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News for the Board of Directors, February 2020

Dear members and friends,

Today we will start with a great presentation from SEC Commissioner Elad L. Roisman.

Myths and Realities: Modernizing the Proxy Rules

I. Introduction

Thank you, Dean [Steven] Payne and David [Blass] for the kind introduction and for the concise summary of the recent SEC proposals to update the rules governing the solicitation of proxies and submission of shareholder proposals.

Thank you also to the Catholic University Columbus School of Law for hosting me and, in particular, to the students, who have come to hear me speak. Before I dive in, I want to make clear that my remarks are my own and do not represent those of the Securities and Exchange Commission ("SEC") or its other commissioners.

Giving further context to the summary you just heard, some of the rules we have been discussing date back to 1954. You can imagine how much has changed in our markets since these particular rules were last amended: including shifts in how public company shares are held and voted and changes in who relies on the SEC's exemptions to the proxy solicitation rules.

From my perspective, the SEC's proposals to modernize these rules were not only necessary, but long overdue. Yet the reaction from the loudest voices came swiftly and furiously. Even before the Commission voted on these proposals, the agency was accused of serving as a shill for corporate interests, suppressing shareholder votes, and sheltering CEOs of big corporations from accountability.

Today, I hope to address some of the most common myths these criticisms invoke, and describe what I see as the reality of the situation. My intention in doing this is not only to further clarify my own views on the SEC's

proposals, but also to dispel an atmosphere of negativity that might dissuade interested people from offering valuable feedback on their content.

II. Materially False or Misleading Statements of Fact

Myth: The SEC's proxy modernization agenda is driven by the lobbying efforts of corporate interests.

I want to address this myth first by making one thing clear to anyone who may not know: the Commission does not act at the behest of lobbyists. No one commenter or group of market participants dictates the agency's agenda or approach to an issue.

We receive input from and listen to the concerns of all market participants and the public. That is our job. In fact, the law generally requires us to consider comments we receive from the public when we propose to make changes to our regulations.

In the case of the two proposals here, the staff had the benefit of public comments that were submitted in connection with the 2018 Proxy Roundtable as well as input from several other requests for comment on similar issues, raised over the last two decades.

Anyone who reads our two proxy proposals will see that they do not reflect wholesale acceptance of any particular market participant's ideas for reform or change.

Rather, they demonstrate a good faith attempt to serve the interests of all market participants through a careful combination of policy and pragmatic questions about how the current rules can be improved.

For my own part, since joining the Commission, I have had more discussions (internally and externally) on proxy reform than almost any other topic.

I have not turned down a single meeting request on this topic, and I have benefitted from hearing perspectives on all sides.

In particular, many of these meetings were with representatives of institutional investors and asset managers, who expressed concerns about the SEC pursuing large-scale reforms to the proxy voting process.

Their concerns resonated with me, and—based on my read of the proposals—I would venture to say that this input informed the staff's thinking as well, as they aimed to achieve the proposals' objectives in a very

tailored manner, using practices and strategies already accepted in the marketplace.

Myth: The SEC is suppressing shareholder votes.

This one is easy to address. Neither of the Commission's proposals alters a shareholder's right to vote in any way, either in person at a company's annual meeting or by proxy.

The SEC's proposals address (1) the requirements for shareholders to submit voting proposals on the corporate ballot, and (2) the requirements of third-party service providers relying on SEC exemptions to provide recommendations to shareholders about how those shareholders should vote their shares, to rely on exemptions from the SEC's rules regarding proxy solicitation.

Myth: The SEC is making it prohibitively expensive for retail investors to submit shareholder proposals.

Some have decried that the proposal to amend the initial submission thresholds raises the minimum ownership requirement from $2,000 to $25,000.

Were that statement made by someone subject to our antifraud rules, I would characterize it as "materially misleading," as it omits a key element of the proposal: time.

The intent of the proposed changes to submission thresholds is not to exclude smaller retail investors. Rather, the goal is to ensure that those submitting proposals have demonstrated more than a short-term interest in a company.

Specifically, for those who hold $2,000 worth of shares in a company, our proposal would not raise the monetary threshold at all. Instead, it would require that such an investor hold this amount of stock for longer than is currently required—three years, instead of one year—before submitting a proposal.

I would be interested to hear from retail investors whether they want the money they have invested in a company to be spent by other shareholders with a limited, short-term interest in that company.

Wouldn't they want the shareholder proposal process utilized by those who have a demonstrated interest in the company's continued success?

