

Welcome to the BREXIT-Workshop for Foreign Banks

TOP 1: Introductory Remarks

Objective of BaFin

being an integrated supervisory authority with responsibility for supervision of banking, insurance and securities / asset management



- to ensure the proper functioning, stability and integrity of the German financial system
 - reliable and professional partnership
 - minimising the operational risk with respect to and for institutions applying for a banking licence in Germany
 - compliance with existing prudential framework
 - honouring the institutional division of tasks in the SSM
 - taking into account banks' well established risk management and servicing processes
 - in good co-operation with UK authorities

General possibilities to conduct banking business in Germany

separate legal entity (subsidiary)

branch pursuant to § 53 KWG

- deemed to be a separate credit institution subject to equivalent prudential requirements
- relaxation of capital requirements / large lending limits for US/JAP/AUS branches by a regulation pursuant to § 53c KWG
- no possibility to use EU passporting procedures

branch of / cross-border services by EU bank pursuant to § 53b KWG

Supervisory responsibilities

Significant Institutions

Less Significant Institutions



Direct supervision
(Credit institutions established in partaking member states, on group-level)

Indirect supervision
(Disclosure of Regulations, directions and guidelines for supervisory practice, monitoring of NCA supervision, etc.)

Common procedures



Support of ECB supervision
(JST Members, expert support, On-site inspections, draft decisions, conduct ECB enforcement, etc.)

Direct supervision
(reporting obligation towards ECB)

non-SSM tasks (Money Laundering, Consumer protection, etc.)

Significant institutions according to Art. 6 (4) SSM R

Criteria	Significant Institutions	Less significant institutions
Size	<ul style="list-style-type: none"> ▪ Assets > € 30 bn ▪ Amongst three largest banks per country 	<ul style="list-style-type: none"> ▪ Assets < € 30 Bn ▪ Not amongst three largest banks per country
Economic relevance	<ul style="list-style-type: none"> ▪ Assets > 20% of GDP of member state (as long as > € 5 bn) ▪ Top 3 banks of member state ▪ Systemically relevant ▪ High interconnectedness ▪ High complexity 	<ul style="list-style-type: none"> ▪ Assets < 20% of GDP of member state (or < € 5 bn) ▪ Not top 3 banks of member state ▪ Not systemically relevant ▪ Low interconnectedness ▪ Low complexity
Cross-border activities	<ul style="list-style-type: none"> ▪ Significant cross-border activities 	<ul style="list-style-type: none"> ▪ No or minor cross-border activities
European stability Mechanism	<ul style="list-style-type: none"> ▪ Request for assistance from the EFSF or ESM 	<ul style="list-style-type: none"> ▪ No assistance from the EFSF or ESM

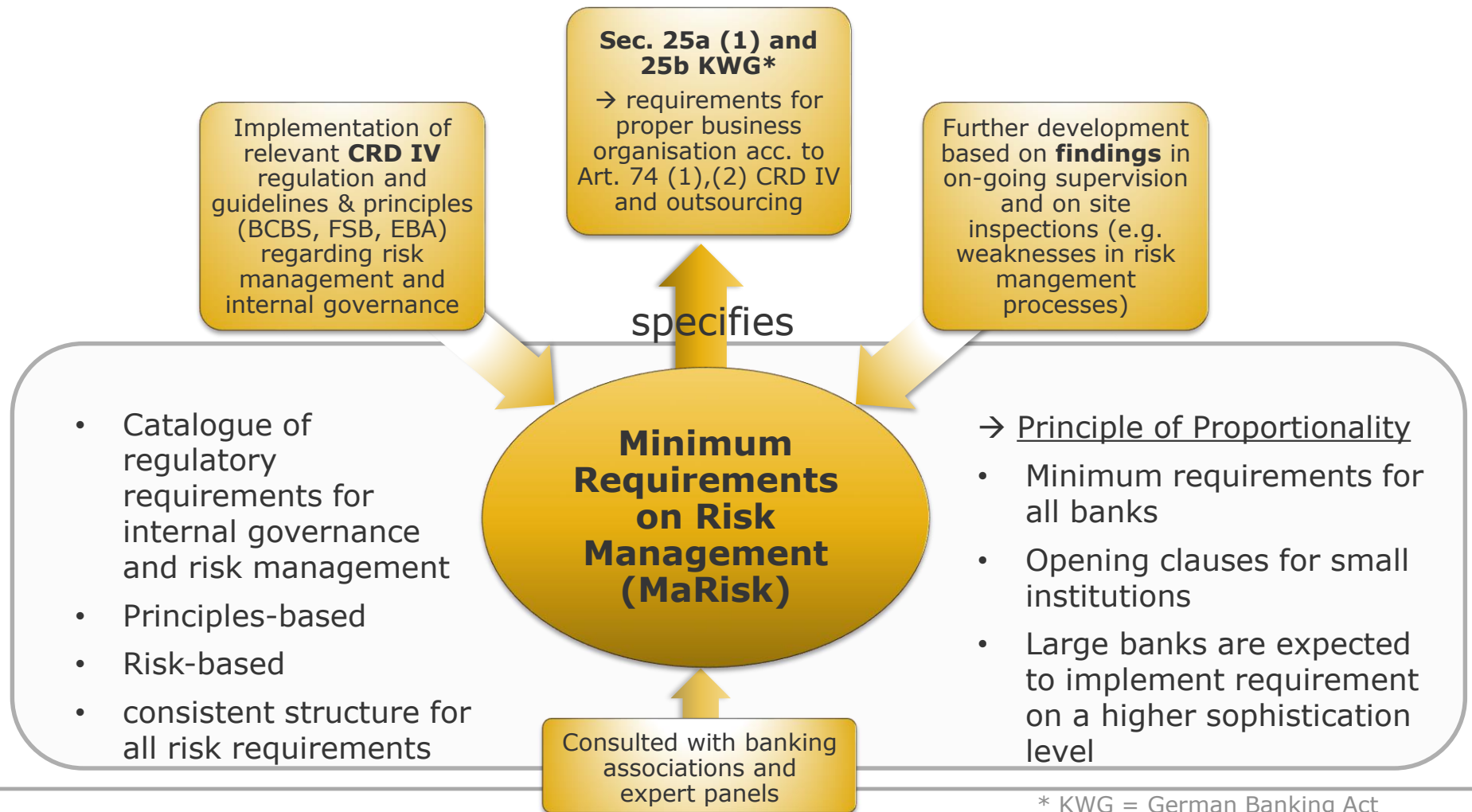
TOP 3: Minimum Requirements for Risk Management (MaRisk) – Outsourcing

