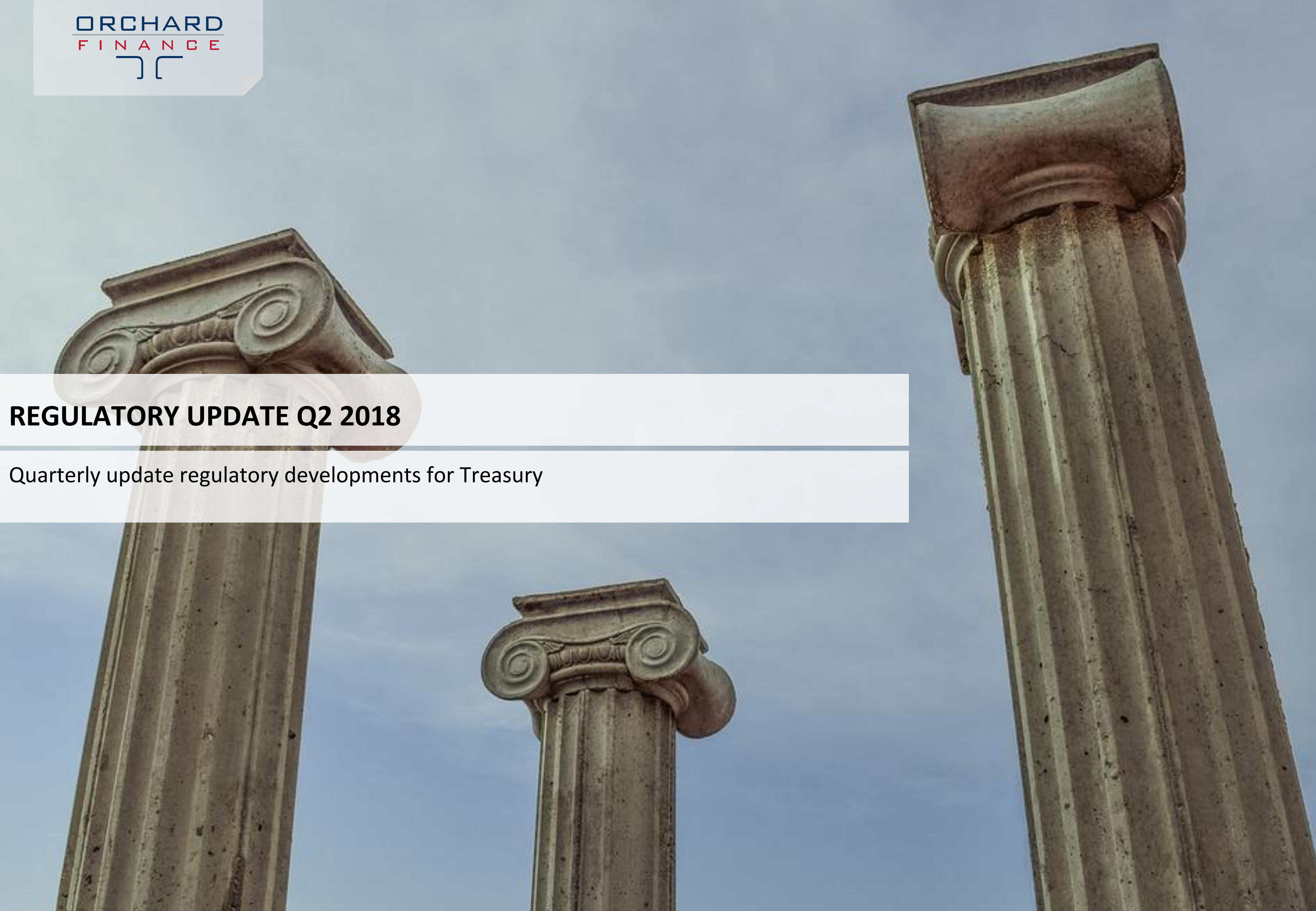


REGULATORY UPDATE Q2 2018

Quarterly update regulatory developments for Treasury

INTRODUCTION

Q2 2018

- In the Regulatory Update we highlight relevant regulatory developments in the financial industry and other relevant legislation potentially impacting the Treasury department.
- The regulatory update is based upon our latest insights on selected regulations and related (technical) publications. We provide qualitative insights regarding the impact on Treasury.
- Content of this update outlined on the right
- For more information, please contact us at info@orchardfinance.com

