MAGYAR BANKSZÖVETSÉG

HUNGARIAN BANKING ASSOCIATION

*Agenda Item No. 4*

# REPORT

## on Activities of the Hungarian Banking Association 4th Quarter 2018

**Budapest, February 2019**

**TABLE OF CONTENTS**

I. Executive Summary ........ 4

II. Macroeconomic outlook: the operating environment of the banking sector ........ 7

III. Corporate sector........ 10

IV. Retail sector........ 11

V. Further important regulatory events influencing the operation of the banking sector........ 11
- Act on the amendment of certain acts on judicial matters ........ 11
- Act on the Amendment of certain acts on the financial intermediary system for the purposes of harmonization of law ........ 11
- Amendment of the rules applicable to public notaries ........ 11
- Failure to submit the sectoral GDPR legislative package in autumn........ 12
- Preparations for the implementation of the Settlement Discipline Regulation ........ 12
- TS2 reform ........ 12
- Methodological change in the National Deposit Insurance Fund's (NDIF) fees ........ 12

VI. Developments in connection with the Magyar Nemzeti Bank (the central bank of Hungary)........ 13
- Review of the Mortgage Financing Adequacy Ratio (MFAR)........ 13
- MNB decree on the detailed rules for the minimum requirements for the development and the operation of the screening system under the Pmt. ........ 13
- Consultation on the management information circular on the risk management of ballon/bullet repayment-type loans ........ 15

VII. Payments........ 15
- The Instant payments project: the state of play ........ 15
- The activities of the SWIFT Hungarian User Group........ 16
- Important decision made by the EPC General Assembly ........ 16
- SEPA SCTInst for a year and TIPS ........ 16
- Regulation 924/2009 – regulating cross-border transaction charges ........ 17
- Bank cards........ 17
- Developments regarding SZÉP cards........ 18
- Developing cash trade........ 18

VIII. Taxation and Accounting........ 19
- Taxation ........ 19
- Reporting ........ 19

IX. Developments within the Banking Association........ 20
- International Relations........ 20
- CECBC Conference........ 20
- Communications........ 20
- Money Week: preparing for the 2018/2019 school year........ 21
- Other working committees and working groups ........ 21

ANNEX – INTERNATIONAL OUTLOOK: REGULATION, SUPERVISION........ 25

I Global Regulation ........ 25
- I.1 Financial Stability Board (FSB)........ 25
- I.2) Basel Committee on Banking Supervision (BCBS) ........ 27

II European Regulation ........ 30
- The European Commission's 2019 Work Program........ 30
- Agreement on the banking regulatory package ........ 31
- Issues concerning prudential regulation........ 31
- Issues concerning rules on resolution ........ 32
- Speeding up the regulatory processes for the Capital Markets Union (CMU)........ 32
- Developments regarding other Level 1 regulatory dossiers in progress ........ 33
- Important EBA and ESMA regulatory processes ........ 33

## I. Executive Summary

In Q4 of 2018, as assumed based on other macroeconomic data the growth rate of the world economy ***likely slowed down***, growth became more articulated in individual regions, as the trade war primarily fought between the United States and China is clearly having an effect on the Chinese and European economy, which are also facing structural difficulties. At the same time, the fact that the two biggest economic powers of the world have recommenced their trade negotiations is encouraging. Money market conditions deteriorated at global level due to the strong fall in developed market exchanges, as opposed to the raising of interest rates by the ECB and the Fed for this year, which were completely priced out.

Protectionist measures have not yet reached a level where they would restrict the growth of the ***US*** economy. In contrast, the voted tax cuts somewhat vitalized growth in the short term, which is now in its mature phase and which continues to be fueled by internal consumption.

Growth in the ***European Union*** slowed down noticeably in the fourth quarter and a technical recession may also be possible in certain countries. Prospects in terms of the real economy have therefore becomes less favorable. There are significant downside risks for future growth, mainly the risk of a trade war, internal tension within large states and political tension at EU level, as well as the increasing likelihood of Brexit happening without any agreements in place.

The ***Chinese economy's*** growth rate probably continued to slow down moderately in Q4. In order to avoid a downturn in economic growth the government uses targeted measures to ease its carefully introduced fiscal and monetary tightening and supports the investments of provincial administrations. It also mitigated its instruments to restrict credit growth from shadow banking.

As a result of globally unfavorable processes, the external environment of the ***Hungarian economy*** became less supportive in terms of growth and external balance prospects. *Consumption* dynamics probably slowed down as a result of a strengthening base, but still remained a definitive factor of GDP growth, to which investments in the real estate, industry and service provider sectors all contributed as well. *Net export* performed weaker than expected in the first two months of the quarter, possibly due to the need for import as a result of the worse terms of trade caused by strong consumption, improving investments and high oil prices. Employment and unemployment improved minimally as regards the *labor market*, the former grew by 0.1 percentage point, while the latter decreased by the same amount compared to the previous quarter. Employment expands at a slow rate due to shrinking labor supply, which actually limits several sectors. The annual rate of *inflation* nearly rose to a record rate in the past six years, reaching 3.8% in the first month of the quarter, however it fell to below the 3% target inflation level by December, due to the high base of fuel prices in the previous year and their steep fall. The fact that inflationary pressure is quite moderate is reflected in core inflation staying under its target, at 2.6%. The *general government deficit* was HUF 1,445 billion at the end of the year. The primary reason for this value is that projects to be funded from EU sources were pre-financed from the budget. Although the robust surplus of the *external trade balance sheet* is becoming more moderate due to a surge in internal demand, external balance indicators remain favorable. The c*apital account* may improve significantly due to the increase in money transfers from the EU, which may contribute to *external financing capacity* rising above 5% of the GDP.

The central bank of Hungary announced the transformation of its *set of monetary instruments*: non-conventional instruments affecting short-term yields will be simplified, and the non-conventional set of instruments affecting long-term yields will be fine-tuned.

According to preliminary supervisory statistics from October and November 2018 the ***aggregated balance sheet total of credit institutions*** grew by 1.6% (HUF 608 billion). On the ***liability side,*** *total gross deposits* grew by HUF 502 billion (1.9%). Both corporate and retail deposits showed an increase, with the former growing considerably (+7.8%, HUF 666 billion), and the latter with a growth slightly below average (+2.2%, HUF 203 billion). As opposed to the above, state deposits decreased significantly (-24.7%, HUF 325 billion). Within ***assets*** the *gross loan portfolio* grew by 1.7% (HUF 349 billion) in October through November and by 1.5% (HUF 268 billion) not considering interbank credit. Lending-related impairment loss and valuation difference continued to decrease slightly. In two months growth in the gross loan portfolio of the *non-financial corporate sector* was over two percentage points above the average value (+2.1%, +HUF 200 billion), while the increase in *household loans* was once again less than average (+1.4%, HUF 83 billion).
As a result of the above effects, the ***total loan-to-deposit ratio***[1] of the credit institutions sector was 67%, and 80% not considering interbank facilities.

***Profit*** before taxes was down by 14% compared to the same period of the previous year, at slightly higher than HUF 510 billion. On an annualized basis, this reflects a 13.3% return on equity, and a 1.5% return on assets. Without dividend, provisions and impairment the profit was HUF 364 billion, with the return on equity and assets being only 9.4% and 1.1% respectively.

In line with the principles of the Funding for Growth Scheme in January 2019 the MNB launched the ***FGS Fix*** with a facility amount of HUF 1,000 billion, the target of which remains the SME sector. According to the central bank's expectations the FGS fix may raise the level of investments in 2019 and 2020 by 0.2 and 0.8 percentage point, respectively, and as a result of this it may contribute to the economic growth expected in 2020 by 0.2 percentage point.
MNB initiated the introduction of an electronic interface, a so-called ***Electronic Loan Application Interface***, through which micro and small enterprises can submit their loan application in the same format to several banks in parallel and the participating banks have to provide an offer within a few days in a comparable format. The Interface is currently under preparation and will likely be launched in H2 of 2019.

The Ministry of Justice postponed the entry into force of its new decree on the ***rules applicable to public notary fees*** to 1 April 2019.
The methodology for determining the ***NDIF's fees*** and their payment will be modified on several points in the near future. One of these is the introduction of a new anticyclical indicator, which will allow for the consideration of macroeconomic cycles when determining fees. This change will not impact the 2019 fees. In addition the beginning of the fee payment cycle will also change (from January 1st to October 1st), in order to increase predictability by having fees be determined based on audited data for the entire duration of individual cycles.
In Q4 the MNB reviewed the methodology for determining the ***Mortgage Funding Adequacy Ratio***, and by these means it wishes to introduce measures to deepen the mortgage bond market. The MNB plans to carry out the modification of the decree on the MFAR in two separate parts, with their entry into force in February and then October of 2019. The modified decree will raise the threshold of the MFAR, increase the original maturity of stable liabilities that can be considered, raise the de minimis and pricing, and will introduce credit rating for securities as well as institutions involved in the issuing process.

---

[1] Net loan to net deposit

The central bank issued a new decree to re-regulate the requirements for the screening system under the act that regulates ***tasks to prevent money laundering***, including online customer due diligence, simplified customer due diligence and expectations for screening systems, while also amending and complementing rules in connection with obligatory training.
The central bank's implementation of the most important project in payments - the ***Instant Payment System*** – proceeds according to the schedule based on the evaluation of project management. Work was concentrated to three areas: the *basic standardization of business processes* closely related to the project in order to establish interoperability between services; defining the business procedure and data content of *Requests to Pay*; and creating the *payment brand*. An assessment on the state of preparedness of participating banks was made, as well as on reasons for delay and risks. Several reasons were given by participants explaining their current state of preparedness, however no one indicated their inability to meet the requirements by the deadline given. 60% of banks undertook to be fully prepared to manage transactions by the end of the year, and most participants aim to achieve continuous availability in 2019. The *new pricing model of the interbank clearing system* aims to establish fee structure to promote the take-up of instant payments. Instead of transaction-based charging (applied until now), GIRO plans to define an annual participation fee at sectoral level. Complementary services will not have any additional costs when package pricing is applied.
A substantive phase of the legislation procedure to amend ***Regulation 924/2009 on cross-border transaction charges*** has been completed. Our arguments were presented through the means of international cooperation and regarded the currency scope, the length of time and the feasibility of technical requirements needed to introduce dynamic currency conversion (DCC) and were heard in merit towards the end of the Austrian Presidency. According to the agreement made at the Trilogue, the regulation for uniform charges on transactions will need to be implemented from December 15, 2019, while our member banks will need to implement rules in connection with DCC a year after.
As regards the ***Széchenyi Recreation Cards (SZÉP cards),*** in addition to exemption from the financial transaction levy, further progress was made in connection with judicial enforcement procedures and strong customer authentication. In addition, the transition deadline was postponed by one month.