I. Overview

II. AT 9 Minimum Requirements for Risk Management (MaRisk)

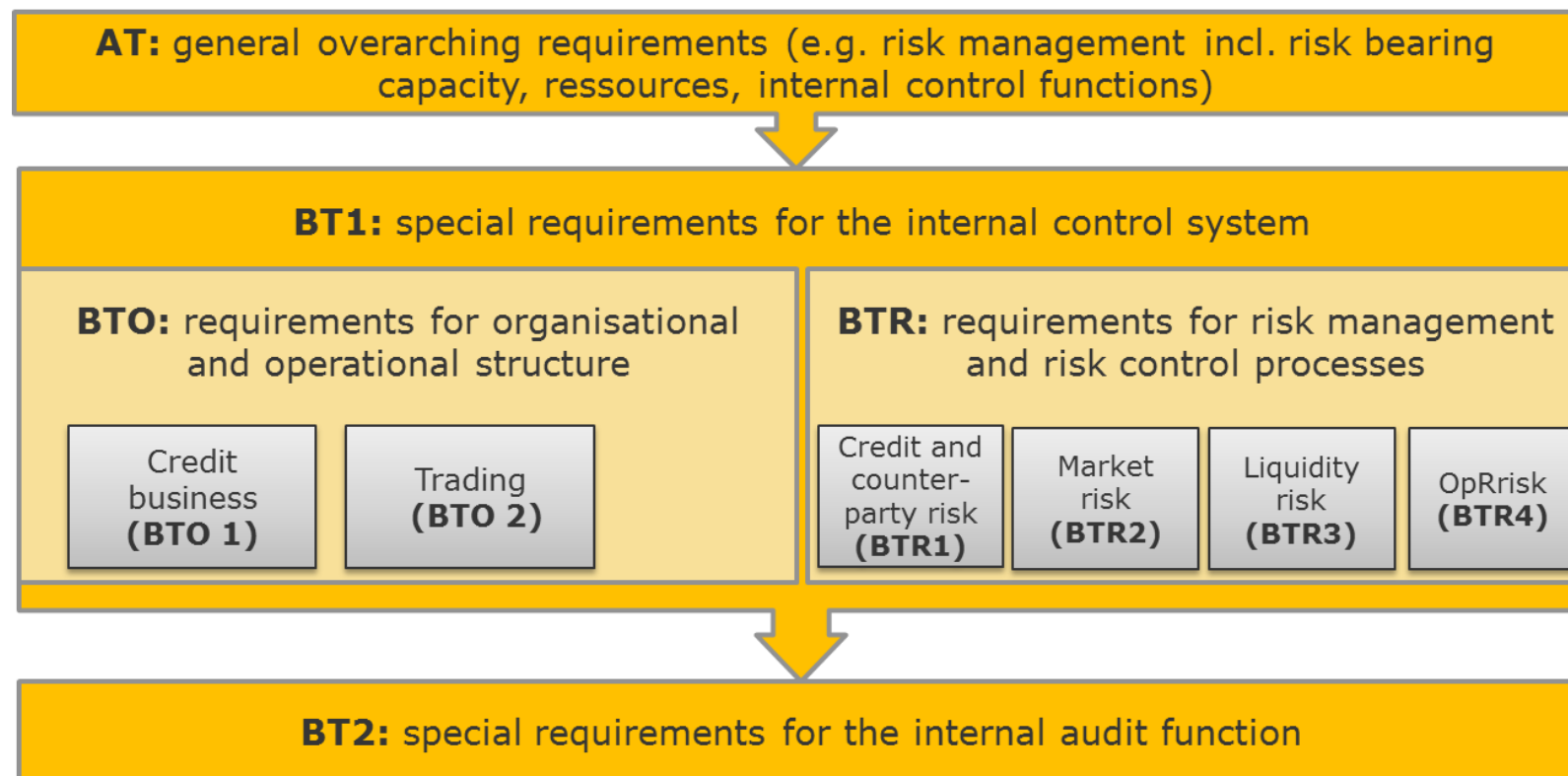
III. Assessment of compliance with (AT 9) MaRisk

I. Overview (1)



I. Overview (2)

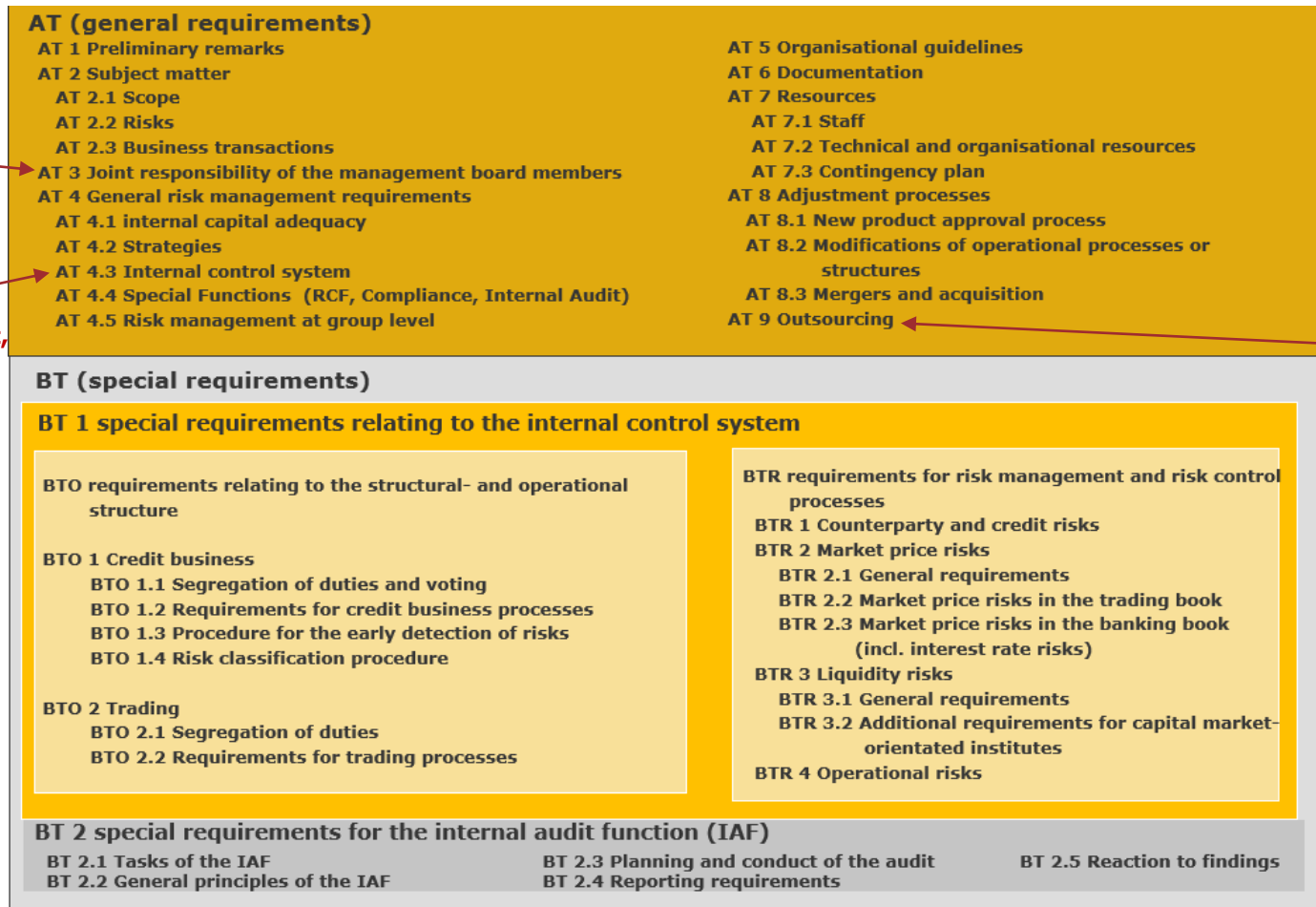
- From general to specific requirements → allows necessary adjustments without changing the whole structure



I. Overview (3)

- detailed overview

and most relevant updates 2016/2017



BT 3 special requirements regarding risk reporting

I. Overview (4)

- Sec. 25a KWG: general requirements for an adequate risk management
 - Sec. 25b KWG: general requirements for outsourcing of activities and processes, e.g.
 - make appropriate arrangements in order to avoid incurring excessive additional risks for activities and processes that are material
 - outsourcing shall not entail the delegation of management board responsibility to the external service provider
 - in case of outsourcing, the institution shall remain responsible for ensuring compliance with the legal provisions to be observed by the institution
- specified in MaRisk, with regard to outsourcing: AT 9 MaRisk
- No notification process in place in Germany

II. AT 9 MaRisk (1)

- In general, all activities and processes can be outsourced provided that the proper business organisation is not impaired, however no delegation of management's responsibility to the service provider
- Limitation of outsourcing:
 - No outsourcing of management's tasks
 - Sound knowledge and experiences have to be ensured in the institution, especially with regard to outsourcing of control functions and core banking units (aims at an effective monitoring of service provider)
 - Complete outsourcing of Risk Control function, Compliance and IR Complete is solely permissible at non significant subsidiary if superordinated institution is the outsourcing company
 - Complete outsourcing of Compliance and IR is also permissible at small institutions
- In case of complete outsourcing of control function the management board shall appoint a responsible officer for the respective function who shall ensure that the outsourced tasks are being properly performed