Content Regulatory update

Regulatory spotlight for Q2: PSD2

Key developments during Q2
(incl. PSD2, EMIR II, Benchmarks)

Time frame

Legislation

Q2 REGULATORY SPOTLIGHT: PAYMENT SERVICE DIRECTIVE 2

Introduction

Technological developments are a key driver for updating the Payment Service Directive from 2007. PSD2 is a directive and requires adoption into national legislation. It should have been implemented in the Netherlands on January 13th 2018, but the revised proposal is still awaiting to pass parliament. PSD2 introduces Account Information Service Providers ("AISP") and Payment Initiation Service Providers ("PISP") which are regulated entities enabling open banking based on Access to Account ("XS2A"). With AISP and PISP licenses the Licensee is able to obtain information regarding the counterparties' (including consumers) bank accounts when the counterparty approves this, or the Licensee is able to initiate payments when consent is provided. This changes the payment landscape radically and developments should be monitored closely in order to be able to benefit from PSD2.

Status

Netherlands and Belgium did not meet the regulatory deadline, other countries did meet the deadline and have granted PSD2 licenses which they can utilize across the European Economic Area based on Freedom of Services and passporting. From July 6th, the license application can be filed in the Netherlands and there are a multiple payment service providers ready to jump into the market.

Treasury

As PSD2 is a key regulation in the payments area, this needs to be monitored closely. Although it is credited to be a jeopardy as well as an opportunity for banks, Treasury can be impacted directly as well as indirectly. PSD2 developments are closely linked with other regulatory developments like GDPR and Instant payments.

Some developments that are expected

- Increased supply of multibank portals, allowing to get all bank information in 1 portal
- Fintech companies providing regulatory services to facilitate AISP and PISP functionality
- Corporates applying for AISP and PISP licenses for external and internal purposes
- Cyber security increasingly important with XS2A and Strong Customer Authentication
- Structuring Consent Management
- Regulatory interpretations on Payment Factories