The fact is that most proposals today come from a miniscule fraction of shareholders.

While some are undoubtedly well intentioned, some proponents appear to be using this system to promote their own social or political agenda without any regard for the specific company funding the ballot and its long-term success. Their efforts to broadcast their views to corporate America through the proxy process impose costs on all other shareholders. I, for one, would like to close loopholes that currently allow people to do this.

Myth: The SEC is making it easier for CEOs to spend shareholder money.

I must admit, this assertion confused me. But, I heard it, so I will respond. Neither of the Commission's proposals reallocates any money. The irony of this myth is that the Shareholder Proposal Rule amendments, in particular, aim to preserve company (and therefore shareholder) money.

Changing the resubmission thresholds as proposed would curb the ability of a small subset of shareholders to spend the money of all other shareholders in furtherance of causes that the vast majority of other shareholders have repeatedly rejected. This happens far too often today.

Our Shareholder Proposal Rule has been amended many times since it was initially adopted, with changes specifically designed to address concerns of abuse by shareholders with limited interests in the company.

For anyone today to pretend that our current proposal is unprecedented ignores the rule's history. This history has been extensively written about, most recently in the lengthy background and history section of the proposal itself.

Myth: Under the proposed rules, CEOs could now sue Proxy Voting Advice Businesses if they criticize the company.

This is wrong for at least two reasons. First, antifraud liability under the SEC's Rule 14a-9 is not new. Second, the standard of 14a-9 liability is "materially false or misleading," not "I don't like it."

Allow me to elaborate. As the Commission explained in the guidance we released this past August, we reiterated our longstanding view that generally, proxy voting advice is a solicitation. If you are interested in the history and consistency of that interpretation, I encourage you to read that release, as well as the proposing release which goes into further detail.

To my second point on materiality, any cause of action against a proxy voting advice business under Rule 14a-9 would have to be based on more than a company's dissatisfaction with any particular recommendation.

These businesses' recommendations are held to the same standard as solicitations from companies, activist investors, or anyone else who is soliciting proxies.

None of these entities may make any "statement which, at the time and in the light of the circumstances under which it is made, is false or misleading with respect to any material fact, or which omits to state any material fact necessary in order to make the statements therein not false or misleading or necessary to correct any statement in any earlier communication with respect to the solicitation of a proxy for the same meeting or subject matter which has become false or misleading."

I see no reason why proxy voting advice businesses should be treated differently from every other soliciting party. And, for those who vehemently oppose this view, I ask: Why in the world would we want investors making voting decisions based on advice that is false or misleading with respect to a material fact? Or worse, why would we grant someone a license to make such statements without liability?

Myth: By allowing companies to review proxy voting advice businesses' solicitations before publication, you will compromise the independence of these businesses.

I have taken a keen interest in hearing from commenters suggesting this, mainly because the Rule 14a-2(b) proposal has been modeled after current market practices.

The two proxy voting advice businesses who have held the vast majority of this market both currently offer opportunities for certain issuers to engage with them and respond to their final voting advice. (ISS has for years granted this opportunity to the largest companies in our markets, and Glass Lewis recently instituted programs to obtain feedback from issuers on the data underlying their reports and the reports themselves.)

These practices were not driven by regulatory requirements, but by the firms' own impetus. The proposal aims to make sure that they are available to all issuers (including smaller ones, who might not have as great a research following as the S&P 500) and other soliciting parties, such as activist investors in a proxy contest, and in a more timely manner.

I believe such a measure could offer investors the opportunity to make more informed decisions when they vote.

In one place, they would have access to the voting advice and the soliciting party's perspective for ready consideration.

To the extent an issuer or other soliciting party believes the firm's voting advice contains errors or methodological biases, it would have a time and place to note that in a way that voting advice business clients can more easily access than they can today. For these reasons, I cannot understand how anyone would argue that this proposal is anything but an improvement upon the status quo.

I will also note that the proposal was careful to preserve the boundaries between proxy voting advice businesses and the companies they review.

The proposal made clear that voting advice businesses would not have to make any changes to their reports in response to the companies' feedback.

The voting advice business would only be required to include a hyperlink in its report to the company's response statement, rather than including such content in the report itself.

In this way, the proposal seeks to maintain separation between the perspectives of the proxy voting advice businesses and companies. If anyone has feedback on whether there is a better way to accomplish our goals and preserve the independence of voting advice businesses, I would be glad to hear it.

I will circle back to this concept of independence toward the end of my remarks.

Myth: These proposed rules are so burdensome that they will stifle competition in the proxy voting advice business market.