II. AT 9 MaRisk (2)

- Risk analysis on a regular and ad hoc basis → institution shall
 - determine independently, which outsourced activities and processes are material in terms of risk (material outsourced activities and processes)
 - analyse the risks related to outsourcing, especially operational, reputational, strategic and IT risks
 - take into account risk concentrations
- central outsourcing management (depending on institution's size and extend of the outsourced activities and procedures → applies especially for large banks) shall in particular
 - implement and further develop an appropriate outsourcing management system and corresponding control and monitoring processes,
 - create and maintain full documentation of outsourcings
 - monitor compliance with internal and statutory requirements for outsourcing,
 - coordinate and review the risk analysis conducted by the responsible units
 - draw up a report on material outsourcings at least once a year and make this available to the management Board

II. AT 9 MaRisk (3)

- Options for action in case of unintended or unexpected termination of outsourcing → institution shall
 - entail exit strategies, as far as is meaningful and possible;
 - ensure that the necessary continuity and quality of the outsourced activities and processes can be maintained or restored within an appropriate period of time
- Requirements for subcontracting
 - in the outsourcing contract: institution shall be given the right to reserve approval **or** it shall be specified when individual work and process steps may be subcontracted → at least it has to be ensured, that agreements between the institution's service provider with the subcontractor is in line with the original outsourcing contract
 - the service provider remains responsible for reporting to the institution

III. Assessment of compliance with (AT 9) MaRisk

- Nearly 20 years of experience with the application of supervisory principles covering bank internal processes and structures-> deep common knowledge base, no checklist
- On-site inspection acc. to sec. 44 (1) sentence 2 KWG / Art. 12 Regulation (EU) 1024/2013
 - BaFin may perform inspections at the institutions and superordinated undertakings, with or without a special reason,
 - BaFin may entrust the Deutsche Bundesbank with the task of carrying out such inspections;
- Part of the institutions annual accounts report
→ sec. 29 (1) sentence 2 no. 2 a KWG
 - The external auditor shall determine in particular whether the institution has fulfilled the requirements pursuant to sec. 25a (1) KWG
 - MaRisk specifies 25a (1) KWG therefore is also part of audit

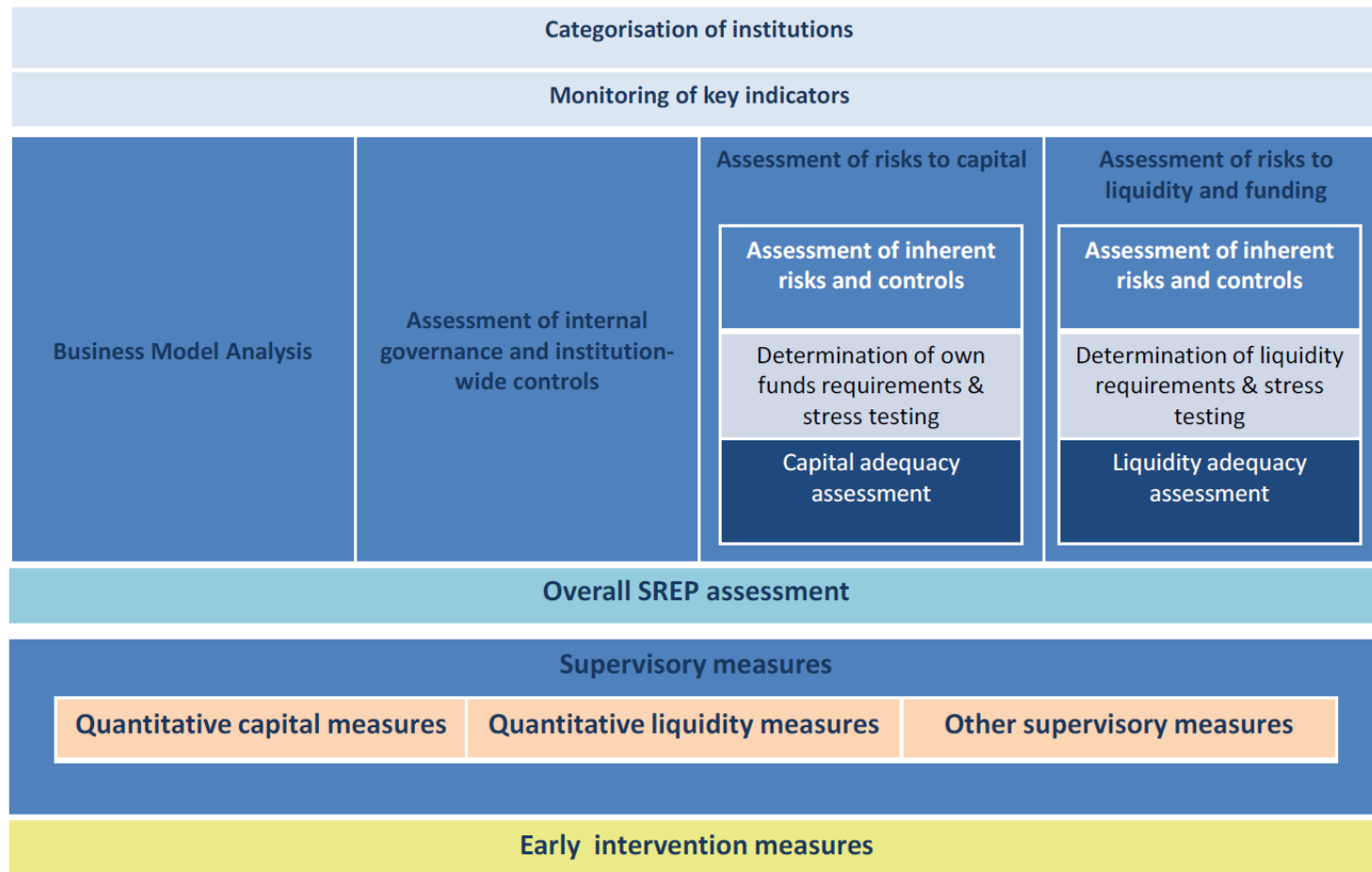
TOP 3: Supervisory Review and Evaluation Process (SREP)