Just as in previous years, 2018 also saw important changes in ***reporting*** and opinions to the ***tax*** laws of the coming year. Concerning the latter, a development to highlight is the proposal for the technical resolution of the technical problems associated with tax exemption from payment transactions between the customer accounts kept by the State Treasury and used by natural persons for sovereign debt trade and their payment accounts kept by another account keeper, introduced from 2019 on.
Important developments concerning the ***international relations*** of the Banking Association were the election of the Banking Association's Secretary General into the Board of Directors at the European Money Markets Institute (EMMI), and having successfully organized the Central European Covered Bond Conference in Budapest.
In Q4, the ***global standard setting bodies*** evaluated global financial stability and regulatory developments in preparation for the G20 summit. Having assessed the *market developments and vulnerabilities of the global financial system*, the ***Financial Stability Board*** believes that normalization of monetary policy in some advanced economies has contributed to a marked tightening of financial conditions in some emerging market economies; that some asset classes – including real estate in a number of economies – are showing signs of overvaluation; and that the persistence of geopolitical uncertainties warrants attention. The FSB highlighted that *risks stemming from the snap-back in interest rates* could be particularly relevant as interest rate rises and widening credit spreads increase debt service costs, which leads to the reassessment of corporate and sovereign risks, and also pointed out that non-bank financial intermediation causes significant maturity and liquidity transformation, thus increasing concentrations in holdings of risky assets. In its report to the G20, the ***Basel Committee on Banking Supervision (BCBS)*** evaluates current professional policy and supervisory issues and the implementation of post-crisis reforms by its members.

***European regulation processes*** were determined by the European parliamentary elections to take place in May 2019, the setting up of the new European Commission, and the considerable number of legislative procedures on the agenda in the field of finance. As a result of these, no preparations were launched to create new Level 1 (directives and regulations) or Level 2 (delegated directives and regulations, as well as RTS and ITS) legislation, EU institutions did however make significant efforts to close open dossiers and procedures in progress. A visible sign of this was the European Commission's ***work program*** for next year, which was published in October, and which sets ambitious targets, primarily to complete the regulatory framework (directives and regulations) for the Capital Markets Union. The most important development within this process was the completion of a series of successful consultations under the trilogue on the ***banking regulatory risk reduction package*** in November. Among other things, the package finalized important issues, such as the calibration of the NSFR and the leverage ratio, the introduction of the simplified NSFR, the introduction of certain rules of proportion for small, non-complex institution, defining SME support factors, an exemption from deductions of certain intangible software assets from own funds in connection with prudential regulation, as well as the limiting of the sale of MREL instruments to retail customers as part of rules for resolution. In addition to the above, the Commission targeted taking another significant step forward by issuing a communication for its consulting parties on the tasks concerning the 10 open regulatory dossiers in connection with the ***Capital Markets Union.***

The Hungarian Banking Association founded its Golden Beehive Award in recognition of outstanding individual work to aid the development and operation of the credit institutions sector and the Golden Beehive Certificate of Recognition to acknowledge a lifetime career of exemplary success in the banking sector. At the 2018 year-end event of the Banking Association, the Board decided to recognize the achievements of the following persons:

- Henrik Auth – Golden Beehive Certificate of Recognition
- Mária Móra (Hungarian Banking Association) – Golden Beehive Award

## II. Macroeconomic outlook: the operating environment of the banking sector

In Q4 of 2018 the growth rate of the world economy likely slowed down, growth became more articulated in individual regions, as the trade war primarily between the United States and China is clearly having an effect on the Chinese and European economy, which are also facing structural difficulties. The IMF consistently lowered its expectation for this year and the next by 0.2 percentage points (to 3.7%). Money market conditions deteriorated at global level due to the strong fall in developed market exchanges, as opposed to the raising of interest rates by the ECB and the Fed for this year, which were completely priced out. Due to worries concerning in part demand and in part supply, by the end of the year oil prices fell by more than they ever have in the past ten years.

The protectionist measures and protective tariffs announced and introduced by the president of America have not yet reached a level where they would restrict the growth of the ***US*** economy; however, the possible reaction from large trade partners may increase the risk of a global trade war. In the mid-term this may damage business confidence and therefore willingness to invest. In contrast, the voted tax cuts somewhat vitalized growth (which is now in its mature phase) in the short term. Based on labor market and income related data the main driving force behind growth may still be internal consumption. Nevertheless, certain corporations already feel the negative effects of the trade war. At the same time, the fact that the two biggest economic powers of the world have recommenced their trade negotiations is encouraging. In December the Fed once again raised the reference rate by 25 basis points (to 2.50%).

Growth in the ***European Union*** slowed down noticeably and a technical recession may also be possible in certain countries. Prospects in terms of the real economy have therefore becomes less favorable. A big surprise was the slight contraction of the German economy, while economic

indicators may be pointing towards further downturn, although consumption may be able to compensate for export difficulties. Declining industrial production and net export are the primary reasons behind weaker performance, caused by the new standards for measuring harmful emissions (introduced in September) as well as the slowing of the Chinese and the global economy. Internal consumption has likely continued to have a positive effect – this assumption is supported by favorable labor market data (unemployment is at its lowest in nine years, while job creation is at its peak). There are significant downside risks for future growth, mainly the risk of a trade war, internal tension within large states and political tension at EU level, as well as the increasing likelihood of Brexit taking place without any agreements being made.
It is expected that the ***Chinese economy's*** growth rate continued to slow down moderately in Q4. Internal consumption remains the main pillar of growth, but the slowing of the rate of growth – along with investment – continues and net export restricts economic expansion as well. Deteriorating economic prospects may incentivize China to end the trade war, although issues regarding patent rights and the so-called "forced" technology transfer may present obstacles to this. In order to avoid a downturn in economic growth the government uses targeted measures to ease its carefully introduced fiscal and monetary tightening and supports the investments of provincial administrations. It also mitigated its instruments to restrict credit growth from shadow banking.

As a result of the above mentioned unfavorable processes, in Q4 the external environment of the ***Hungarian economy*** became less supportive in terms of growth and external balance prospects. ***Consumption*** dynamics probably slowed down as a result of a strengthening base, but it is predicted that it will remain a definitive factor of GDP growth. ***Investments*** continue to aid growth, with the real estate, industry and service provider sectors each playing their part. Due to the new regulation on harmful emissions (WLTP), the ***industry*** has shown moderate performance since Q3 of last year, however industrial production may speed up as car manufacturers gradually obtain marketing authorizations. This is supported by inaugurated production industry capacities, favorable industry confidence indices, as well as the recent surge in new industrial orders. Considering future production, it is very encouraging that a decision was made to invest a record amount of working capital, HUF 1380 billion, last year. These trends are not yet visible in ***net export***, which performed weaker than expected, possibly due to the need for import as a result of the worse terms of trade caused by strong consumption, improving investments and high oil prices.
Employment and unemployment improved minimally as regards the ***labor market***, the former grew by 0.1 percentage point, while the latter decreased by the same amount compared to the previous quarter. Employment expands at a slow rate due to shrinking labor supply, the virtually sole cause of which is the job creation of the primary labor market. A lack of labor supply may actually limit several sectors, therefore wage dynamics may remain high not only as a result of increased minimum and guaranteed minimum wage, but also as a result of increasing market wages.
The annual rate of ***inflation*** nearly rose to a record in the past six years, reaching 3.8% in the first month of the quarter, however it fell to below the 3% target inflation level by December, due to the high basis of fuel prices last year and their steep fall. An 11% increase in income and the subsequent rise in demand is still not noticeable in prices save for a few subareas. Its effects are likely compensated for by persistently low imported inflation and decreased wage and entrepreneurial burdens. The fact that inflationary pressure is quite moderate is reflected in core inflation staying under its target, at 2.6%.
The ***general government deficit*** was HUF 1,445 billion at the end of the year. The primary reason for this value is that projects to be funded from EU sources were pre-financed from the budget. This amounted to a total of HUF 1,886 last year, while the EU only transferred HUF 1,430 billion. According to the ministry responsible and calculated with the EU methodology (EU pre-financing adjusted) it may have taken on a value of under 2% by the end of the year.

Although the robust surplus of the ***external trade balance sheet*** is becoming more moderate due to a surge in internal demand, external balance indicators were also favorable. The ***capital account*** may improve significantly due to the increase in money transfers from the EU, which may contribute to ***external financing capacity*** rising above 5% of the GDP.

The central bank of Hungary announced the transformation of its ***set of monetary instruments***, the phasing out of certain instruments, as well as the introduction of one new one. In addition, it disclosed that it will start to prepare for the normalization of monetary conditions. At the same time, interbank forint liquidity, which remains significant keeps short-term yields well under the 0.9% base rate. Non-conventional instruments affecting short-term yields will be simplified within the new set of instruments, and the non-conventional set of instruments affecting long-term yields will be fine-tuned. The three-month deposit instrument was phased out towards the end of 2018 and the minimum reserve will take over the role of lead instrument in the future. Looking forward it seems that the central bank wishes to create the monetary conditions necessary for the sustainably reaching the target inflation through an optimal combination of two instruments – swap portfolio granting forint liquidity and the interest rate corridor. In addition to this the monetary policy targeted IRS instrument and the mortgage bond acquisition program were both phased out by the end of 2018. MNB will sterilize the liquidity emerging within the Funding for Growth Scheme Fix through a preferential deposit design yielding interest at the base rate.

The EUR-HUF exchange rate steadily decreased throughout the quarter, varying between HUF 320.5 and 326 HUF/EURO.

According to preliminary supervisory statistics from October and November 2018 the ***aggregated balance sheet total of credit institutions*** grew by 1.6% (HUF 608 billion). Forint assets basically remained at their September value (expanding by only HUF 6 billion). In contrast, foreign currency assets rose significantly (EUR stock: +5.3%, other foreign currencies: +5.1%).

On the ***liability side,*** all important liability types increased. ***Total gross deposits*** grew by HUF 502 billion (1.9%). Within this, interbank deposits decreased (by 1.7%), while there was an above average increase in other deposit types (2.7%). The increase in the latter was due to the balanced expansion of both domestic and foreign deposits (2.7% and 2.9%, respectively), although the nominal increase in domestic deposits is what is of primary significance (HUF 552 billion as opposed to HUF 27 billion).

