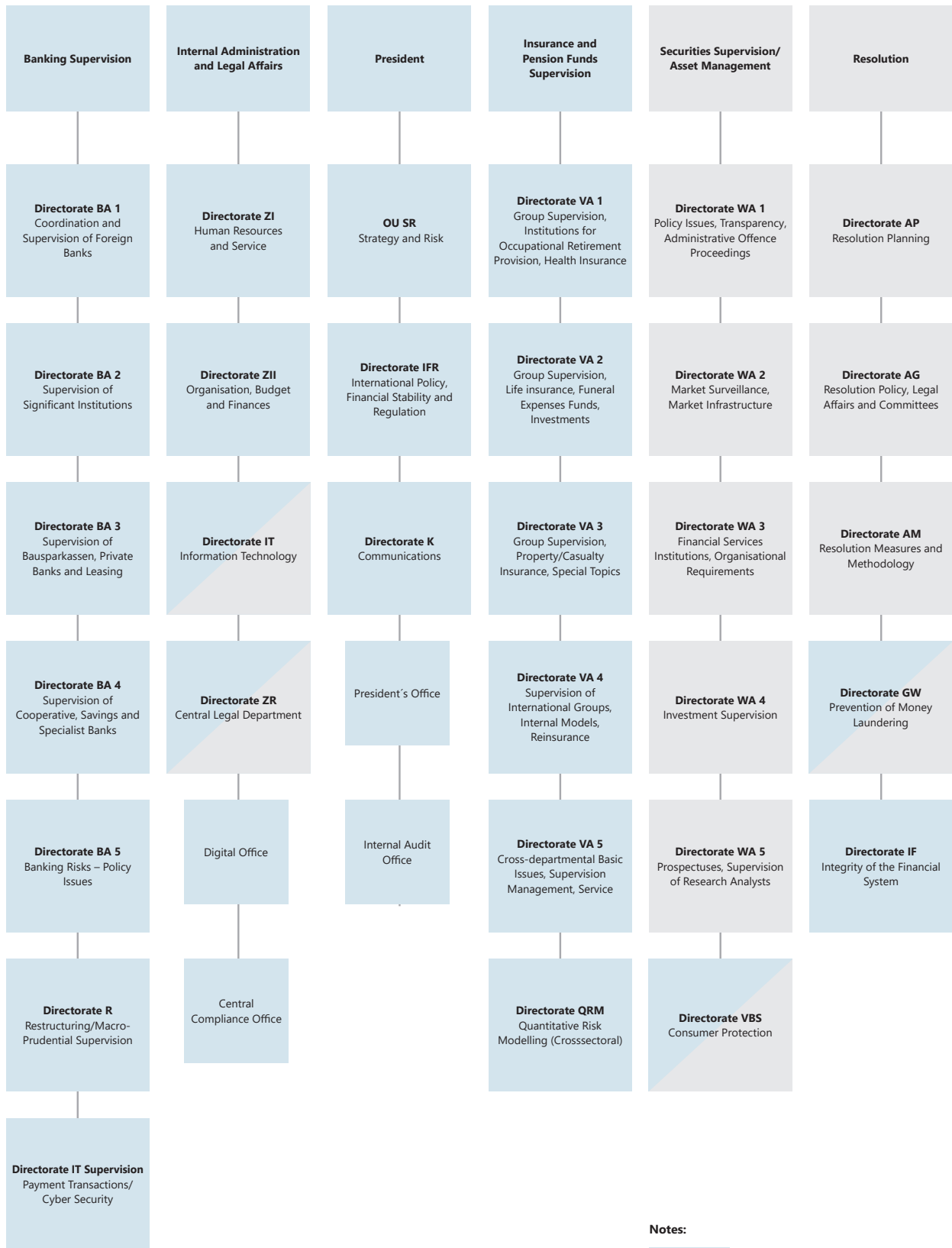
In addition to its Annual Report, which appears in German and English, BaFin published its annual statistics on the status and development of primary insurance undertakings and *Pensionsfonds*, plus its statistics on reinsurance undertakings, for the last time on its website at [www.bafin.de](http://www.bafin.de). BaFin will continue to make the information and data relating to these statistics available on the website. The reinsurance statistics were also published in English.



# Appendix



# 1 Organisation chart\*



**Notes:**

- Bonn office
- Frankfurt office
- Offices in Bonn and Frankfurt

\* A detailed organisation chart can be found on BaFin's website at [www.bafin.de/dok/7859566](http://www.bafin.de/dok/7859566). As at March 2021.

## 2 Complaints statistics for individual undertakings

For many years, BaFin published complaints statistics, broken down by insurance undertaking and class, in its annual reports. The Berlin Higher Administrative Court (*Oberverwaltungsgericht*) had ordered the Federal Insurance Supervisory Office (*Bundesaufsichtsamt für das Versicherungswesen*), one of BaFin's predecessors, to make this information available (ruling dated 25 July 1995; case ref.: OVG 8 B 16/94). Since 2019, the complaints statistics have no longer been published in BaFin's annual report. They are available on BaFin's website.<sup>1</sup>

The complaints statistics list how many complaints BaFin processed in full in 2020 for its Insurance Supervision Sector.

They do not state whether the complaints processed are justified, and hence are not indicative of the quality of the insurance business.