1. Background
2. EBA Guidelines on SREP
3. National SREP
4. Outlook

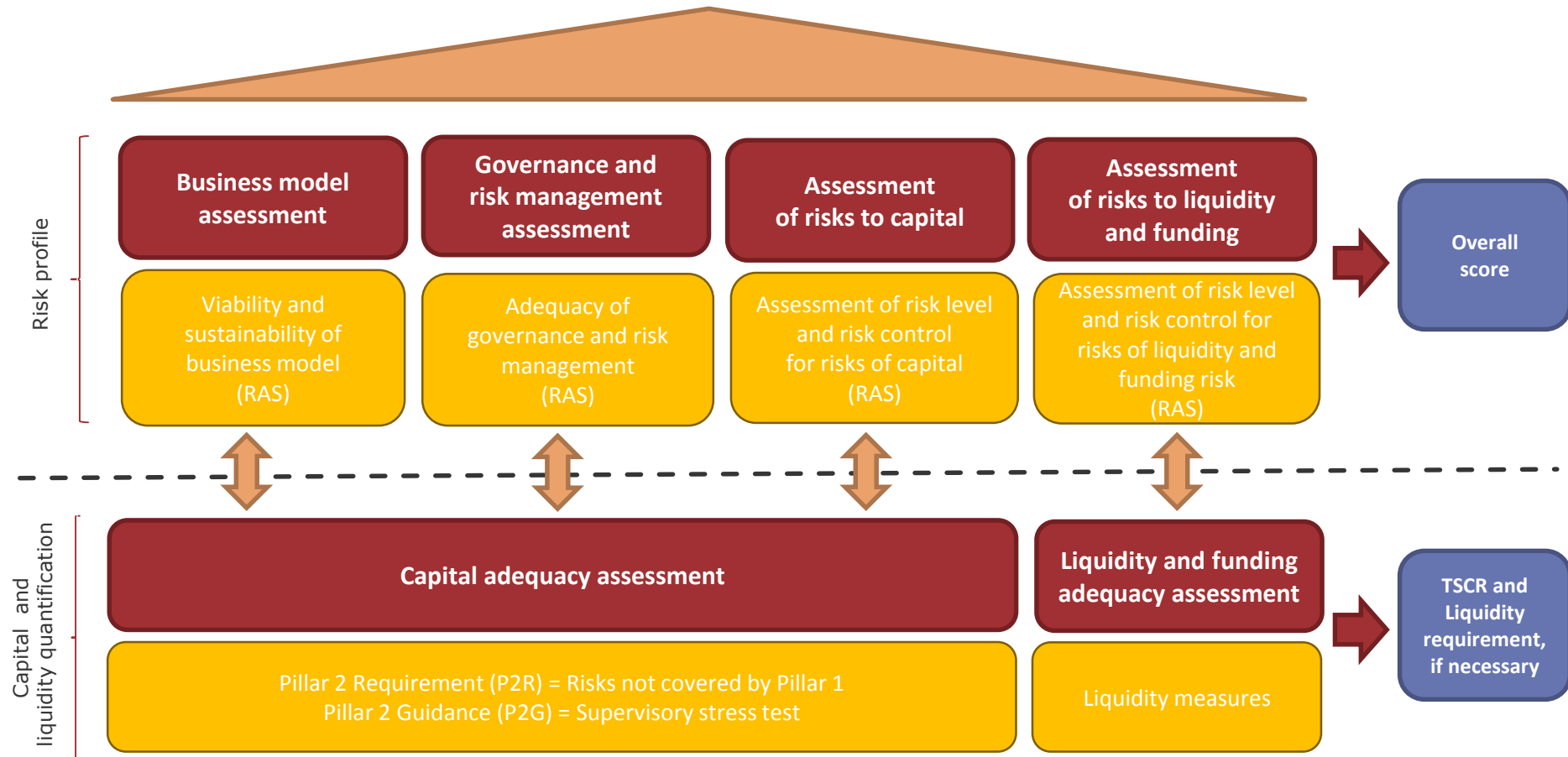
1. Background

- EBA published the guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) in December 2014
- Competent authorities are expected to apply these guidelines from 1 January 2016
- In the SSM-area, the ECB is in charge of the significant institutions (SIs) and the national competent authorities are responsible for the less significant institutions (LSIs)

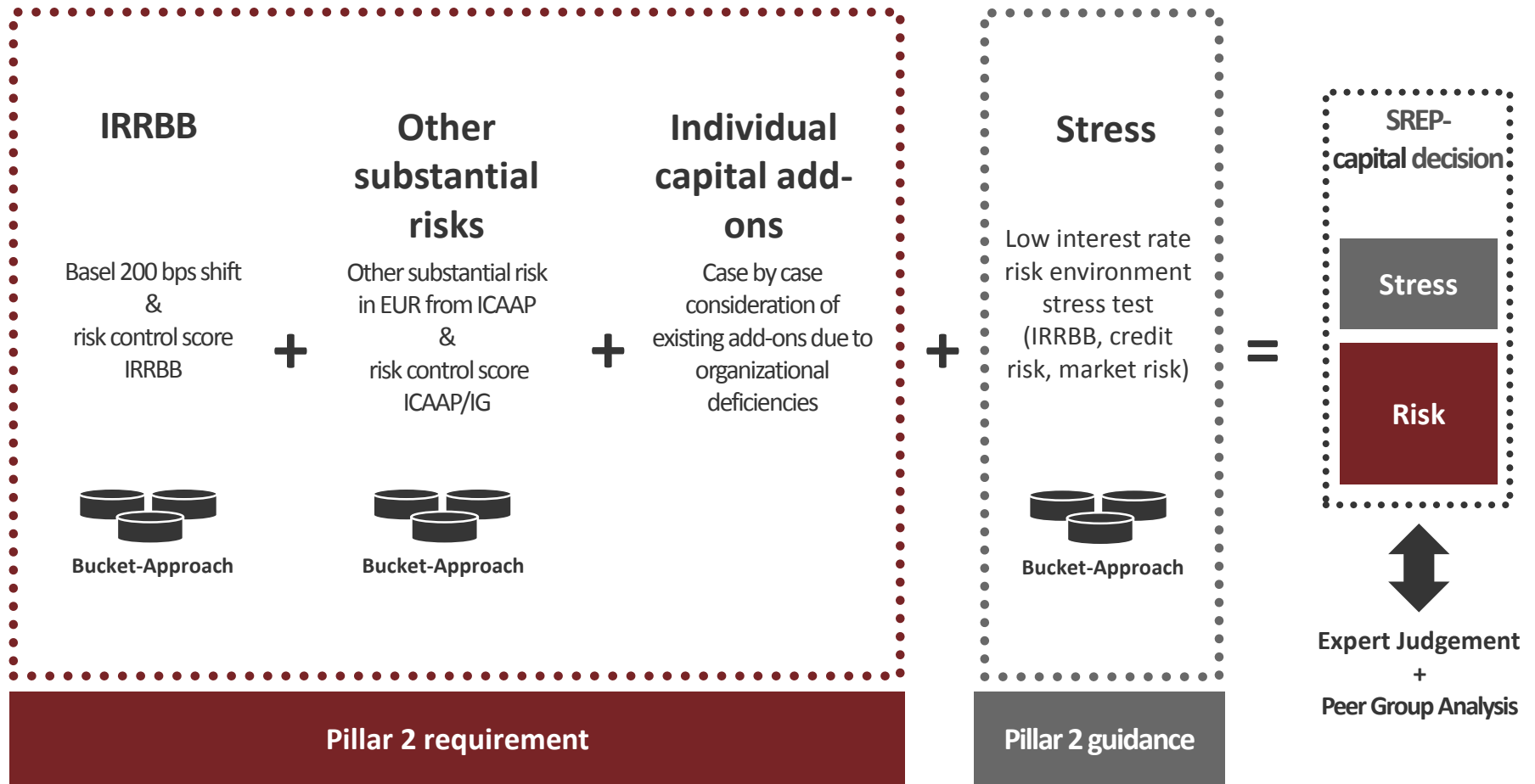
2. EBA Guidelines on SREP



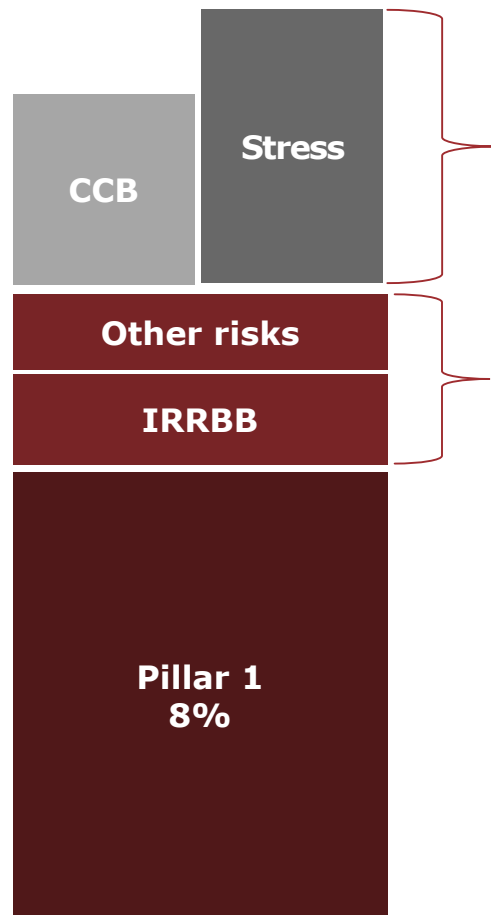
3. National SREP: Overview



3. National SREP: Pillar 2 Capital Determination



3. National SREP: Stacking Order



Pillar 2 guidance

- To cover losses under a stress scenario
- Early warning indicator, infringement leads to intensification of supervision