The average maturity of interbank deposits increased, while all other maturities became shorter. Both corporate and retail deposits showed an increase, with the former growing considerably (+7.8%, HUF 666 billion), and the latter with a growth slightly below average (+2.2%, HUF 203 billion). As opposed to the above, state deposits decreased significantly (-24.7%, HUF 325 billion). The restructuring of instruments continued in ***interbank liabilities*** (which include interbank credit), as well as in both those domestic and those foreign, with an increase in the latter, while total interbank liabilities remained the same. ***Equity*** increased by HUF 78 billion (1.8%) during the quarter.

Within ***bank assets*** all important asset types increased apart from debt securities. The ***gross loan portfolio*** grew by 1.7% (HUF 349 billion) in October through November and by 1.5% (HUF 268 billion) not considering interbank credit. Lending-related impairment loss and valuation difference continued to decrease slightly. Not counting the interbank portfolio, the domestic portfolio showed an average increase (+1.6%, HUF 249 billion), while growth in the foreign portfolio remained well below 1%.

In two months growth in the gross loan portfolio of the *non-financial corporate sector* was over two percentage points above average value (+2.1%, HUF 200 billion) and reversal of impairment could still be observed over this period. The increase in *household loans* was once again less than average (+1.4%, HUF 83 billion).

As a result of the above effects, the ***total loan-to-deposit ratio***[2] of the credit institutions sector was

[2] ***Net loan to net deposit***

The ***profit*** before taxes was down by 14% compared to the same period of the previous year and was slightly higher than HUF 510 billion. On an annualized basis, this reflects a 13.3% return on equity, and a 1.5% return on assets, which is less than in the previous quarters. Without dividend, provisions and impairment the profit was HUF 364 billion, with this calculation the return on equity and assets was only 9.4% and 1.1% respectively. Net interest revenues stagnated compared to the same period of last year. Revenue from fees increased by nearly 10 percent, however, administrative expenses increased by just about the same amount (in addition to a 14% increase in labor costs).

**III. Corporate sector**

*According to data from MNB*, corporate lending continued to grow dynamically in 2018 H1. In an annual comparison, as a result of transactions, loans outstanding rose by 12 per cent, while the corporate loans outstanding of SMEs rose by almost 15 per cent. In the case of SME forint loans with maturity over one year, the ratio of fixed-rate loans decreased in the first half-year, while in the third quarter it rose back to the level registered at the end of last year. At present long-term, fixed-rate loans are not concluded by a wide range of borrowers in the SME credit market, therefore, with a view to shifting lending towards a healthier structure, the MNB launched the ***Funding for Growth Scheme Fix*** (FGS fix).
In November, the MNB information packet confirmed that the previous three phases of the FGS managed to stop the SME sector's loan portfolio from shrinking; the MNB therefore believes that the scheme was successful. In line with the previous FGS principle, in January 2019, the MNB launched its FGS fix program with a facility amount of HUF 1,000 billion, the target of which remains the SME sector. According to the central bank's expectations the FGS fix may raise the level of investments in 2019 and 2020 by 0.2 and 0.8 percentage point, respectively, and as a result of this it may contribute to the economic growth expected in 2020 by 0.2 percentage point. The SME working group participated in the finalization of the elaboration process of the framework contract between individual credit institutions and the MNB as well as the product information. The product was introduced on January 1, 2019.

Respondent banks participating in the ***Lending Survey*** reported the easing of credit conditions in all corporate size categories. Most respondents noted that the easing is due to stronger bank competition and the favorable trends in economic prospects. Corporate credit demand increased further in the first three quarters of 2018 both for short-term and long-term loans. It seems that, looking at the result of MNB's questionnaire-based survey, the absence of micro and small enterprises' willingness to borrow is explained primarily by the lack of investment plans and the aversion to loans and external financing, while fear of rejection does not appear to be an important consideration.

***The Standardized Loan Application Interface***

Based on the international and domestic experiences, the complexity of the loan application process causes problems to many small and medium enterprises. Simplification of the loan application procedure of the SMEs is very important to the MNB and they believe that it would enhance both appetite to borrow and bank competition if there were an electronic interface through which the micro and small enterprises could submit their loan application in the same format to several banks in parallel and the participating banks had to provide an offer within a few days in a comparable format. The concept also includes the creation of a clear guide that contains useful information. In order to elaborate the Standardized Loan Application Interface (SLAI) the SME working group met with MNB representatives several times during the quarter. SLAI will probably be launched in H2 of 2019.

## IV. Retail sector

***Results of the positions taken and the consultations regarding the Family Housing Allowance (CSOK)***

In Q4 the Ministry of Finance once again issued a new, complementary professional opinion regarding state aid for housing purposes, which serves the uniform application of law. The Ministry's previous professional opinion with regard to the heatability of the flat's premises and the inspection of heating systems was modified according to the practical problems indicated.

In effect from December $1^{st}$, the information packets on home building, the acquisition of new or used homes and the extension of dwellings for allowance applicants with two or with three or more children have been updated.

## V. Further important regulatory events influencing the operation of the banking sector

***Act on the amendment of certain acts on judicial matters***

The proposal on the amendment of certain acts on judicial matters was sent by the Ministry of Justice to the Banking Association, and the draft was consulted by the Legal and the Workout Working Group. The Banking Association has made a proposal with regard to the obligation to open Széchenyi Recreation Cards and the exemption from enforcement of restricted payment accounts opened in the context of the earmarked nature of amounts deposited on them to amend Act LIII of 1994 on Court Enforcement; the relevant provisions are set out in Act XCI of 2018 on the Amendment of Certain Acts on Judicial Matters, published on 6 December 2018.

***Act on the Amendment of certain acts on the financial intermediary system for the purposes of harmonization of law***

With a view to protecting the interests of employees in bank branches, the Banking Association initiated the amendment of the regulations applicable to the witnessing rules for private documents with full probative value. The relevant provisions are included in Act CXXVI of 2018 on the Amendment of certain acts on the financial intermediary system for the purposes of harmonization of law, published on 21 December 2018. The new provision now present in the Act on credit institutions does not however provide a reassuring solution to the issue, as in the case of CSOK transactions the address of the witnesses still needs to be indicated. In order to form a common practice the Banking Association will initiate the clarification of this law in the 2019 spring legislation period.

***Amendment of the rules applicable to public notaries***

On the basis of the new Decree of the Ministry of Justice on the public notary fees, the charges to customers would have increased significantly, leading to a great increase in costs for customers taking out a mortgage loan. In view of the consultations launched with a view to resolving this problem, the entry into force of this new decree has been postponed by the Ministry of Justice from 1 October 2018 to 1 January 2019, then to 1 April 2019.

***Failure to submit the sectoral GDPR legislative package in autumn***

After the 25 May 2018 entry into force of the European Union's General Data Protection Regulation (GDPR), the Ministry of Justice amended Act CXII of 2011 on the Information self-determination right and the freedom of information by appointing the Hungarian National Authority for Data Protection and Freedom of Information as supervisory authority. The GDPR has a significant effect on banking processes, thus sectoral legislation needs to be amended in connection with that Regulation, in which context the Data Protection Working Group collected its proposals and observations. The Ministry of Justice held several consultations with strategic partners, including the Banking Association, on the comments and proposals; however, in the autumn session the package submitted to the Parliament was not discussed and adopted. At the end of Q4, the Ministry of Justice has sent to the Banking Association its proposal on the amendment of certain acts in the context of the European Union data protection reform, for consultation, in which context the Data Protection Working Group held a meeting and compiled its suggestions. In connection with this, in early 2019, face-to-face consultations took place in the ministry with the involvement of ministries in charge of the relevant legislation (Ministry of Finance, Ministry of Human Capacities, Ministry for Innovation and Technology).

***Preparations for the implementation of the Settlement Discipline Regulation***

The primary background legislation for the SDR - Settlement Discipline Regulation of the EU is the CSDR - Central Securities Depository Regulation. In the CSDR, basic rules have already appeared with regard to the settlement of transactions; however, detailed rules became known only in September 2018, upon the publication of the Settlement Discipline Regulation (SDR). The SDR contains provisions for the tracking of failed settlement, the prevention and management of settlement failure, and encouraging settlement discipline. In view of the direct effect of that Regulation and its applicability as of 13 September 2020, KELER has started the preparation and consultations with market players and associations. The above explained legal nature of that Regulation also means that no derogation is permitted; the primary objective is therefore to establish a smooth practice for the sector.

***TS2 reform***

In May, in the framework of the corporate event reform, KELER, the Budapest Stock Exchange, and the central bank of Hungary initiated a consultation with a view to ensure the national compliance required for KELER's joining the securities settlement system (T2S), and the further increase of transparency and automation in the field of processes and operation. An inter-institutional *ad-hoc* Regulatory and Tax Working Group was set up, led by KELER, to develop the topics of this initiative, which drafted an industry level position in Q3 and Q4 in connection with the origination and cancellation of securities and nominee shareholder, as well as the payment of security yield, tax return and automatic rights compensation. These consultations are expected to continue with other representatives of the sector.

***Methodological change in the National Deposit Insurance Fund's (NDIF) fees***

Under Section 224 (1) of the Hpt.[3] the NDIF Board develops the NDIF fee policy once a year and presents it to credit institutions. In this process, it sets the fee rate, the basic fee and sets the level of the correction coefficient.

As of 2019, the NDIF sets the annual fees by 30 September in line with the Sztv[4] and the Hpt after receipt of **audited data**; accordingly, the fee-paying period lasts from 1 October until 1 September in the next year. In the 2019 transition period, member institutions pay an advance fee.

[3] Act CCXXXVII of 2013 on Credit Institutions and Financial Enterprises

NDIF continues to treat the achievement of the target level as a priority, and the fee policy will be set with equal charging up to 2024. The annual payment obligations of NDIF members must be set, in addition to the above, to take into account the phases of the business cycle, the effect of the pro-cyclic payments to the amount of annual payments, and the financial situation of credit institutions. In view of the cyclic nature of the economy, as of 2019 a new variable will be introduced, aiming to make the entire fee payment anti-cyclical. The Macroprudential Directorate of the MNB decides on the economic environment allowing for the application of the **anticyclical indicator**, and at the same time it makes a proposal to NDIF to the level of that indicator.