KEY DEVELOPMENTS Q2

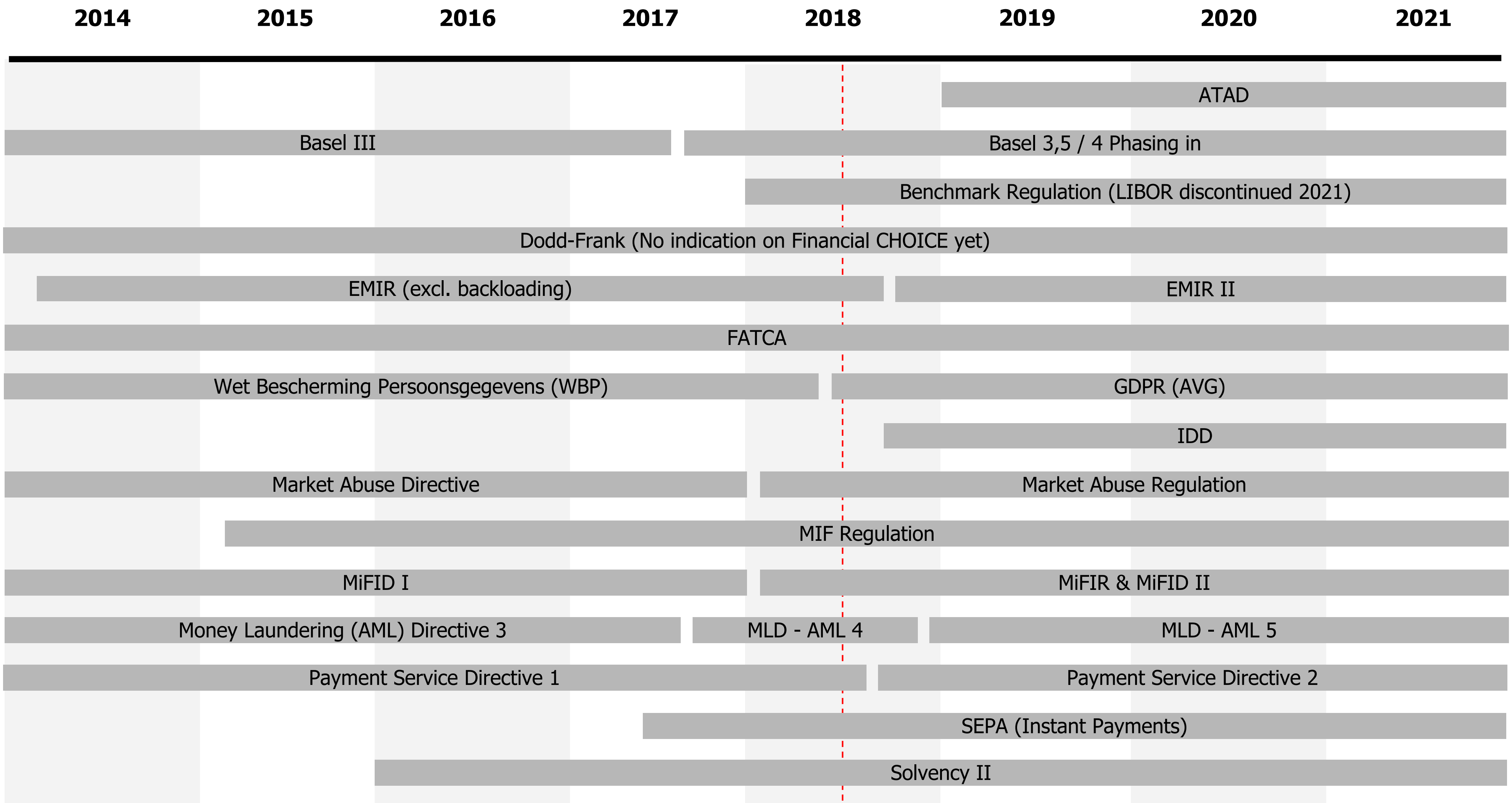
Key developments Q2

- PSD2 has been delayed in the Netherlands and is not expected until mid Q3 (IDD delayed as well)
- GDPR went live
- EMIR II text has been agreed in DRAFT format in May, legislation will be finalized shortly in “Trilogues”
- Working group on Risk Free Rate established as EONIA and LIBOR do not qualify for benchmark regulation
- AML 4 in process of implementation

Other selected (regulatory) developments that require monitoring

- Brexit
- Blockchain / ICO / Cryptocurrency regulation
- RegTech solutions for Identity Management - KYC - Fraud - Sanctions
- New IFRS regulation (e.g. IFRS 16)

TIME FRAME



This does not consider impact of phased in or hybrid processes

REGULATORY UPDATE (1 / 5)