Hard Pillar 2 requirement

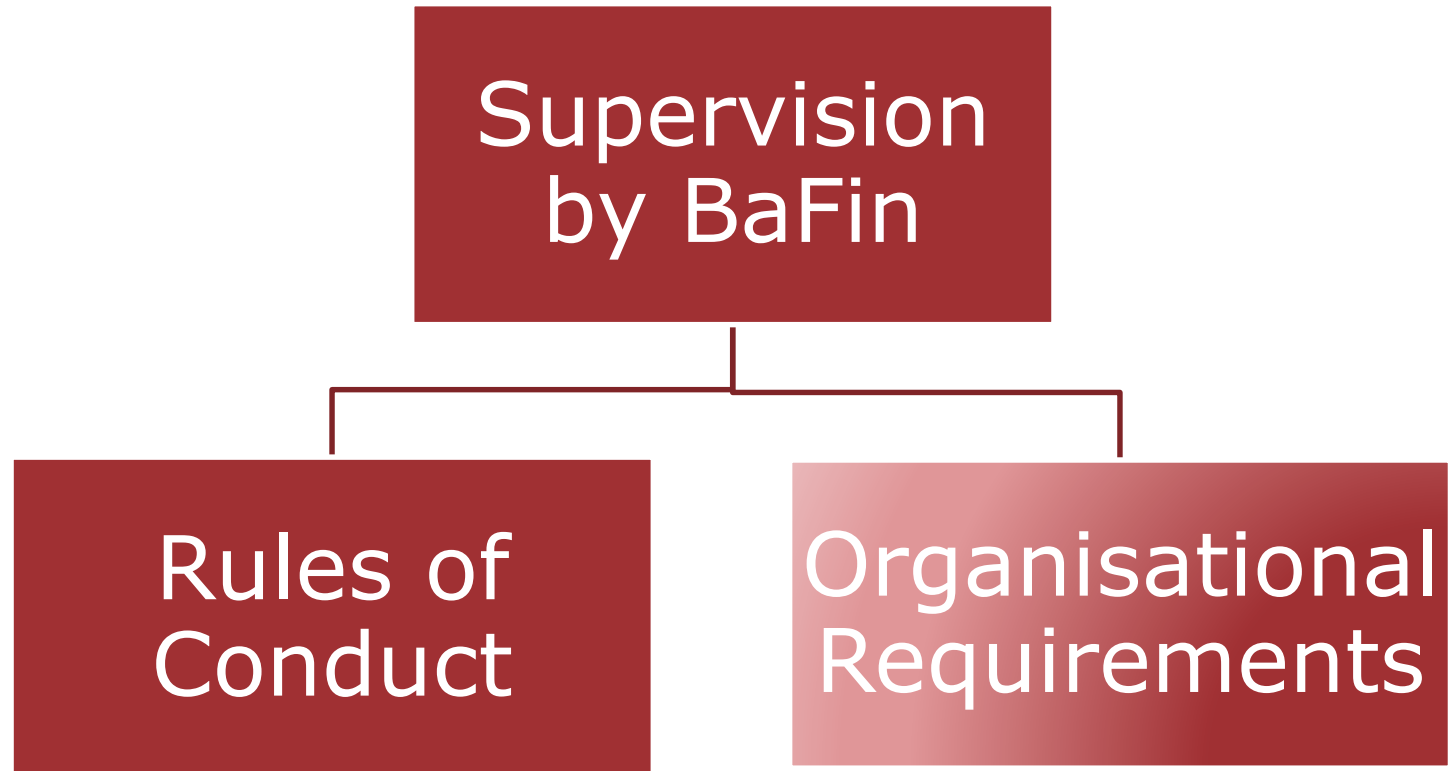
- Needs to be met at all times

4. Outlook

- ECB in collaboration with the competent authorities is currently elaborating a common framework of the SREP for the LSIIs in the SSM-area
- The starting point for application of these harmonised framework is presently approximately 1 January 2018

TOP 4: Compliance According to the WpHG

What would be new?



Directive 2004/39/EC of the European Parliament and of the Council (MiFID I)

Directive 2014/65/EU of the European Parliament and of the Council (MiFID II)

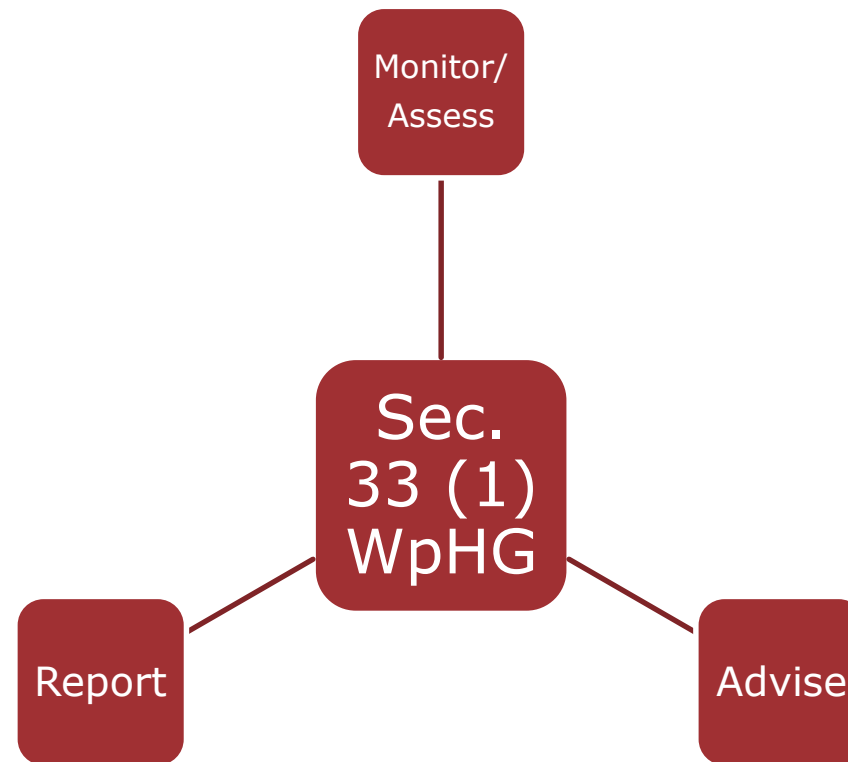


- Act implementing the Markets in Financial Instruments Directive (**FRUG**)
- Securities Trading Act (**WpHG**)
- Regulation specifying Rules of Conduct and Organisational Requirements for Investment Services Enterprises (**WpDVerOV**)
- Ordinance on the Examination of Investment Services Enterprises (**WpDPV**)
- Minimum Requirements for the Compliance Function and Additional Requirements Governing Rules of Conduct, Organisation and Transparency pursuant to Sections 31 et seq. of the WpHG for Investment Services Enterprises (**MaComp**)



English Version: www.bafin.de

Responsibility of Compliance



- Separation of Compliance-Division and Legal
- Seniority of COB
- Staff – amount and well-educated
- Contrast to MaRisk-Compliance
- Compliance: part of the annual external audits in the course of supervision
- Compliance-Culture
- Outsourcing

TOP 4: Impact on the Securities Prospectus Law

- Regarding the securities prospectus law two scenarios have to be distinguished:
 - 1. Great Britain leaves the EU but remains in the EEA
 - 2. Great Britain leaves the EU and the EEA („hard“ Brexit)

Brexit - Impact on the securities prospectus law

Scenario 1 - Great Britain leaves the EU but remains in the EEA



- Scenario 1 would have no impact on the area of securities prospectus law:
- The Prospectus Directive 2003/71/EC and the German Securities Prospectus Act (Wertpapierprospektgesetz, WpPG) apply to the EEA.
- Securities prospectuses which have already been approved and notified to other EEA supervisory authorities could still be used for an offer to the public or to admit securities.
- UK-issuers and third country issuers, who have chosen UK as their EEA home member state could still submit their securities prospectuses to the UK authority for the approval process.

Brexit - Impact on the securities prospectus law

Scenario 2 (1) - Great Britain leaves the EU and the EEA



- Scenario 2 would have far-reaching impact on the area of securities prospectus law:
- **Securities prospectuses** which **have already been approved and notified** to UK could no longer be used for an offer to the public or to admit securities in UK and vice versa.
 - Ongoing public offers, which are based on a notified securities prospectus must be stopped.
 - Securities which have already been admitted to trading on a regulated market retain their admission in UK and in the EEA.