## VI. Developments in connection with the Magyar Nemzeti Bank (the central bank of Hungary)

***Review of the Mortgage Financing Adequacy Ratio (MFAR)***

MNB decree 20/2015 (VI. 29.) on the regulation of the forint maturity mismatch of credit institutions was reviewed in Q4 of 2018 in order to promote the further inclusion of mortgage covered liabilities with a long-term maturity at systemic level and to thus achieve the further deepening of the mortgage bond market. The MNB plans to carry out the modification of the Decree in two separate parts, with their entry into force in February and then October of 2019. The **value of the MFAR** must always reach 0.25 (instead of the previous 0.2 minimum). Through the modification the original maturity of the one and two-year liabilities within the items that can be taken into account in the numerator will change to three years from October 1, 2019. Mortgage bonds will from now on be **priced** in a way that the bonds held for this purpose may be considered as a reducing factor when calculating the ratio in specific cases and to a specific degree. From 2019 on the **de minimis** will increase from HUF 3 to 10 billion, i.e. the credit institutions which will fall under the scope of the decree must have a net retail mortgage loan stock of at least HUF 10 billion or more, with a residual maturity of more than one year. **Credit rating** will be a new requirement, which must be fulfilled with regard to either the security, the issuer or the institutions undertaking to pay.

***MNB decree on the detailed rules for the minimum requirements for the development and the operation of the screening system under the Pmt.***

On the basis of a few months of experience of the practical application of the MNB Decree on the implementation of the Act on the prevention and combating of money laundering and terrorist financing relating to service providers supervised by the MNB and the minimum requirements of the development and operation of the filtering system specified in the Act on the implementation of the restrictive measures imposed by the European) Union and the UN Security Council related to liquid assets and other financial interests, the AML Working Group of the Banking Association has prepared and sent earlier, on two occasions, the corrections proposed by the sector.

Rather than amending the decree, the MNB decided to re-regulate the issue, because although the re-regulation covered only a few topics, in view of their gravity and nature, codification considerations warrant the creation of a new law.

In the framework of this review, essentially the online customer due diligence, the simplified customer due diligence and expectations for screening systems were re-regulated by the MNB, and also training-related rules were somewhat amended and complemented. The working group drafted its proposals to the text of the new decree in line with its earlier comments.

---

[4] Act C of 2000 on Accounting

***Consultation on the management information circular on the risk management of ballon/bullet repayment-type loans***

The MNB assessed the risks associated with the specificities of balloon loans (loans where the last installment must be paid off with one final, large payment) and bullet loans (loans to be paid off with a large lump sum payment) among financial institutions. As a result of the assessment, the MNB compiled a management information circular to create a best practice for the uniform interpretation, measurement and management of prudential risks stemming from these types of loans at sectorial level. Prior to issuing the circular, the central bank consulted with the banking sector, towards the end of November. An essential missing part from the draft was the clear determination of its scope, which allowed for other products with very different, lighter risk to fall under it, such as transactions of less than one year, microloans, financing without a repayment profile or covered by liquid assets, etc. Other important problems were: the definition of such loans differing from that in the ICAAP handbook; and that it doesn't recognize the risk reducing role of these repayment methods in project financing when they are applied.

The MNB will send out the circular after having considered the above.

## VII. Payments

***The Instant payments project: the state of play***

At its *meeting in October* the Project Launch Committee reviewed the state of the instant payments project. Dr Mónika Iszály, the project's head from GIRO's side informed everyone about where the project is at currently, presenting its timetable, tasks and the requests for change that were approved (in order to finalize the liquidity management function, the Committee also received essential help from the Banking Association's Liquidity Working Group). Business testing will start in January, alongside the fully testable functionality of the system. Mandatory business testing will be concluded on May 31$^{st}$, while testing of the project may be carried out until the end of June.

Gábor Bakati discussed how prepared participating banks are according to the assessment, as well as talking about reasons for delay and risks. Several reasons for the above were given by participants in connection with their current state of preparedness; however no one indicated their inability to meet the requirements by the deadline given. Mr. Bakati said that 60% of banks plan to be fully prepared to manage transactions by the end of the year, and most participants aim to achieve continuous availability in 2019. He also concluded that tasks will add up in the time remaining.

The *new pricing model of the interbank clearing system* was presented by Dr Zsolt Selmeczi-Kovács. The change in fees aims to incentivize the increase in the turnover of money transfers, to simplify the fee structure and to make it possible for financial institutions to plan their payments expenses. According to the project goals, it is necessary to create a fee structure that will promote the take-up of instant payments. From now on a clearing and settlement turnover participation fee will be determined annually at sectoral level, as opposed to transaction-based charging applied at GIRO up until now. Complementary services will not have any additional costs when package pricing is applied. Requests to pay and the use of secondary account verification will be virtually free. Sending, receiving, complementary services and other services in connection with using the system will be included in the system use fee.

Communications preparatory tasks associated with the face of the instant payments system brand are ongoing (choosing a brand name and the visual planning of its logo). Communications activities will intensify in 2019; the communication strategy is currently being elaborated.

***The activities of the SWIFT Hungarian User Group***

After SWIFT's[5] largest annual professional event, SIBOS, the Hungarian user and shareholder group's agenda for the H2 meeting was compiled based on the SIBOS topics: gpi[6] (a service developed for the quick and transparent management of cross-border payments, to be mandatorily introduced from 2020 at global level); the instant payments solution developed by SWIFT in order to "speed up payments" – this was ordered and first applied by the Australian payments system; and cyber security, which remains a key issue. Starting from last year the CSP[7] became obligatory, to be repeated annually, as has become fulfilling the requirements of KYC-SA[8]. Members had to complete the required tasks for these by December 31, 2018. Application of the SWIFT strategy (spanning until 2020) will continue next year: the migration of payments-related messages to the ISO 20022 standard.

***Important decision made by the EPC General Assembly***

During the first part of its General Assembly in December the EPC[9] decided on significant issues concerning its organization and personnel, then, in his address to the Board, the Director General presented the activities relevant to the ERPB[10] and the EPC's participation in the ERPB's different working groups, such as those dealing with issues like *EIPP[11], SCTInst[12], Request to Pay, Payment initiation and API access scheme*. He discussed the main points of the strategic meeting in September, emphasizing that the EPC Charter would only be reviewed in 2019. In addition, the Chair of the SEM[13] WG briefly talked about updating the rulebooks and the modification of information related to credit transfers in line with market needs, as well as its optional application from 2019. In connection with mobile payments he mentioned that the White paper on non-NFC Mobile Card-based proximity Payments was put up for public consultation and he also summarized work on Mobile Initiated SEPA Credit Transfer (including SCTInst).

The Director General also talked about the workplan and budget for 2019. Despite changes to EPC members the membership fee stayed then same in MODUL1, to which the Banking Association belongs. Our member banks are generally concerned in the SCT and SCC core models, the annual membership fee for these is €213 and € 314, respectively, while participation in the SCTInst model will remain free in 2019. Annual participation fees will be reviewed in 2019.

***SEPA SCTInst for a year and TIPS***

The SEPA infrastructure has been expanded to include another element in November. By the request of the ERPB the first Pan-European instant euro transfer model, developed by the EPC, first started operating in October 2017. At its launch, it already had five hundred active payment service providers (fundamentally credit institutions) as its members; by early 2018 this number grew to over one thousand and over the course of the year, once TIPS was launched, the number of participants rose to over two thousand.

TIPS[14], the system and service developed by the ECB[15] was launched in November 2018, with the specific purpose of clearing and settling instant euro payments in central bank money. Therefore,

---

[5] SWIFT: Society for Worldwide Interbank Financial Transfer
[6] Gpi: Global Payment Initiative
[7] CSP: Customer Security Programme
[8] KYC-SA: Know Your Customer – Self Attestation
[9] EPC: European Payments Council
[10] Euro Retail Payment Board
[11] EIPP: Electronic Invoice Presentment and Payment
[12] SCTInst: SEPA instant transfer
[13] SEM WG: Scheme Evolution and Maintenance Working Group
[14] TIPS: TARGET Instant Payment Settlement
[15] ECB: European Central Bank

there are now two operating systems which are capable of completing the final clearing and settlement of small-sum, cross-border (if needed) consumer transfers at Pan-European level of up to 15 thousand euros, in under just 10 seconds. (The other such clearing and settlement system is the RT1, operated by the EBA[16].)
The ECB is applying the principle of full cost recovery while operating TIPS, while at the same time it does not charge its account holders a joining or maintenance fee. The new service is provided at 0,0002€/ initiated transaction in the first two years, while the first ten million payments settled on each TIPS account before the end of 2019 will be free of charge.
Payment service providers from Spain, Germany and France were the first to join the service and to make use of the opportunity to aid the mass use and promotion of the service through innovative payment solutions.
The ECB's service is also capable of performing clearing and settlement services for other currencies of the EEA besides the euro. For now, no Hungarian members have joined the model or the clearing and settlement system.

***Regulation 924/2009 – regulating cross-border transaction charges***

The legislation procedure concerning the proposal to amend Regulation 924/2009 initiated by the European Commission started towards the end of the first quarter. The original proposal contains two main elements. According to the first, the payment service providers of member states outside the euro area have to apply the charge to euro credit transfers as they apply for domestic credit transfers equal to the same amount. The other element concerns payment cards in the case of the so-called dynamic currency conversion (DCC): when using POS[17] terminals and ATMs[18], the PSPs must transparently indicate to consumers all charges and exchange rates to be applied in order that the consumer may at the place of payment decide whether to pay in the local currency or in the one on his or her account. Payment service providers have three years to prepare for meeting this last requirement.
We represented the banking sector's professional arguments with regard to the modification proposals through several official channels and via international interbank cooperation, initially under the Bulgarian Presidency, then under the Austrian Presidency. Among other things, we asked to be treated equally to other EU member states. However, the relevant EU organizations voiced opinions opposite to ours during the legislation process. Our arguments were heard in merit only towards the end of the Austrian Presidency. Our arguments regarding the currency scope, the length of time and the feasibility of technical requirements needed to introduce DCC were already taken into consideration at the first meeting of the Trilogue.
On December 19, 2018, the draft regulation adopted by COREPER II at the end of the Trilogue accepted the suggestions of the banking sector on several points. Work on technical, clarification-type issues will continue under the Romanian presidency; content will no longer be discussed. According to the agreement the regulation for uniform charges on transactions will need to be implemented from December 15, 2019, while our member banks will need to implement rules in connection with DCC a year after.