Regulation	Date	Description
Anti Tax Avoidance Directive (ATAD) **BEPS**	1-1-2019	Anti Tax Avoidance Directive is EU legislation effectively implementing (part of) the OECD guidelines of Base Erosion and Profit Shifting ("BEPS"), which will ultimately be implemented in the Netherlands as per 1-1-2019. ATAD goes beyond mere transfer pricing considerations as substance, economic rationale, and documentation of the mentioned considerations also need to be in line with taxation. The Dutch government confirmed a Controlled Foreign Company ("CFC") regime on passive types of income (e.g. dividends, interest, financial lease income, royalties) for CFCs in Low Tax Jurisdictions is expected. The Switch-over clause from BEPS has not been included as political agreement was not reached on this point. Treasury: Especially when CFCs are present, it is important to consider how the elements of substance, economic rationale and documentation are met. It is therefore recommended to analyse transfer pricing policies and underlying processes.
Basel	Basel III 1-1-2013 Basel IV proposal 7-12-2017	Basel III is a comprehensive set of measures developed by the Basel Committee on Banking Supervision, to strengthen regulation, supervision and risk management of the banking sector in a 3-pillar approach. These measures aim to: improve the banking sector's ability to absorb shocks arising from financial and economic stress, improve risk management and governance, and strengthen banks' transparency and disclosures. Basel IV as proposed on 7/12/2017 is an enhancement of Basel III taking lessons learned into account, limiting a.o. the internal models in operational risk as well as credit risk and is to be implemented fully before 2027. Treasury: Basel III is considered to have had a negative impact on credit availability with associated costs and spreads. As the regime is risk-based the nature and tenor of their depository business is included in pricing. Notional cash pooling is being scrutinized due to Basel capital requirements. Basel IV is expected to increase required capital for low risk loans as standard model is a floor for internal model (limiting risk sensitivity), and is expected to increase required capital further to limit systemic risk.
Benchmark Regulation	1-1-2018	Due to several incidents in LIBOR and commodity indices, it was deemed to be critical to ensure the integrity of these indices with regulation for a well functioning EU capital market union. The Benchmark Regulation is applicable since 1-1-2018 and will be phased in actively in the next few years. LIBOR for instance will not be actively pursued by the FCA in UK from 2021 onwards. Within EU it however is still unsure which reference rate would need to be used as EONIA does not comply (yet). SONIA in UK and SOFR in US have been evaluated to comply with the benchmark regulation. Treasury: To prevent any impact when rates would need to be changed (or a switch is to be made) it is recommended to identify any direct LIBOR exposure and phase out reference rates to rates that comply with the Benchmark Regulation.

REGULATORY UPDATE (2 / 5)

Regulation	Date	Description
Dodd-Frank **Incl. "FCA"**	21-7-2010	Supervision of financial institutions, increasing transparency of financial system. Enforcing compliance with consumer financial laws, stringent regulatory capital requirements, changes in the regulation of OTC derivatives, reform regulation of credit rating agencies. Trump administration is targeting Dodd-Frank to be scaled down, the Financial CHOICE ("The Financial Creating Hope and Opportunity for Investors, Consumers and Entrepreneurs Act" or "FCA"), is supposed to be relieving part of the regulatory burden. It however still needs to pass the Senate, which is expected to be challenging. The SEC would experience significant changes in the proposal and some Basel III requirements which are included in Dodd-Frank would be relieved should the leverage ratio above the threshold. Treasury: Financial CHOICE Act is intending to provide more room for innovation, less costs for (investment) banks and reduce the regulatory burden, which could ultimately transfer to corporates. It still not expected to become law on short notice.
EMIR **Incl. "EMIR II"**	EMIR 16-8-2012 EMIR II proposal 3-5-2017	EMIR introduced requirements aimed at improving the transparency of OTC derivatives as well as reduce systemic and counterparty risk. EMIR requires that OTC derivatives meeting certain requirements are subject to the clearing obligation and for all OTC derivatives that are not centrally cleared that risk mitigation techniques apply. In addition, all derivatives transactions need to be reported to Trade Repositories (TRs). EMIR II proposed after the REFIT program introducing Small Financial Counterparties and reducing threshold for clearing. Next to that, the responsibility of reporting is proposed to shift to the financial counterparties and access to clearing is proposed to be improved. In Switzerland "FinfraG" is introduced, which is very similar to EMIR II but incorporates some elements from MiFID II and MAR as well. Treasury: Most corporates have an NFC- status (when NFC+, this should be known) and requirements are limited to risk mitigation and reporting to a TR. Impact Assessment of REgulatory FITness on EMIR made a few recommendations, which are reducing the regulatory burden, as it is proposed to remove the reporting obligation for intragroup and shift reporting responsibility to the Financial Counterparty (both for NFC-) It is recommended to review current reporting processes and determine whether the organisation could potentially benefit. Is not expected before Q4.
FATCA	3-1-2010	Tax regulation aimed to ensure that US taxpayers that hold funds outside the US, correctly report to the IRS. Foreign Financial Institutions are obliged to inform US Tax authorities. TC are exempt but status need to be confirmed and FI need to be informed on the status to avoid withholding tax. Treasury: Treasury needs to report the status of the corporate by filling in specific forms (for instance when opening new bank accounts). This form will be checked by the bank and the bank will determine whether the corporate is exempt from the regulation. Due to the frequency of filling new forms, automation solutions have been created. IRS is targeting payers to identify whether filings have been made correctly. Existing process, but continues to be considered to be a time consuming task.