Brexit - Impact on the securities prospectus law

Scenario 2 (2) - Great Britain leaves the EU and the EEA



- **New securities prospectuses** which have been approved in UK but which have not yet been notified could no longer be notified to other EEA supervisory authorities and vice versa.
 - New public offers in UK based on a notified securities prospectus would no longer be possible and vice versa.
 - New applications for admission to trading on a regulated market based on a notified securities prospectus would no longer be possible.
- The **exemption** according to **Art. 4 (2) (h) Prospectus Directive 2003/71/EC** could no longer be used. Pursuant to Art 4 (2) (h) Prospectus Directive 2003/71/EC the obligation to publish a prospectus for admission to trading shall not apply for securities which are already admitted to trading on another regulated market.

Brexit - Impact on the securities prospectus law

Scenario 2 (3) - Great Britain leaves the EU and the EEA



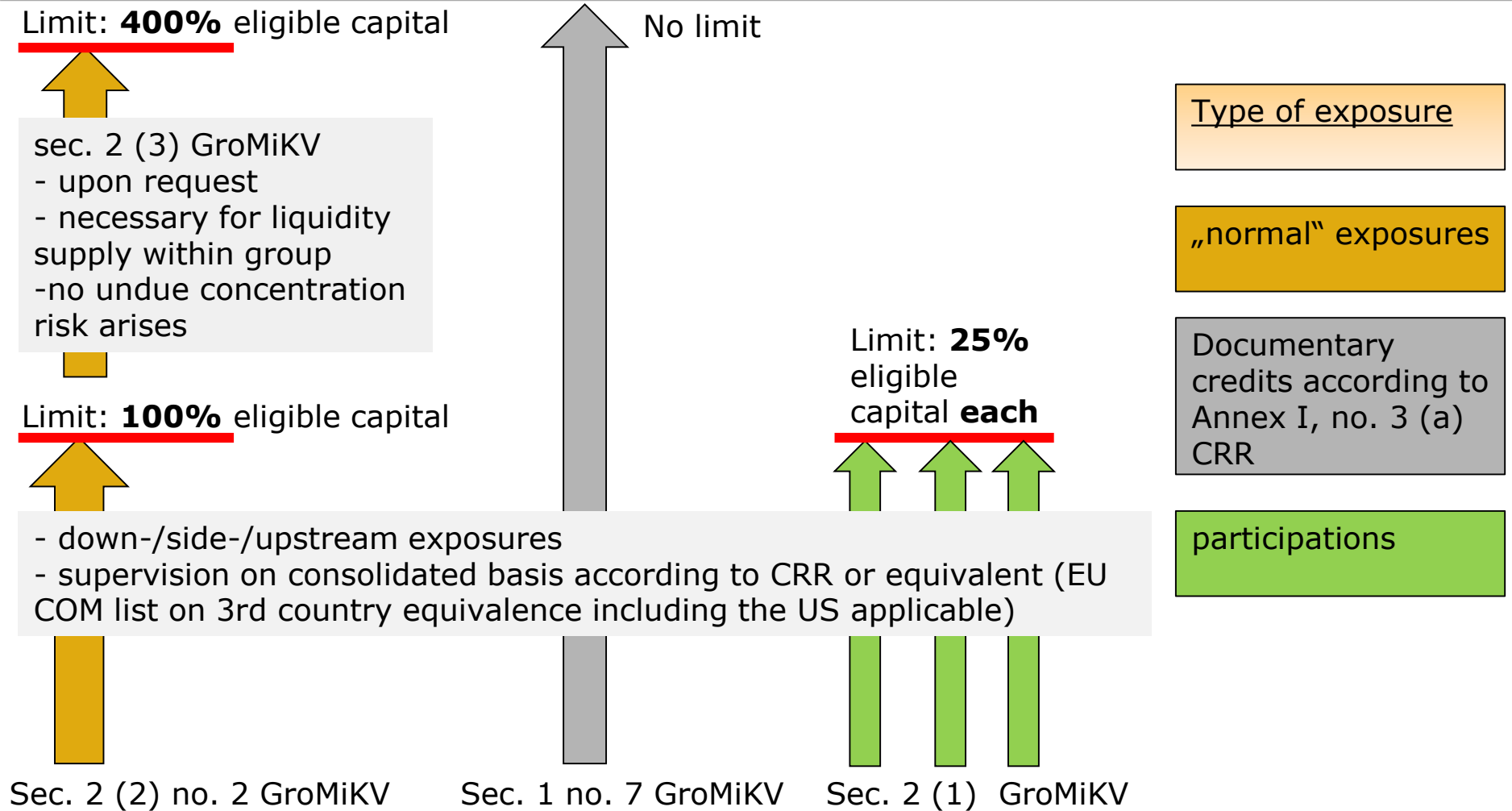
- Issuers who have their registered office in the EEA would have to draw up a **securities prospectus** in accordance with **UK law** if they would like to offer shares to the public in the UK or have their shares admitted to trading on a regulated market.
- UK-issuers and third country issuers who have chosen UK as their EEA home member state would have to draw up **new securities prospectuses** pursuant to the **Prospectus Directive 2003/71/EC** if they would like to offer shares to the public or admitted shares to trading in the EEA.
- UK-issuers would have to **choose a new supervisory authority in the EEA** for the approval of those securities prospectuses which should be used in the EEA.
- If BaFin shall be chosen as supervisory authority more information about the prospectus approval process at BaFin can be found on the website www.bafin.de/supervisory/securities and investment prospectuses. The information is available in German and English.

TOP 5: Large Exposures Regime

German LE regime: treatment of crossborder intragroup exposures

- Sec. 2 and 1 no. 7 GroMiKV implement Member States discretion of Art. 493 (3) (c) CRR and apply to significant and less significant institutions. The ECB implementation of the Competent Authority discretion of Art. 400 (2) (c) CRR does not apply, see Art. 9 (7) of ECB-Regulation (EU) 2016/445
- GroMiKV applies during the period mentioned in Art. 493 (3) CRR, i.e. until the entry into force of any legal act following the review in accordance with Art. 507 CRR, but not after 31.12.2028.

German LE regime: treatment of crossborder intragroup exposures



German LE regime: treatment of crossborder intragroup exposures

- Technical remark on wording - GroMiKV exemptions relate to exposure value: „When calculating the utilization of the LE limit exposures are disregarded for the amount of 75% / 93,75% of their value.“ This translates to limits of 100% / 400% of eligible capital.

Example:

- institution with eligible capital of 100 -> LE limit = 25
- maximum exposure value:
 - under sec. 2(2) is 100 (-75% (= 75) = 25)
 - under sec. 2(3) is 400 (-93,75% (=375) = 25)

CRR LE regime: „institution“ and equivalence

- Art. 391 CRR: exposures to a third country bank are only considered as exposures to an „institution“ in case of equivalence.
- relevant e. g. for Art. 390 (6) (d) CRR (provision of money transmission): intraday exposures to a third country bank (including a group member) only unlimited in case of equivalence.
- under BaFin practice the EU COM list on equivalence (Implementing Decision 2014/908/EU) may also be used for purposes of Art. 391 CRR.

TOP 6: Internal Risk Models

Internal Risk Models

– The Incentive

Calculating own funds requirements (RWA) with

an **internal risk model**

- risk sensitivity makes OFR proportional to economic exposure
- hedge trades can reduce RWA
- outputs compatible with use in daily risk management (quality pressure)
- establishing risk transparency
- implementation conceptually complex
- significant cost of implementation and production/maintenance
- needs to be tailored to the bank
- **BaFin's preferred solution**

the **standardised approach**

- no (very little) risk sensitivity
- no diversification or hedging effects
- not suitable for risk management purposes
- simple, basic operations of arithmetic
- conservative metric
- punitive to some products and business models
- can be bought off the shelf
- default/fallback solution, implementation mandatory (soon)

Internal Risk Models – The Challenge

- Banks have to seek approval to use their internal risk models
- Regulatory approval on basis of supervisory assessment
- Compliance with a multitude of quantitative and qualitative requirements
- Usually investigated through an on-site inspection with an in-depth analysis of
 - stochastic model
 - data quality, process maturity
 - governance, risk management (use test)
- As a result, the model approval process is comprehensive and elaborate, but also quite expensive and time-consuming.