***Bank cards***

According to the latest data published by MNB on December 15, 2018 in the third quarter of 2018 payment card transactions continued to increase. The number of physical merchant acceptance points once again grew (to 118,000 acceptance points; 145,000 POS terminals) and there was a

[16] Euro Banking Association
[17] POS: Point of Sale
[18] ATM: Automated Teller Machine

significant (nearly 25 percent) increase in purchases by payment cards in Hungary (199 million transactions, representing a total value of HUF 1,396 billion), with 70% of total purchases made using the quick and modern contactless payment method. The number of payment cards issued in Hungary continued to grow, increasing by 95 thousand; thus 9.2 million were in circulation by the end of Q3.
The Bank card working group constantly monitors and supports member institutions' preparation processes for PSD2, especially the introduction of strong customer authentication and the amendment of EU Regulation 924/2009, with special attention dedicated to the DCC (spot exchange rate) implications for bank cards, as well as the EU's amendment of the regulation on the Inter-regional Interchange Fee. In addition, the working group consulted with the authorities that inspect fraud cases and the competent representatives of card companies throughout the quarter, in the subject of fraud and card forgery, as well as following foreign fraud exposures and events with the help of EAST. Moreover, we participated in the Nézőpont Intézet orgnaization's lecture and roundtable discussion on rendering payment processes cash-free.

***Developments regarding SZÉP cards***

The new government decree of 20 April 2018 classifies the issuing of the Széchenyi Recreation Cards (SZÉP cards) as part of payment services. We consulted and will continue to consult with the Ministry of Finance and the central bank of Hungary to lower the costs of this transition as much as possible. So far, the HBA achieved the following:

- According to the resolution issued by the Ministry the exception rule of the RTS regulating the PSD2 strong customer identification is applicable; therefore SZÉP cards currently in use may continue to be used.
- According to the modification of the government decree, the transition must be completed by January 5, 2019 instead of by November 30, 2018.
- Transforming the current system would mean higher financial transaction levy for employers. We therefore recommended that the SZÉP cards be exempt from this. The relevant law was amended and the SZÉP card issuers concerned created a regulatory framework which will simplify the exemption process at transferring banks.
- According to the government decree the account linked to the SZÉP card will be classified as a limited-purpose payment account, therefore transfer to and from authorities is not possible. The Judicial Enforcement Act (Vht.) was amended[19] in the interest of the above.
- During the preparatory phase certain issues were raised (such as the management of the account's balance during transactional corrections as well as the date of expiry and the types of sub-accounts that the heir can provide in the case of inheritance), where we asked for a resolution from the Ministry for clarification. In response, we received the guidelines to be followed by the issuers of SZÉP cards.

***Developing cash trade***

In Q4, within the framework of compiling the Feasibility Study aimed at developing interbank cash trade offers were requested from another 6 IT development firms. Negotiations have taken place with a total of 9 IT development firms, and most of the firms came up with an offer. The offers received will be evaluated at the beginning of the next quarter by the delegated banking professional.

---

[19] See Chapter V

## VIII. Taxation and Accounting

### *Taxation*

On 19 October 2018, the draft law on the amendment of the tax laws (T/2931) was published on the Parliament's website. In connection with this draft, we submitted the comments of our members' experts to the Ministry of Finance. A highlighted issue is the option to enforce the net funding costs in the corporate tax base, needed to transpose the EU Directive against tax evasion (2016/1164). As of the 2019 tax year, the Corporate Tax Act enables group registration for corporate tax. The proposal of the Banking Association mainly concerned technical details and the rules of carrying losses forward. In the final text of the act, most of our clarification proposals were taken into account.

With regard to Section 3 (4) (r) of Act CXVI of 2012 on the financial transaction duty (hereinafter the Pti. tv.), effective as of 1 January 2019, we signaled to the Ministry of Finance that we consider its implementation impossible in technical terms, and we sent a proposed amendment to the text. Under the Pti. tv. as of January 2019, no tax is payable for payment transactions between customer accounts kept by the State Treasury (MÁK) and used by private individuals for sovereign debt trade and their payment accounts kept by another account keeper. The scope of exempt transactions is impossible for two reasons. On the one hand, in the MÁK system, transfers take usually place to central accounts, from where the MÁK allocates received amounts to individual customer accounts on the basis of identifiers specified in the message field. On the basis of the air transfer to central account, compliance with the condition provided for in the law is not possible. On the other hand, the account keeping financial institution has no information on whether the target account kept by the MÁK is held by a private individual, and if yes, whether the party initiating the transfer is identical to the holder of the MÁK customer account. In our amending proposal, we requested to exempt transactions between payment accounts of private individuals and the account kept by the treasury for sovereign debt trade, and that the amended provisions be applicable from 1 January 2019.

The Tax authority provided the opportunity to express our opinion in Q4 2018 on its reporting and tax return forms affecting the banking sector. Many comments were made on tax returns for the financial transaction tax and the special tax of financial organizations, as well as distributors and investment funds. Upon our request, the Tax Authority confirmed that no information is to be provided for retail transfers of a maximum of HUF 20,000. This information significantly simplifies member bank developments.

### *Reporting*

*NDIF TB and KBB reporting developments*

On 5 December 2018 we held a data structure consultation on the Banking Association proposals related to the new Total Deposit Portfolio (Teljes Betétállomány, TB), with the participation of our members and the NDIF. This consultation was not successful; no approximation of views took place. The NDIF expects contributions from member banks on the TB data model until 18 March 2019.

*2019 MNB reporting decrees*

In early September, the MNB held a consultation day on the 2019 decrees, on which we have sent comments and proposals, following several consultations. By taking these into account, the final 2019 decrees have been published in mid-November 2018.

After one year's preparatory work, the HITREG decree was published on 13 November 2018. In accordance with the earlier information from the MNB, the first reporting on the basis of this decree will take place on 17 February 2020, regarding 2019.

## IX. Developments within the Banking Association

### *International Relations*

*EMMI*

The Hungarian Banking Association has been a member of the European Money Markets Institute (EMMI) since 2017. In December 2018 the Secretary General of the HBA was elected into the EMMI Board of Directors, making him the first Central European member. This new position is important, as EMMI is planning to introduce its new hybrid methodology for EURIBOR (Euro Interbank Offered Rate) in the near future. Preparations for this started in 2013, and its testing phase was completed recently. The transitory tasks set by EMMI require significant professional work, to which the Hungarian Banking Association's Secretary General will also contribute, starting from December 2018.

*V8 meeting in Warsaw*

The "V8" meeting, the extended regional consultation of the banking associations of the Visegrád countries was held on November13-14, 2018 in Warsaw, organized by the Polish Bank Association. In addition to participating countries presenting their economic situation and main banking topics, the main topics discussed and presented about were the stabilization and economic role of foreign capital within the banking sectors of the Central and Easter European countries, current EU regulations and the practical management of foreign currency denominated loans, as well as cyber security challenges. The decision was also made to hold the next V8 event in the spring of 2019 in Budapest, linked to the Hungarian Banking Association's 30th anniversary program series.

### *CECBC Conference*

The Hungarian Banking Association and its member institutions took initiative to organize the Central European Covered Bond Conference in Budapest, on November 22-23, 2018. The main organizers of the event were the Association of German Pfandbrief Banks (Verband Deutscher Pfandbriefbanken; VdP) and the Hungarian Banking Association, with the help of the Magyar Nemzeti Bank, who provided the venue of the conference. A main topic of the conference was the new EU covered bond regulatory package, which was published by the Commission in March 2018. An advanced version of the text in the Parliament and the Council was already available at the time of the conference, which was discussed by domestic and foreign supervisory authorities, and regulatory and market actors. Other agenda items included triumphs and challenges concerning digitalization and possible instruments for developing the Central-Eastern European market.

### *Communications*

Q4 of 2018 was quite an active period in terms of communications, with regular media requests. According to our statistics, during the quarter we were featured in online media approximately 471 times, 62 times in printed media and 41 times in electronic media. Throughout the entire quarter, the Hungarian Banking Association had approximately 576 appearances in Hungarian media. During these three months, we responded to banking topics that were addressed by the press and the public by releasing a number of interviews and statements. The main communications topics of the quarter were card and ATM security, while current professional news included banking sector issues related to the introduction of PSD2 and the GDPR, as well as retail lending, more specifically terminated foreign currency lending and the Certified Consumer-Friendly Housing Loans. In order to raise consumer awareness, we joined the European communications campaign together with the Hungarian National Police Headquarters, the National Bureau of Investigation and the National Cyber

Security Center through in the issuing of information materials and in several media events shared with the authorities.

***Money Week: preparing for the 2018/2019 school year***
During the 2018/2019 academic year, schools will now have the chance to participate in the program series about finance and entrepreneurship a.k.a. Money Week for the fifth time. The program series will take place from February 25 to March 1, 2019, with the support of state, market and non-governmental organizations. From the 2014/2015 school year and on, the Hungarian program has joined the international European Money Week and the Global Money Week initiatives.
The organizers (the Hungarian Banking Association, the Ministry of Human Capacities, the Ministry of Finance, the Money Compass Foundation, the Ministry for Innovation and Technology and Junior Achievement Hungary) signed the six-party Cooperation Agreement on November 23, 2018 at the ITM, with the event open to the media. The main topic of this year will be: investment and savings. Curriculums have been prepared for four age groups and they have each been professionally reviewed (by banking and pedagogy experts – the latter from the Hungarian Institute for Educational Research and Development), while mock teaching sessions have been conducted to ensure a high level of professionalism. Detailed lesson plans, webinars and e-learning materials are available to help with preparations for the lessons. Several hundred schools had registered for the program by December, when the recruitment of volunteers started. A definitive goal for the Banking Association for 2018/2019 was to support the events of the program series by putting together a team of nearly 400 volunteers from all over the country. We regularly inform the Heads of Communications of our member institutions about the preparation process and opportunities to join in.

***Other working committees and working groups***

- *Creating a new working group: The Family Support working group*

The aim of the current government is to promote a family-oriented approach, which considers demographics in all areas of life: in politics, education, the economy and the scientific world as well. Many measures have been taken in favor of reaching the above mentioned goal. The person responsible for the government's family support provisions is dr. Katalin Novák, the state secretary of the Ministry of Human Capacities (EMMI). In addition, mainly for reasons pertaining to the budget, EMMI is in permanent collaboration with the Ministry of Finance. The Hungarian Banking Association supports the government's family policy aims, that is why on September 3, 2018 the HBA Board unanimously voted for the establishment of the Family Support working group. The aim of the working group is to aid the turnaround in demographics and to support families at sectoral level. The working group held its inaugural meeting on December 6, 2018. Participants included delegated colleagues from the HR and retail departments of the Banking Association's member institutions, as well as representatives of the Ministry of Finance, the Ministry of Human Capacities and Kopp Mária Institute. The working group Chair was elected and the working group's tasks were also established at the meeting.