REGULATORY UPDATE (3 / 5)

Regulation	Date	Description
GDPR	25-5-2018	GDPR is the most quoted legislation in Q2. Although this has been coming for a couple of years, the last months before implementation are when most work is being done. In the Netherlands this is also known as the "Algemene Verordening Gegevensbescherming", and is far reaching legislation requiring organisations to change the way they operate with respect to data. Should it be determined that an organisation has been acting negligent with privacy sensitive data larges fines are possible, but reputational damage could be even bigger.
		Treasury: GDPR is regulation which is important in a very broad context, and thereby also includes Treasury, a.o. the Privacy Officer should be known to Treasury as well as the reporting process for data breaches. Overall, a general awareness for cyber and privacy risks is considered to be key. GDPR and PSD2 may have contradictory consequences, which is causing challenges at banks.
Instant Payments (SEPA)	1/1/2019	The Single European Payments Area is a long-standing payment integration initiative covering the EEA. It has published the 'SEPA Instant Credit Transfer Scheme Rulebook' in 2017 which adds a new initiative to the list. Instant payments are expected to be fully implemented in 2019, but first links are already being implemented.
		Treasury: SEPA initiatives, and developments based on SEPA standards, are important to monitor. Instant payments is a major example, which (in conjunction with e.g. PSD2) may change the payment experience significantly for consumers. A SEPA related development is that agreement has also been reached that EUR cross-border payments conforming with SEPA standard will cost the same amount within EU as well as externally (previously this just applied with EU).
Insurance Distribution Directive	1-10-2018	The Insurance Distribution Directive is replacing the Insurance Mediation Directive to create a level playing field for all parties involved in selling and distributing insurances to the ultimate insured. Deadline is pushed back to October 1st, 2018.
		Treasury: Especially important when insurance is part of the product being delivered by the organisation, leasing companies for instance might become subject to this legislation. Exemptions are included but it is considered to be important to determine whether the exemption actually applies. When subject to this legislation the organisation will need to comply with several organisational requirements, like attaining certain insurance certifications. A review of applicability of this regulation is recommended when an insurance component is being delivered by the organisation.

REGULATORY UPDATE (4 / 5)