Internal Risk Models

– The Veteran’s Advantage

- Supervisory approval itself is not transferable, but...
- in practice, rolling out an approved model to another entity is considerably easier than starting from scratch:
 - A bank applying to calculate RWA (solo) capital requirements for its foreign subsidiary with its approved group model does have a significant leading edge, if
 - the risk model has proven its adequacy for a similar portfolio
 - key processes have already been in place and operative
 - plenty of high-quality evidence for the quality of the model and its adequacy is readily available (performance history, validation reports, etc.)
- Key advantage to leverage the efficiency of the model approval process

Risk Oriented Supervision #1

– Focusing on the Essentials

- Minimum requirements for the internal model
 - output deeply integrated into risk management
 - internal model adapted to portfolio
 - model has to be fit-for-purpose
- Quantitative requirements
 - well-calibrated stochastic model
 - reliable valuation process
 - model validation, backtesting time series, P/L analysis
- Qualitative requirements
 - limit framework, risk reporting
 - governance, model risk transparency
 - default and collateral management processes
 - emergency procedures, business continuity plan

Risk Oriented Supervision #2

– Focusing on Materiality

- Portfolio complexity and size matter:
Scale of on-site inspection risk oriented
- Scope of trade migration predetermines
size of NewCo's "T+1 exposure"
- Big move or organic portfolio growth
- Adequacy of processes and governance
- Full back-to-back trading (1:1 identical hedges)
 - could eliminate market risk exposure
 - would not help with (counterparty) credit risk
- Starting with a low risk profile could back supervisor's rationale
of a temporary/phased/preliminary approval

Internal Risk Models

– Phased Model Approval Process

Brexit → approval decision under time pressure

Keeping supervisory balance:

- Equal treatment, maintaining level playing field
- Being reasonable, making allowances for Brexit being an external effect

Efficiency Measures

- Utilizing preparatory pre-application phase
- Leveraging on track record
- Targeted on-site phase
- Minimum requirements

Prudence

- “Tentative approval”
- Conditions and obligations
- Floors/capital add-ons
- Restricted scope of model usage
- Follow-up audits + intense model monitoring

Moving Target #1: Timing the Approval Process to the Brexit



Moving Target #2: Regulatory Requirements of 2019ff.

Topic	FRTB (Basel)	CRR proposal (EU COM)
Timeline	Adoption: January 2016 Entry into force: 1/1/2019 Application: end of 2019	Entry into force: 1/1/2019 at the earliest, (more likely: 1/7/2019 or later) Application: 2 years after entry into force of the respective CRD/CRR-package
Transition to new capital requirements	No phase-in period	Significant downward recalibration of FRTB capital requirements (35% capital reduction) with a review clause in three years' time, after which the Commission is entitled to prolong or adjust it via a delegated act (Art. 501b)
EU sovereign exposure	No explicit preferential treatment, but national discretion to assign a zero default risk weight (§137)	Reduced credit spread risk weights, zero default risk weights
EU covered bond exposure	No preferential treatment	Reduced credit spread risk weights
Proportionality measures for banks with only minor trading activity	No proportionality measures Rules were designed for internationally active banks	Derogation, i.e. banking book treatment allowed, for small trading books (Art. 94) Introduction of a simplified standardised approach (Art. 325a)

Internal Risk Model Approval – The Name of the Game

The greatest challenge to any thinker
is stating the problem in a way
that will allow a solution.

(Bertrand Russell 1872-1970)

TOP 7: Cross-Border Services Scope of MiFID License

1. Cross-border services

- Basics
- Market Targeting
- Passive Servicing
- Individual Exemption

2. MiFID

- CRD IV license vs. MiFID II license
- Some clarifications on MiFID ancillary services

- **MiFiD licensing requirements** are not regulated within Securities Trading Act (WpHG), but **in German Banking Act** ("Kreditwesengesetz - KWG") as "Financial Services"
- Sec 32 (1) KWG:

*"(1) Anyone wishing to **conduct** banking business or to provide financial services **in Germany** commercially or on a scale which requires commercially organised business operations needs written authorisation from BaFin. (...) "*

Cross-border Services

- Basics (2)-

- Exhaustive **catalogue of banking business and financial services** in sec 1 (1) and (1a) KWG – includes regulated activities from both CRD IV and MiFiD II regime as well as **specific domestic business types**, such as:
 - granting of money loans and acceptance credits (**credit business**);
 - ongoing purchase of receivables on the basis of standard agreements, with or without recourse (factoring);
 - conclusion of financial lease agreements in the capacity of the lessor and the management of asset-leasing vehicles (financial leasing)
 - purchase and sale of financial instruments separately from the management of a collective investment scheme Capital Investment Code for a community of investors, who are natural persons (...) (asset management).
- Almost identical requirements in Sec 8 (1) in Payment Services Supervision Act for Payment Services (“Zahlungsdiensteaufsichtsgesetz – ZAG”).

Cross-border Services

- Basics (3) -

License necessary for:

- local presence
 - subsidiary (sec 32 (1) in conjunction with section 33 (1) sentence 1 no. 6 KWG)
 - branch (sec 32 (1) in conjunction with section 53 KWG, including branches in the meaning of sec 53c KWG)
- cross-border services without local presence

No separate licensing requirements for:

- EEA-notified (“passport”) services, via branch (sec 53b (2) KWG) or cross-border (sec 53b (2a) KWG)
- Passive freedom of rendering services (including non-EEA countries)
- Representative offices (sec 53a KWG)
- Individual Exception by BaFin (sec 2 (4) KWG, post MIFiD II sec 2 (5) KWG)

Cross-border Services

- Market targeting -



Interpreting „conduct (...) in Germany“

1. Conduct („betreiben/erbringen“):
sufficient: incitement to file a serviceable offer/bid for one or more specific banking business or financial/payment services
and
2. in Germany (“im Inland”)
 - a) Relevant parts of this conduct must take place in Germany
and
 - b) intentional **market targeting at domestic clients**
(„zielgerichtetes Wenden an den dt. Markt“)
3. repeatedly and on a commercial basis
(“Wiederholt und geschäftsmäßig” / gewerbsmäßig)

Cross-border Services

- Passive Servicing -

MiFiD II 2014/65/EU, Art. 42: Provision of services at the exclusive initiative of the client

Member States shall ensure that where a retail client or professional client within the meaning of Section II of Annex II established or situated in the Union initiates at its **own exclusive initiative** the provision of an investment service or activity by **a third-country firm**, the requirement for authorisation under Article 39 shall not apply to the provision of that service or activity by the third country firm to that person including a relationship specifically relating to the provision of that service or activity. An initiative by such clients shall **not entitle the third-country firm to market** otherwise than through the branch, where one is required in accordance with national law, **new categories of investment products or investment services to that client.**

- Principle applied by BaFin on all banking business, Financial and Payment Services
- Prerequisite: no prior “market targeting”
- No entitlement for subsequent cross sales of different service categories in established customer relationships

Cross-border Services

- Individual Exemption -

De lege ferenda: Sec 2 (5) KWG after MiFiD II transposition as of Jan 23rd, 2017
(de lege lata: sec 2 (4)):

“Subject to the regulation provided for in Title VIII MiFiR (VO (EU) Nr. 600/2014), BaFin may, in individual cases, decide that sections 1a, 2c, 10 to 18, 24, 24a, 25, 25a to 25e, 26 to 38, 45, 46 to 46c and 51 (1) of this Act shall not apply as a whole to an institution established in a third country which intends to conduct banking business or to provide financial services in Germany commercially or on a scale which requires commercially organised business operations via cross-border servicing, as long as the undertaking does not require additional supervision by BaFin in respect to the business which it conducts in Germany due to its supervision in its country of origin. On the basis of an exemption pursuant to clause 1, BaFin may also decide that section 24c shall similarly not apply to the institution. Sentence 1 and 2 shall apply mutatis mutandis on institutes established in the EEA, for whom market access is not regulated in sec 53b (1)”