- *Agriculture working committee*

During the quarter the committee consulted with a representative of the Ministry of Agriculture on carrying out the Rural Development Program (hereinafter: RDP) according to the state assessed in November 2018, on the new tenders, on calls that can be applied for, on commitments, on the sum of the aids paid, as well as on the European Commission's proposal for the general conditions of the Common Agricultural Policy 2020.
In response to the committee's request, the Hungarian State Treasury (hereinafter: MÁK) sent its resolution on the support received in connection with the area and the number of animals under the RDP. As regards the requests for payment of the support, it informed us that the final payments,

after having paid advances and instalments, will be made gradually, to be completed by March 2019 at the latest. At the same time MÁK stated that as for the payment of other possible individual requests that may have remained unpaid due to reasons outside of its scope, it plans to send the support to farmers concerned by June 30, 2019, the latest.
In addition, consultations were held with representatives from the public warehousing supervisory authority and the Hungarian Public Warehousing Association to evaluate last year's report on the warehousing market, to discuss the current state of the public warehouse market and the goals of the Public Warehousing Association for this year.

- *Internal control working group – benchmarking assessment*

Based on a cross-checked questionnaire, the working group conducted a benchmarking research, focusing on the following issues:

- The total number of staff in the internal control departments of member institutions, and within this, the colleagues carrying out central and network control tasks, methodology experts, IT auditors and the number of leaders and their ratio;
- The proportion of the number of internal control department staff to the credit institution it is in;
- The mapping out of important tasks carried out by the internal control department that do not belong to core activities (MNB contact, regulatory tasks, providing opinions to/approving regulations, operative tasks, fraud prevention);
- Which committee's work internal control participates in and what right it has to do so;
- Qualifications obtained by internal controllers (CIA, CISA, CISM, etc.).

Over half of the members of the working group (15 institutions) participated, including almost all larger institutions. Members discussed the results of the research in detail at the last working group meeting of 2018, complementing it by also discussing the practices in branch networks, agent networks and outsourced activities.

- *Digitalization working group*

The working group consulted with IdomSoft Zrt on the possible opportunities for the use of the e-ID cards in banking. The Nézőpont Intézet prepared a study containing proposals for cash-free payments under the topic of "whitening" the economy the aim of which is to further suppress the black market in the Hungarian economy. The working group collaborated with other working groups (Bank Cards, Payments, SEPA WGs) in inviting the experts of Nézőpont Intézet to present survey in detail.

- *IT Security working group*

The MNB sent its draft recommendation on "the use of social and public cloud services" which aims to transpose the recommendations on outsourcing to cloud service providers issued by the EBA into national law. It also aims to replace the MNB's previous recommendation on the use of social and public cloud services. We sent our new modification proposals and the reasoning behind them for the text of the draft recommendation to the MNB.

- *GIRO bank account switching*

During the inspections carried out at payment service providers the MNB criticized that the number of justifications for denials in documents of the GIRO bank switching service is much larger that what is provided for in government decree 263/2016. (VIII. 31.) on payment account switching. The position of the MNB is that it is necessary to significantly reduce the number of justifications.
In collaboration with the Hungarian Banking Association and GIRO Zrt., payment service providers examined the justifications for denial currently in use and recommended keeping other justifications in addition to the ones promoted by MNB, as well as rewording and clarifying them. Based on the MNB's resolution GIRO Zrt. made modifications to its application for GIRO Bank switching.

- *Mortgage bank real estate valuation working group*

The working group tasked with real estate valuation discussed the possibilities for creating a real estate database operated by MNB, possibilities for valuation without on-sight inspection, as well as starting to assess whether it is possible to reduce the area of residential real estate in a standardized manner. Opinions were given for the previously developed concept on the asset valuation expert register with regard to the GDPR and competition law. The working group reviewed the relevant legislative procedures and received information on the current state of the amendment proposals to the law on retail lending which also concerns asset valuation, as well as on the detailed rules of geodesy for real estate registry purposes and cartography. In addition, it consulted on the legislation regarding nearly zero-energy buildings.

- *Mortgage bank legal and capital market working group*

The central bank of Hungary consulted with the Hungarian Banking Association's relevant working group on the amendment of the MNB decree on the regulation of the forint maturity mismatch of credit institutions (MFAR) on several rounds. The text of the MNB decree was finalized in late 2018.
In Q4 the European Council adopted the general approach to the EU legislative package on covered bonds, and the European Parliament's mandate was also adopted, therefore the trilogue began in November, with the participation of the European Commission. The working group participated in the preparation of the EU materials containing national positions for the European Covered Bonds Council. These materials contain comments on the text proposals of individual EU institutions.
The working group initiated and actively participated in organizing the Central European Covered Bonds Conference on November 22-23.

- *SME working committee*

The SME working committee and the legal working group consulted with the representatives of the National Infocommunications Service Company Ltd. (NISZ), since, as a result of the further development of the Company Gateway, new access management functions became available in the previous quarter. Owing to this access may be given to individual items, and given users may be blocked from sending any. The aim of the consultation was to have working group members share their additional proposals, needs and comments at user level for developing the Company Gateway's new service. Committee members received the information that from January 1, 2019 on the delegated non-natural person business organization can only manage their tax administration for the National Tax and Customs Administration (NAV) electronically, through the Company Gateway or through the office gateway. Also starting from January 1, 2019, NAV will send its official documents to the client's Company Gateway or office gateway.

- *Leasing working group*

At its meeting the working group consulted with the representatives of the Ministry of Interior and the National Infocommunications Service Company Ltd. (NISZ) in order to simplify the current document office administration process, taking into account the numerous changes that took place within electronic administration. After the consultation the working group started to compile a presentation on the current process for the transfer of vehicle ownership and to compile a proposal for steering individual elements of the process towards electronic administration. The compilation is ongoing, once finished, the presentation and proposal will be sent out officially.
The working group also consulted with the representatives of Eximbank Zrt. with regard to the Export Recovery Leasing Program. After the meeting the working group initiated a multilateral consultation with representatives from the National Health Insurance Fund Manager in order to debate the

difficulties (request for provided employee certificates) presented by the leasing companies that are in contact with Eximbank through refinancing.

- *Documentary transactions working group*

At the meeting of the Documentary Transactions working group experiences were shared in connection with the joint guidance issues by the Hungarian Banking Association and the Compliance Verification Experts Body (TSZSZ). The guidance explains the role of TSZSZ in disputes about invoking bank guarantees for architectural/technical planning, building and construction contracts. After the consultation the working group prepared a proposal for amending the TSZSZ law in connection with cases that dispute the justification for other liabilities.

The working group also discussed the practical problems of completing the E-diary with the representatives of TSZSZ, The Ministry of Innovation and Technology and the Lechner Knowledge Center. The working group plans to conduct another trilateral consultation on the issue in 2019.

In addition, the working group proposed that the ICC Hungarian department of the Hungarian Chamber of Commerce and Industry be contacted to solve issues concerning the inconsistent translation of concepts also used in the Union Customs Code: guarantee /comprehensive guarantee.

- *Workout working group*

The Ministry of Justice set up the Insolvency working committee, which includes representatives from the Banking Association. The working committee holds meetings regularly; its task is to prepare the new law on insolvency procedures. The workout working group held regular meetings in Q4 to address the procedure and the tasks related to the working committee and represented the positions and proposals established at these during the Insolvency working committee’s meetings.

- Electing working group Chairs

- In recognition of his previous activity, the HBA Board nominated **Mr. Gergely Suppan (Takarékbank)** at its November meeting to become Chair of the *Macroeconomics working committee* for a year.
- The *Internal Control working group* re-elected its pervious chair, **Mr. Róbert Kollár (K&H)** for another three-year term. The HBA Board approved the result of this election at its meeting in December.
- The *Compliance working group* elected **Mr. András Bácsfalvi (MKB)** to follow Mr. Gábor Sudár (OTP) as the next Chair for a term of three years. The HBA Board approved this at its meeting in December.
- The *Leasing working group* voted at its meeting for **Mr. Tamás Pfandler (Budapest Bank)** to follow Mr. Dániel Hatvani (CIB) as Chair of the working group for a term of three years. The HBA Board approved the above at its meeting in December.

**ANNEX – INTERNATIONAL OUTLOOK: REGULATION, SUPERVISION**

## I Global Regulation

### *I.1 Financial Stability Board (FSB[20])*

***FSB preparations and reports for the G20 summit***

In October the Financial Stability Board held a plenary session to review the ***vulnerabilities of the financial system*** and to discuss the ***reports to the G20 summit***.

Having assessed *the market developments and vulnerabilities of the global financial system*, the FSB believes that the following warrant attention: (i) normalization of monetary policy in some advanced economies has contributed to a marked tightening of financial conditions in some emerging market economies; (ii) some asset classes – including real estate in a number of economies – are showing signs of overvaluation; (iii) geopolitical uncertainties persist.

The Plenary considered that *risks stemming from the snap-back in interest rates* could be particularly relevant. Interest rate rises and widening credit spreads increase debt service costs, which leads to the reassessment of corporate and sovereign risks, especially in emerging and developing economies. *The core of the financial intermediary system is much more resilient* than before the global financial crisis, with strengthened bank capital and liquidity. At the same time, *non-bank financial intermediation (NBFI*[21]*) has grown,* adding to diversity of funding, but with associated maturity and liquidity transformation risks, and concentrations in holdings of risky assets. New forms of interconnectedness have emerged that could, in some scenarios, act as channels for domestic and cross-border amplification of risks. The FSB highlighted that authorities should consider using their existing instruments to build resilience, particularly macroprudential buffers where appropriate.

Plenary members discussed the main elements of the *FSB work program for 2019 and future years*, including potential deliverables to the G20 next year during the Japanese Presidency. The work program will focus on (i) finalizing and operationalizing post-crisis reforms; (ii) monitoring the implementation and evaluating the effects of post-crisis reforms; and (iii) addressing new and emerging vulnerabilities in the financial system.

Specific new initiatives include:

- An evaluation on the effects to date of reforms to end too-big-to-fail, which will be launched in early 2019 and completed in 2020.
- An initiative to explore ways to address the risk of market fragmentation.
- A project on financial stability implications of decentralized financial technologies.
- A project to develop effective practices relating to a financial institution's response to, and recovery from, a cyber incident, on which a progress report will be published by mid-2019.