Regulation	Date	Description
Market Abuse Regulation	16-4-2014	Ensuring market integrity the Market Abuse Regulation was updated to include the OTC market as well as trading over new trading facilities. Insider trading is a key concern being targeted by MAR. Treasury: Investor protection and increased scope of instruments and trading facilities ensuring market integrity. Insider trading and abuse of information continue to be targeted. Share buyback programs as such are not in scope of this regulation.
MIF Regulation *Regulation on Interchange Fees for Card-based Payment Transactions*	27-1-2015	Interchange fees for card-based payments. Regulates the interchange fee rate, by which issuing banks are compensated for the costs and risks that are entailed in enabling transactions using payment cards. Treasury: Both Germany and UK have seen some cost reductions, but this reduction is not required to be passed to merchants and consumers directly. This legislation will work together with PSD2 removing barriers in the EU market, thereby indirect impact on treasury. Fintech solutions are targeting part of this market as well.
MiFID II	3-1-2018	Encloses both an update of MiFID I as well the new MiFIR regulation. MiFID II has a wider scope of trade reporting (including currencies, commodities, credit products and their derivatives), expanding status of organized trading facilities, stricter governance requirements and addressing some lessons learned. MiFIR is part of the package to ensure EU wide consistency in implementation. Treasury: EMIR and MiFID II will lead to a duplication in transaction reporting for some organisations, but transactions reported in accordance with EMIR to a trade repository which is approved as an ARM will typically satisfy the MiFIR reporting requirement as well. Mostly being conducted by financial institutions, but treasury is expected to receive questions by their banks. It is therefore important to have good data in respect of (derivative) trading. Currently impact is primarily expected to hit commodity trading firms, consequences for other firms may be limited to reporting. Although this is conducted by banks, data requests are expected to change to treasury.

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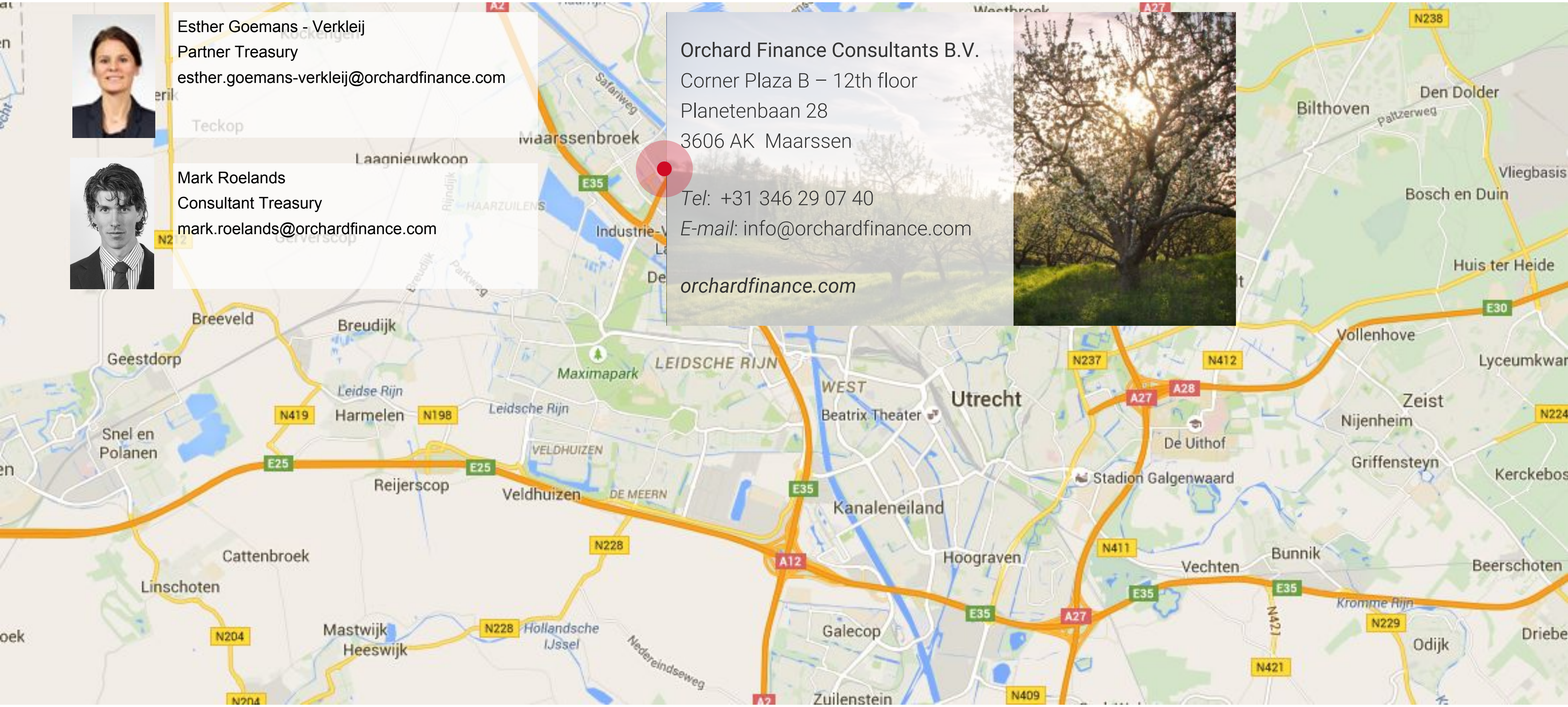
REGULATORY UPDATE (5 / 5)