- Inofficial, non-binding translation. Only German legislative text is binding -

Legislative confirmation of established BaFin practice.
BaFin Practice is subject to changes and alterations

Questions in relation to the scope of MiFID raised in discussions so far

CRD IV license vs. MiFID II license

- Deposit taking vs. holding client money
- Lending business vs. granting credits or loans in accordance with Section B.1 of Annex I MiFID II

Questions in relation to the scope of ancillary services

- Holding client securities vs. administration of financial instruments for the account of client

Holding money as opposed to deposit taking

- Functional link between holding client money and provision of specific investment services
- Art. 16(9) MiFID II: Investment firm has to prevent the use of client funds for its own account
- In contrast, deposit taking is defined as:

Taking repayable funds from clients as deposits, regardless of whether or not interest is paid, unless the reclaim is securitised

Lending business vs. granting credits or loans in accordance with Section B.2 of Annex I MiFID II

- In both instances, a license for lending business is required
- Limited scope of Section B.2 of Annex I MiFID II
 - „[...] to allow him to carry out a transaction in one or more financial instruments [...]“
 - „[...] where the firm granting the credit or loan is involved in the transaction“

CRD IV license vs. MiFID II license

Holding client securities vs. administration of financial instruments for the account of client

- Provision of custodian business requires a license
- Holding of client securities for trading purposes, e.g. securities collected as margin, does not require a license for custodian business
- Administration of financial instruments involves the execution of clients rights (e.g. subscription rights or proxy voting)

TOP 8: Recovery Planning and German Bank Separation Act (GBSA)

- **German Recovery and Resolution Act („SAG“) and BRRD:**
 - All CRR credit institutions and CRR investment firms („institutions“) are required to draw up recovery plans
 - Recovery plans shall identify options to restore financial strength and viability when the firm comes under severe stress
- **Scope of application to foreign banks in Germany**
 - depends on whether an entity is a branch or a subsidiary of a foreign bank
 - and whether the foreign bank is established in European Union or in a Third Country

Recovery Planning Scope

German subsidiaries of ...

- **institutions established in the European Union**
 - **Individual recovery plan for subsidiary not required**
 - BRRD and SAG require Union parent undertaking to draw up group recovery plan
- **institutions established in Third Countries**
 - **Individual Recovery plan for subsidiary is required**
 - Irrespective of requirement for parent institution to draw up group recovery plan in its home jurisdiction

German branches of ...

- **institutions established in the European Union**
 - **Recovery plan for branch not required**
- **institutions established in Third Countries**
 - **Recovery plan for branch not required**
 - Such branches are not deemed to be CRR credit institutions or CRR investment firms under German law

- **Simplified obligations for recovery planning**
 - For institutions that are not potentially systemically relevant
 - Determination of eligibility for simplified obligations by BaFin and Bundesbank
 - Simplified obligations are expected to apply to vast majority of foreign banks
- **Content**
 - Simplified obligations will be set out in regulation issued by Ministry of Finance (expected Q 1 2017)

Recovery Planning Procedures and timing

Procedures

- Institutions are obliged to prepare recovery plans after they have received a written request from BaFin

Timing

- Simplified obligations: 12 months to draw up recovery plan
- Full obligations: within 6 months (possibility of further 6 months extension)

Support

- Recovery planning is an iterative process
- BaFin and Bundesbank offer support to institutions (e.g. institution-specific workshops)

German Bank Separation Act (GBSA)

Scope of institutions



- **CRR credit institutions or groups with a CRR credit institution**
 - The German Bank Separation Act (GBSA) covers all companies which fall under the scope of consolidation under sec. 10a KWG.
 - German CRR credit institutions which are subject to the licence requirement pursuant to sec. 32 (1) KWG (because of its business operations in Germany) with their consolidated subsidiaries and foreign branches
 - CRR credit institutions which are domiciled abroad but maintain a branch (sec. 53 KWG) or other physical presence in Germany/operate in Germany only by way of cross-border business (BaFin's Guidance Notice regarding the licensing requirements cross-border banking business) – however, limited to business operations in Germany!
 - EU passport entities and their branches and cross-border business (§ 53b KWG) are excluded
- **Materiality threshold**
 - „afs“ and „hft“ > 100 bn. Euro (absolute threshold) or
 - > 20% of total assets if total assets > 90 bn. Euro (relative threshold)
- **Whole consolidated or sub-consolidated group are affected**

GBSA

Prohibited transactions



- **Mandatory for all credit institutions or groups within scope**
 - Proprietary business as business on own account but not as a service for a third party („Eigengeschäft“)
 - Lending and guarantee business with hedge funds and other funds which employ a similar leverage (AIF)
 - High frequency trading (except market making)
- **Exemptions**
 - Transactions of the group to hedge positions with customers
 - Interest rate, currency or liquidity management
 - Long term shareholdings

- forbidden vs. allowed proprietary trading
- proprietary business as business on own account but as a service for a third party („Eigenhandel“)
 - allowed
- proprietary business as business on own account not as a service for a third party („Eigengeschäft“)
 - forbidden

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Legal Consequences



- The CRR credit institutions and groups affected by the provisions must identify prohibited transactions by means of a **risk analysis** within a period of six months (sec. 3 (3) sentence 1 no. 1 KWG)
- They must either **terminate** the transactions thus identified or else transfer them to a **financial trading institution (FTI)** within a further period of six months (sec. 3 (3) sentence 1 no. 2 KWG).
 - FTI must be economically, organisationally and legally independent (sec. 25f KWG). The Waiver Provision (Sec. 2a KWG) does not apply to the FTI.
 - FTI can
 - belong to a group of institutions, financial holding group or mixed financial holding group (sec. 10a (1) KWG)
 - use the infrastructure of the parent company or group companies or their services
 - use intragroup refinancing at arm 's length reflecting existing market conditions.
- In addition, under sec. 3 (4) KWG BaFin may require that further types of business – in particular, market making – be discontinued or transferred (**case-by-case decision**).
- conduct of banned high risk business can be sentenced with 5 years prison or a fine (sec. 54 (1) no. 1 KWG).

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BaFin's Interpretative Guidance



More than 50 FAQs, esp.

- scope
- definition of prohibited business activities
- organisational requirements for trading entity
- transitional processes

TOP 9: The Licensing Process in Germany

- 1. Responsibilities**
- 2. Applicable national law**
- 3. Licensing procedure**
- 4. Legal requirements**
- 5. Duration of the licensing procedure**

Articles 4(1)(a) and 14 SSM Regulation

- European Central Bank
- Federal Financial Supervisory Authority (BaFin) as National Competent Authority
- Deutsche Bundesbank (BBk) (§ 7 German Banking Act)

Art. 8 CRD IV and following

- § 32 German Banking Act
- § 14 Reports Regulation

Licensing procedure

BaFin

ECB

BaFin

Submission of application and documents	Assessment	Notification
Inform BBk and deposit protection scheme	Additional information	Monitoring
Completeness check	Complete draft decision	
Assessment	Approval Supervisory Board	
Proposal for draft decision	Approval Governing Council	

1. Specification which of the **banking services** the license shall cover
2. **Suitable evidence of the resources** required for business operations
3. At least two **managing directors**
 - Professionally qualified (adequate theoretical and practical knowledge of the business concerned and managerial experience)
 - Trustworthiness
 - Sufficient time to perform their duties

4. **Viable business plan** (planned business, organisational structure, planned internal control procedures)
5. Names of the **holders of qualified holdings** (amount, trustworthiness, annual accounts for the last three financial years, structure of group and the consolidated accounts for the last three financial years)
6. Evidence indicating a **close link** between the institution and other natural persons or other undertakings
7. **Members of the administrative or supervisory body** (trustworthiness, expertise, sufficient time to perform their duties)

- Presumed duration of the licensing procedure: 6 month (§ 33 para. 4 German Banking Act)
- Depending on the complete documentation for the application

Thank you very much for your attention!