The FSB prepared and submitted the following **reports to the G20 Summit** in Buenos Aires in November 2018:

- Fourth annual report on the implementation and effects of the G20 financial regulatory reforms.
- Evaluation of the effects of financial regulatory reforms on infrastructure finance,
- Incentives to centrally clear over-the-counter (OTC) derivatives: A post-implementation evaluation of the effects of the G20 financial regulatory reforms – final report

---

[20] Financial Stability Board: the highest international financial regulatory body

[21] ***non-bank financial intermediation***: the FSB has decided to use this term consistently in the future instead of "***shadow banking***"

- Report on FSB member jurisdictions' actions to remove legal barriers relating to OTC derivatives trade reporting
- Progress report on the action plan to assess and address the risks from the decline in correspondent banking relationships
- Cyber Lexicon
- Climate-related Financial Disclosures: Status Report
- Progress report on reforming major interest rate benchmarks
- Second phase of the G20 Data Gaps Initiative (DGI-2): Third Progress Report
- 2018 Resolution Report
- Discussion paper on financial resources to support CCP[22] resolution and the treatment of CCP equity in resolution

In addition to the above, jurisdiction-specific profiles on the implementation of reforms and jurisdictions' responses to the IMN survey are also available on the FSB's website.

In addition the above mentioned items, the following topics were also discussed at the FSB Plenary in October:

- Systemic risk in the insurance sector;
- Non-bank financial intermediation;
- FSB internal processes and transparency review;

received updates about ongoing workstreams.

***Appointment of new FSB Chair and Vice Chair***

Starting from December 2, 2018, the Plenary of the FSB appointed Randal K. Quarles (Governor and Vice Chairman for Supervision at the US Federal Reserve) as its new Chair and Klaas Knot (President of De Nederlandsche Bank) as Vice Chair. The Plenary also agreed that after three years on 2 December 2021 Klaas Knot will take over as Chair for the next three-year term.

FSB Plenary members expressed their gratitude to the last FSB Chair, Mark Carney for his exemplary leadership over the past seven years.

***Annual report on the tof the G20 leaders on the financial regulatory reforms***

The FSB compiled its fourth Annual Report on Implementation and Effects of G20 Financial r*egulatory Reforms. The report, delivered to the G20 Summit calls for the support of the world's leaders in implementing the agreed reforms, and reinforcing global regulatory cooperation.*

- Regulatory and supervisory bodies should lead by example in promoting the timely, full and consistent implementation of remaining reforms to Basel III, resolution regimes, OTC derivatives and non-bank financial intermediation. This will support a level playing field and avoid regulatory arbitrage.
- Frameworks for cross-border cooperation between authorities should be enhanced in order to build trust, allow for the sharing of information, and to preserve an open and integrated global financial system.
- Authorities should evaluate whether the reforms are achieving their intended outcomes, identify any material unintended consequences, and address these without compromising on the objectives of those reforms.

[22] central counterparties

- Financial stability authorities should continue to contribute to the FSB's monitoring of emerging risks and stand ready to act if such risks materialize.

***Potential financial stability implications from crypto-assets***

Back in October, the FSB published *Crypto-asset markets: Potential channels for future financial stability implications.* The report assesses the primary risks present in crypto-assets and their markets, such as low liquidity, the use of leverage, market risks from volatility, and operational risks. Based on these features, *crypto-assets lack the key attributes of sovereign currencies and do not serve as a common means of payment, a stable store of value, or a mainstream unit of account*.

Based on the available information, *crypto-assets do not pose a material risk* to global financial stability at this time. However, vigilant monitoring is needed in light of the speed of market developments as the spreading of crypto-assets could have implications for financial stability in the future, such as confidence effects and reputational risks to financial institutions and their regulators; risks arising from direct or indirect exposures of financial institutions; risks arising if crypto-assets became widely used in payments and settlement; and risks from market capitalization and wealth effects.

Crypto-assets also raise several broader policy issues, such as the need for consumer and investor protection; strong market integrity protocols; anti-money laundering and combating the financing of terrorism regulation and supervision, including implementation of international sanctions. (Relevant national and international measures are outside the primary focus of the report.)

National authorities and standard-setting bodies have issued numerous warnings to investors about the risks from crypto-assets. At the same time the underlying distributed ledger technology (DLT) should be supported to enhance the efficiency of the financial system. Authorities must find the right balance between promoting innovation and adequately managing risks.

***I.2) Basel Committee on Banking Supervision (BCBS)***

***Reports on Basel III Standards***

The Basel Committee on Banking Supervision has been regularly publishing its reports monitoring the implications of the Basel III standards for banks. The results of this exercise in October are the first to consider the impact of the finalization of the Basel II reforms in December 2017.

The Committee also regularly assesses the *implementation of the Basel III standards in individual jurisdictions.* The Fifteenth progress report on adoption of the Basel regulatory framework, which depicts the state of September 2018 also takes the important decisions made in December 2017 into consideration. The report is based on information provided by individual members as part of the RCAP[23].The report includes the status of adoption of the Basel III risk-based capital standards, the leverage ratio, the standards for global and domestic SIBs and interest rate risk in the banking book (IRRBB), the Net Stable Funding Ratio (NSFR), the large exposures framework and the disclosure requirements.

A *report to G20 Leaders* was also made on the implementation of the Basel III regulatory reforms.

The Basel Committee' governing body, the Group of Central Bank Governors and Heads of Supervision, set as a high priority the full and effective implementation of the adopted Basel standards within the globally agreed time frame.

***Pillar 3 disclosure requirements - updated framework***

---

[23] Regulatory Consistency Assessment Programme

The BCBS published *updated Pillar 3 disclosure requirements*. These requirements, together with the updates published in January 2015 and March 2017, complete the Pillar 3 framework. Pillar 3 of the Basel framework seeks to *promote market discipline* through regulatory disclosure requirements. The revised Pillar 3 framework reflects the Committee's *December 2017 finalized* Basel III standards and pertains to the following areas:

- credit risk, operational risk, the leverage ratio and credit valuation adjustment (CVA) risk;
- risk-weighted assets (RWAs) as calculated by the bank's internal models and according to the standardized approaches; and
- an overview of risk management, RWAs and key prudential metrics.

In addition, the updated framework sets out new disclosure requirements on asset encumbrance and, when required by national supervisors at the jurisdictional level, on capital distribution constraints.

The standard incorporates feedback collected during the February 2018 public consultation from Pillar 3 preparers and users. In particular, the CVA disclosure requirements have been substantially streamlined.

The implementation deadline for the disclosure requirements is *1 January 2022*, which accords with the introduction of the finalized Basel III standards. The implementation deadline for the disclosure requirements for asset encumbrance, capital distribution constraints and the prudential treatment of problem assets has been extended by one year to end-2020.

***Revisions to leverage ratio disclosure requirements***

The Basel III leverage ratio standard comprises a 3% minimum level that banks must meet at all times, a buffer for global systemically-important banks and a set of public disclosure requirements. For the purpose of disclosure requirements, *banks* must report the leverage ratio *on a quarter-end basis or*, subject to approval by national supervisors, report a measure based on *averaging*.

Heightened volatility in various segments of money and derivatives markets around key reference dates (e.g. quarter-end) has alerted the Basel Committee to potential regulatory arbitrage by banks. A particular concern is *"window-dressing"*, in the form of temporary reductions of transaction volumes in key financial markets around reference dates resulting in the reporting and public disclosure of elevated leverage ratios. In this regard, the Committee published a *newsletter* in October in which it indicated that window-dressing by banks is unacceptable, as it undermines the intended policy objectives of the leverage ratio requirement and risks disrupting the operations of financial markets.

This consultative document seeks comments on revisions (up until March 13$^{th}$) to leverage ratio Pillar 3 disclosure requirements to include, in addition to current requirements, mandatory disclosure of the leverage ratio exposure measure amounts of securities financing transactions, derivatives replacement cost and central bank reserves as calculated using daily averages over the reporting quarter.

Prior to the above, in October the Committee launched a consultation on the *treatment of client cleared derivatives when calculating the leverage ratio*. Possibly changing the current practice would serve to prevent excessive leverage and to promote central clearing of standardized derivatives contracts.

***Incentives to centrally clear over-the-counter (OTC) derivatives***

The final report from the BCBS and other standard-setting bodies (the FSB, CPMI[24] and IOSCO[25]) examines the effects of G20 financial regulatory reforms on the incentives to centrally clear over-the-counter (OTC) derivatives.
The report concludes that the reforms - particularly capital requirements, clearing mandates and margin requirements for non-centrally cleared derivatives - are achieving their goals *of promoting central clearing, especially for the most systemic market participants.* This is consistent with the goal of reducing complexity and improving transparency and standardization in the OTC derivatives markets. Beyond the systemic core of the derivatives network of central counterparties, dealers/clearing service providers and larger, more active clients, the incentives are less strong.
The report also identifies some reform areas that may merit potential adjustments or need further reforms, bearing in mind the original objectives of the reforms.

***Stress testing principles***
After its public consultation announced in December 2017, the Basel Committee issued its *Stress testing principles*, which replace its guide issued in May 2009. The 2009 principles were designed to address key weaknesses in stress testing practices as highlighted by the global financial crisis. Since then, the role of stress testing has rapidly evolved and grown in importance in many jurisdictions. The updated principles reflect that stress testing is now both a *critical element of risk management for banks* and *a core tool for banking supervisors and macroprudential authorities*. The updated principles are set at a high level so that they can be applied across banks and jurisdictions while remaining relevant as stress testing practices continue to evolve.
The principles are guidelines that focus on the core elements of stress testing frameworks: targets, governance, policies, processes, methodology, resources and documentation that guide stress testing activities. Each principle is followed by a short description of considerations that are equally relevant for banks and authorities. This description is followed by additional points  fro banks, with particular relevance to banks' own internal stress testing activities and their participation in bank-run supervisory stress tests, as well as additional points for authorities, with particular relevance to supervisor-run stress tests and the authorities' role in bank-run supervisory stress tests. They also cover the role of authorities in their oversight of banks' internal stress testing activities.

***Report on cyber-resilience: a range of practices***
In December the BCBS published a report in which it presents the range of observed bank, regulatory and supervisory cyber-resilience specificities and practices across jurisdictions.
The report is based on the analysis of authorities' responses to previous international surveys, on exchanges between international experts and on input from market players.
The current challenges and initiatives to enhance cyber-resilience are summarized in *10 key findings* and illustrated by case studies. These key finds concern general landscape, strategy, cyber risk management, governance/organization, workforce, testing, incident response, metric, information sharing and third party risk.
By describing the diversity of approaches thematically, the report will help banks and supervisors navigate the regulatory environment and will serve as useful input for identifying areas where further policy work by the Committee may be warranted. Going forward, the Committee will *integrate* the cyber dimension into its broader operational resilience work.