Regulation	Date	Description
Money Laundering Directive	MLD4 23-6-2015 MLD 5 proposal 5-7-2016	Money laundering and terrorist financing is targeted with MLD legislation. Financial service companies including service providers to the financial industry are obliged organisations. Customer Due Diligence is amongst the requirements as well as analysis of beneficiary ownership. The list of Politically Exposed Persons (PEPs) was extended in MLD 4. MLD 5 was introduced quickly, introducing transparency with ownership registers, and introducing lower thresholds for extensive due diligence and external investigation. MLD 4 however is still awaiting full implementation in the Netherlands. Finally it is important to be aware that suspicious transactions need to be reported.
		Treasury: Ensuring Due Diligence procedures are in place and payments are being made to approved counterparties. When entities under financial supervision are in scope this is of increasing importance as these are amongst the obliged organisations. This is an area of compliance on which RegTech companies are focussing, start-ups in different phases of maturity provide promising techniques in Identity Management, Verification, Authentication, Fraud management and Due diligence. This can potentially be integrated in a TMS system via APIs, which could be a value adding service to treasury.
Payment Service Directive 2	PSD2 Expected Q3 2018	PSD2 contains new rules designed to open up access to payments to third party providers. Account Information Service Provides (AISPs) are introduced as well as Payment Initiation Service Providers (PISPs) new types of licensed entities addressing Fintech innovation and fostering competition in payments. Strong Customer Authentication rules are introduces as well as APIs enabling the sharing of data between platforms. PSD2 should have been implemented in January 2018, but this is delayed and not expected until Q2 in the Netherlands. The impact on privacy is leading to public scrutiny and this will need to be addressed.
		Treasury: PSD2 provides customers with the right to be provided with information that inform access provided, this is referred to as consent management. PSD2 is leading the Open Banking era, and APIs being a prime instrument. MT940 statements might be replaced, and TMSs will need to adopt. Innovators like APEXX, Ibanity and Auka are contributing to new connectivity modes for banking services. Impact is expected on a consumer level first before impacting the corporate environment. DNB has made July 6th as license application date. PSD2 is also causing some concerns for organisations operating a Payments On Behalf Of structure within Germany due to interpretation of the German regulator Bafin. PSD2 is not expected to go live in the Netherlands before summer (leading to dissatisfaction at Dutch Fintechs)
Solvency II	1-1-2016	Solvency II is the Basel equivalent to the insurance industry, taking a 3-pillar approach to strengthening the insurance sector to possible crisis situations. Solvency Capital Requirements need to be calculated, Governance requirements are set including 4 key functions (Internal Audit, Compliance, Risk Management and Actuarial) and reporting and disclosure requirements are increased. SII is in process of some early reviews ensuring it is actually meeting objectives without unduly compliance requirements.
		Treasury: When the organization is involved in an insurance entity in EU region Solvency II will have an impact. Other countries are also applying for regulatory equivalence, but due to the increase regulatory burden a shift towards alternative structures like Protected Cell Companies is made by some organisations. SII is also recognised to impact pricing and capacity in some lines of business (e.g. Motor insurance).



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