The number of complaints that BaFin processed in full in 2020 is compared with the number of policies in the relevant insurance class as at 31 December 2019 so as to give an indication of the size of the insurance business. The undertakings concerned report the data for their existing business. This focus on existing business does not adequately reflect the position of insurers that recorded strong growth in the reporting period (often newly established undertakings), because the statistics do not capture the increase in the volume of business that is the basis for the complaints over the course of the year.

In the life insurance class, the figure given for existing group insurance relates to the number of insurance contracts. The data for the existing health insurance business shows the number of natural persons with health insurance contracts, rather than the number of insured persons under the various premium scales, which is usually higher. As in the past, this figure is not yet entirely reliable.

The information on property and casualty insurance relates to the insured risks. Where undertakings agree group policies with large numbers of insured persons, this leads to a higher figure for existing business. 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*)), only the figures for existing business at insurers with gross premiums earned in 2019 of more than €10 million in the insurance classes or types concerned can be included. The tables do not provide any information on existing business ("n.a.") for undertakings falling below this limit in the individual insurance classes.

Insurance undertakings that do business in a listed class but for which no complaints were received in the year under review are not included in the relevant statistics.

Undertakings domiciled in other countries in the European Economic Area (EEA) were not required to submit reports to BaFin and therefore no data is provided for their existing business. However, the number of complaints is included in order to present a more complete picture.

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<sup>1</sup> [www.bafin.de/dok/8230614](http://www.bafin.de/dok/8230614).



### 3 Memoranda of Understanding (MoUs)

Banking Supervision		Banking Supervision		Securities Supervision	
Albania	2012	Mexico	2010	Dubai	2006
Argentina	2001	Moldova	2014	Estonia	2002
Armenia	2011	Nicaragua	2011	France	1996
Australia	2005	Netherlands	1993	Guernsey	2011
Belgium	1993	Norway	1995	Hong Kong	2018
Bosnia and Herzegovina	2016	Austria	2000	Iran	2016
Brazil	2006	Philippines	2007	Israel	2017
China	2004	Poland	2004	Italy	1997
Denmark	1993	Portugal	1996	Japan	2019
Dubai	2006	Qatar	2008	Jersey	2012
El Salvador	2011	Romania	2003	Canada	2003
Estonia	2002	Russia	2006	Korea	2010
France	1995	Sweden	1995	Croatia	2008
Finland	1992	Serbia	2011	Lebanon	2016
Georgia	2011	Singapore	2009	Monaco	2009
Greece	1993	Slovakia	2002	Poland	1999
United Kingdom (BE/FSA)	1995	Slovenia	2001	Portugal	1998
United Kingdom (SIB/SROs)	1995	Spain	1993	Ontario (Canada)	2018
United Kingdom (BSC)	1995	South Africa	2004	Qatar	2008
United Kingdom (PRA/FSA)	2019	Czech Republic	2003	Russia	2001
Guernsey	2011	Turkey	2011	Russia	2009
Hong Kong	2004	Hungary	2000	Switzerland	1998
India	2013	USA (OCC)	2000	Singapore	2000
Ireland	1993	USA (NYSBD)	2002	Slovakia	2004
Italy (BI)	1993	USA (Fed Board/OCC)	2003	Spain	1997
Japan	2019	USA (OTS)	2005	South Africa	2001
Jersey	2012	USA (FDIC)	2006	Taiwan	1997
Canada	2004	USA (SEC)	2007	Czech Republic	1998
Korea	2006	Vatican	2014	Turkey	2000
Kosovo	2011	United Kingdom	2019	Hungary	1998
Croatia	2008	Vietnam	2010	USA (CFTC)	1997
Latvia	2000			USA (SEC)	1997
Lebanon	2016			USA (SEC)	2007
Lithuania	2001			USA (SEC)	2020
Luxembourg	1993			Vatican	2014
Malta	2004			United Arab Emirates	2008
Macedonia	2011			Cyprus	2003
		Securities Supervision			
		Argentina	1998		
		Australia	1998		
		Brazil	1999		
		China	2019		

## Insurance Supervision

Egypt	2010
Australia	2005
China	2001
Connecticut (USA)	2011
Dubai	2006
Estonia	2002
Florida (USA)	2009
Georgia (USA)	2012
Guernsey	2011
Hong Kong	2008
Japan	2019
Jersey	2012
California (USA)	2007
Canada	2004
Korea	2006
Croatia	2008
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
Czech Republic	2002
Hungary	2002
USA (OTS)	2005
Vatican	2014

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# Imprint

## **Published by**

Federal Financial Supervisory Authority (Bundesanstalt  
für Finanzdienstleistungsaufsicht – BaFin)  
Directorate K (Communications)

Graurheindorfer Straße 108 | 53117 Bonn  
Marie-Curie-Straße 24–28 | 60439 Frankfurt am Main

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E-mail: [poststelle@bafin.de](mailto:poststelle@bafin.de)

Bonn and Frankfurt am Main | May 2020  
ISSN 1611-910X

**Editorial deadline:** The Annual Report covers the year  
2020. The exception is the spotlight on Wirecard (from  
page 27).

## **Editing**

Directorate K (Communications)  
Heimbüchel pr – kommunikation und publizistik GmbH

## **Design**

Werksfarbe.com, konzept+design, Frankfurt

## **Typesetting**

CMS – Cross Media Solutions GmbH

## **Printed by**

Druck- und Verlagshaus Zarbock GmbH & Co. KG