---

[24] Committee on Payments and Market Infrastructures. It operates within the framework of BIS, similarly to the Basel Committee on Banking Supervision.
[25] International Organisation of Securities Commissions

## II European Regulation

In the fourth quarter due to the European elections of May 2019, the setting up of the new European Commission, and the considerable number of legislative procedures on the agenda in the field of finance no preparations were launched to create new Level 1 (directive and regulation) or Level 2 (delegated directive and regulation, as well as RTS and ITS) legislation. EU institutions did however make significant efforts to close open dossiers and procedures in progress.

### *The European Commission's 2019 Work Program*

The Commission work program for next year was issued towards the end of October and does not contain any initiatives that would deeply impact the banking sector's regulatory issues. In contrast, the REFIT[26] initiatives envisage the review of three new legislations, and the regulatory amendment proposals resulting from it will directly influence the activities of financial service providers:

- The evaluation of the consumer credit and the directive on the distance marketing of consumer financial services will look into the functioning of the consumer credit market and the distance marketing and selling of retail financial services. It will primarily deal with the elements of providing information to consumers, such as that of examining the information provided about sales, including basic information found in advertising or the lack thereof (APR, interests, expenses and other important information).
- *The Fitness Check of supervisory reporting* will analyze cross-sectoral reporting requirements to supervisory authorities stemming from EU Financial Services Legislation (e.g. Capital Requirements Directives - CRR/CRDIV, Markets in Financial Instruments Directive - MiFID/MiFIR, European Market Infrastructure Regulation - EMIR etc.).
- *The Fitness Check of corporate reporting* will evaluate corporate reporting requirements including the Accounting Directive, the Non-financial reporting Directive, the Transparency Directive, and the International Accounting Standards Regulation (IFRS).

In addition to the above, the Work Program ambitiously undertakes to complete currently open regulatory packages concerning banking and the Capital Markets Union. The regulations and reviews to complete are the following:

- Risk Reduction Package (RRP – see in detail below);
- Review of the recovery and resolution of central counterparties (CCP);
- Amending the Capital Requirements Regulation (CRR) with regard to the minimum loss coverage for non-performing exposures;
- Topics to close in connection with the Capital Markets Union:
    - Creating an EU covered bonds framework;
    - Facilitating the cross-border distribution of collective investment funds;
    - Regulating crowdfunding;
    - Introducing a Pan-European Personal Pension Product (PEPP) regulation;
    - The prudential regulation of investment firms (IFD, IFR), which will include the prudential rules for non-systemic investment firms, which will in turn be pulled from regulations on capital requirements;
    - Modifications to promote SMEs' financing through capital markets;
    - Review of the licensing, supervision and recognition of CCPs within the framework of amending EMIR;
    - The law applicable to the third-party effects of assignments of claims:

[26] Regulatory fitness and performance (REFIT) programme - the Commission's program for targeted and effective regulation

- Modification of the regulations on insolvency (concerning the preventive restructuring frameworks, second chance, and measures to increase the efficiency of insolvency and discharge procedures);
- Re-regulating European supervisory authorities and the ESRB (with the relevant complementary tasks and scope of application of these authorities added in as a result of the Maltese, Estonian and Danish money laundering scandals).

- Finishing the modifications made in connection with the review of the European Market Infrastructure Regulation started in 2015;
- Finalizing the directive on the representative actions for the protection of the collective interests of consumers.

***Agreement on the banking regulatory package***
Towards the end of November the negotiating parties of the trilogue came to an agreement about the details of the risk reduction package. The EU Economic and Financial Affairs Council reinforced this on December 4th. The following compromises were made on the issues that were open prior to the agreement.

***Issues concerning prudential regulation***
- According to the agreement, *capital requirement would be decreased for pension and salary-backed loans* (from 75% to 35%) with the aid of certain guarantees and risk reducing factors, in consideration of their low default risk.
- Small non-complex institutions would get the advantage of a simplified disclosure and reporting obligations. The EBA was authorized to create the framework for this. The EBA's targeted a minimum of 10% reduction of expenses for the above, up to a target of 20%, if possible.
- In order to support derivatives backed by margins, trade financing and similar short-term trade financing techniques such as factoring, the NSFR[27] will be recalibrated, while the symmetrical management of repo and passive repo transactions will be realized.
- A *simplified NSFR* (sNSFR) will also be introduced, to be applied by small-sized, non-complex institutions. The sNSFR will require fewer data points to be collected, however, it will remain at least as conservative and safe as the fully-fledged metric.
- Supporting factors for SMEs: extending the existing supporting factor for loans to SMEs in an amount up to EUR 2.5 million (up from 1.5 million), the scope of which would also be extended to certain infrastructure projects.
- Changes made to requirements on own funds:
  - *Holdings in insurance subsidiaries* ("Danish Compromise"): a transitional period is provided for that would allow institutions not to deduct certain types of insurance holdings until 31 Dec 2024;
  - Profit and loss transfer agreements will be recognized upon adherence to certain criteria;
  - Minimum Value Commitments (MVC) will be assigned a credit conversion factor of 20%;
  - An exemption from deductions of *certain intangible software assets* is granted from own fund items provided that certain requirements are fulfilled. The mechanics and details of the non-deduction will be set out in an EBA regulatory technical standard.
- In connection with sustainability requirements, the EBA was mandated to produce a report on the prudential treatment of "green" and "brown" assets (penalizing RWA factors for assets posing environmental risk).
- The introduction of new reporting requirements with regard to the new standards concerning the FRTB[28]. The final standards should be implemented as soon as they are finalized at international level.

---

[27] Net Stable Funding Ratio
[28] Fundamental Review of the Trading Book

- Intermediate parent undertaking (IPU): large non-EU banking groups with two or more subsidiary institutions in the EU would be required to establish an intermediate parent company to consolidate all their activities in the Union under that IPU.
- The EBA also received authorization to conduct a study to assess the feasibility of an integrated reporting system for all EU banks.

***Issues concerning rules on resolution***

- If the MREL requirement is not fulfilled MREL related MDAs[29] will be applicable following a grace period of nine months, with no automaticity.
- Moratorium maintained at the internationally accepted 48 hours after the state of FOLF[30] is determined.
- Institutions that are failing or likely to fail, but not subject to resolution, would be wound up in an orderly manner in accordance with the applicable national law.
- As regards massive asset disposals, the new provisions would help banks with high level of non-performing loans to dispose of them with a limited impact on their capital requirements, subject to certain requirements and within a pre-determined timeframe.
- A limit of 27% of total risk exposure amount in Pillar 1 convertible requirements for MREL and 30% in Pillar 2 was determined for global systemically important institutions, where 8% of total liabilities and own funds (TLOF) is higher than this value. If the resolution authority wishes to set a higher requirement in domestic regulation, it needs to provide due reasoning.
- subject to an assessment of the resolution authority, for Top Tier banks the total risk exposure amount (TREA) metric shall be applied when certain criteria are met and taking into account the risk of disproportionate impacts on business models, without going below 27% TREA, where 8% of total liabilities and own funds (TLOF) leads to a higher Pillar 1 subordination requirement than 27% TREA; such limitation of the Pillar 1 requirement at 27% TREA, subject to an assessment of the resolution authority, would be without prejudice to the possibility of requiring additional subordination through Pillar 2;
- Two alternatives to be chosen under own discretion were given to member states to *safeguard the sale of MREL instruments to retail customers*:
    A. Option A: retail investors with an investment capacity below EUR 500,000 may only invest a minimum initial amount of 10,000 EUR in those instruments representing not more than 10% of their investment capacity;
    B. or – Option B: a minimum denomination of EUR 50,000 (for member states with a smaller capital market this may be EUR 10,000).

According to current documents the new regulations would enter into force on the twentieth day following their official announcement. In accordance with standard practice they would need to be implemented by member states two years after their entry into force.

***Speeding up the regulatory processes for the Capital Markets Union (CMU)***

The European Commission's Work Program for 2019 includes the completion and entry into force of Level 1 regulations for the CMU. Based on the status of dossiers under consultation, this will be a challenging commitment to undertake. In order to speed up processes in its Communication published at the end of November, the Commission asked the institutions participating in the legislation process to make the necessary efforts to fulfil this commitment. It emphasized that out of the 13 regulatory topics undertaken for the CMU 10 are pending and out of these only 2 (insolvency procedures and Pan-European Personal Pension funds) are in the trilogue phase, to be completed quickly (the formerly mentioned topic was completed at the end of the year).

---

[29] Maximum Distributable Amount
[30] Failing or Likely to Fail

***Developments regarding other Level 1 regulatory dossiers in progress***

- In mid-December the Council and the Parliament reached consensus on the *amendment of the insolvency directive*. The modifications made must be transposed into national legislation within two years of their official publication.
- In mid-December consensus was also reached within the Council on the amendment of the CRR with regard to minimum loss coverage for non-performing exposures, thus allowing for the trilogue to begin.

***Important EBA and ESMA regulatory processes***

- In mid-November the EBA finalized its draft regulatory technical standards specifying the nature, severity and duration of an economic downturn, which completes the implementation of internal model-based risk management. In addition, the EBA is also currently finalizing the Guidelines on the estimation of loss given default appropriate for conditions of an economic downturn.
- In mid-December the European Supervisory Authorities (ESA) published a joint draft RTS on risk mitigation techniques for OTC derivatives not cleared by a central counterparty.
- The EBA also published two guidelines in mid-December. The guidelines on disclosure of non-performing and forborne exposures will be in effect from late 2019, while the guidelines on the STS[31] criteria in securitization will enter into force on May 15, 2019.
- Throughout Q4 the EBA held several consultations about technical modifications (primarily concerning reporting). In addition in mid-December an important consultation on guidelines to establish requirements for credit institutions, investment firms and payment service providers on the mitigation and management of their information and communication technology risks. The consultation will run until mid-March.
- In mid-December the ESMA launched several consultation in connection with sustainable finance initiatives, which concern the directives regarding financial market instruments (MiFID II) and those regarding investment funds (AIFMD, UCITS[32]). The consultation will end on February 4, 2019.

[31] STS: simple, transparent and standardized

[32] Markets in Financial Instruments Directive II (MiFID II), Alternative Investment Fund Managers Directive (AIFMD), Undertakings in Collective Investment in Transferable Securities (UCITS)