As a believer in the positive power of free markets, I am always concerned about overly burdensome regulation that entrenches incumbent market participants and freezes out others. I believe the proposals try to avoid this by taking a light-touch approach to the SEC's oversight of proxy voting advice businesses.

For example, rather than require voting advice businesses to follow onerous regulatory procedures to have the Commission review their voting procedures and methodologies (as some policy-makers have advocated for), the proposals are modeled after current market practices—calling for such businesses to disclose their conflicts of interests and allow time for company review and response before publication.

Additionally, since competition in the industry is an important concern, we have taken care to provide an alternative proposal for public comment, specifically asking whether we should exempt smaller proxy voting advice businesses from these requirements. Everyone has the opportunity to respond to this question, and I hope we receive constructive feedback.

Myth: The SEC is attempting to solve a problem that does not exist.

I have heard some institutional investors and asset managers ask why we felt the need to propose any changes to the proxy solicitation rules. They have stated that the proxy voting advice businesses' clients are happy with their voting advice and don't worry so much about any errors or methodological weaknesses in these reports.

But institutional investors and asset managers are not the only investors that the SEC is charged to protect. And, in this context, I worry much more about the ultimate retail investors, who may have a substantial portion of their life savings invested in our stock markets.

These Main Street investors increasingly invest their money in funds and will benefit from (or bear the cost of) institutional investors' or asset managers' voting decisions. In essence, I believe it is our job as regulators to help ensure that such advisers—fiduciaries, who take on voting authority for their clients—vote proxies in a manner consistent with their fiduciary obligations and that the proxy voting advice upon which they rely is complete and based on accurate information.

For many years, institutional investors and asset managers relied extensively on proxy voting advice businesses to tell them how to vote shares held by their underlying clients.

In the past year, the Commission clarified that investment advisers cannot outsource their voting decision-making to these third parties.

But, it is clear that many do and will continue to rely on their advice as inputs in voting decisions, so much so that a large group of institutional investors recently characterized proxy voting advice businesses' recommendations as "market-moving."

In light of this, how could anyone argue that the SEC should not care about proxy voting advice businesses' recommendations, or whether they are influenced by the types of conflicts of interest, errors, or methodological biases that have been brought to the SEC's attention?

III. Independence: Myth or Reality?

Before I conclude, I will tell you about a particular concern I have about the independence of proxy voting advice businesses, which I can only hope is a myth. I have been told that some asset manager clients of these businesses use them as a "fig leaf."

As it was explained to me, everything in proxy voting advice business reports is in there because certain asset managers get together and decide, for instance, that they do not like a particular member of a company's board of directors.

They then instruct the proxy voting advice business to recommend a vote against the director.

The term I heard for this practice is "social arbitrage," a way for an asset manager to vote against a company, while maintaining its relationship with management so that it can sell products to that company such as providing 401(k) services.

A coordinated effort along the lines I just described is deeply troubling to me.

This is exactly the type of conflict of interest I worry about—that a proxy voting advice business might base its general proxy voting advice to all its clients on the preferences of a select group of its own clients, whether they are asset managers or shareholders themselves.

I believe that this type of conflict should be disclosed to all consumers of proxy voting advice businesses' reports. Also, I think this type of behavior could represent a potential Section 13D violation.

IV. Conclusion

The impetus for this speech was not to convince you that the SEC's proposed rules to modernize the proxy process are perfect as-is.

People have questioned certain aspects of them, and I am open to changing my mind on anything and everything the Commission has proposed.

My goal, however, is to encourage constructive feedback.

For two decades, the Commission has sought comment and deliberated in general terms about how to modernize our proxy rules.

During this time, many commenters submitted general arguments about how they thought the system should change or not change.

On November 5 of last year, the Commission put forward specific rule proposals.

In voting to support them, I held out hope that all those who have expressed so much interest over the years would now comment on these

specific proposals, and offer particular feedback on how they could improve.

Yet, in some of the reporting and the comment file, I have seen many generalities, recycled from comment letters predating the recent proposals.

More disturbingly though, I have also seen comments suggesting dissatisfaction, based entirely on misinformation. Thus, today, I have aimed to dispel some of the myths that I have heard, which might prevent constructive dialogue, from which we can all benefit.

I remain hopeful that, as we progress through the comment period, we will receive feedback on the specifics of the proposals which will help us determine how—not if—to move forward.

Thank you.

Stress testing in Latin America: A comparison of approaches and methodologies

BIS Papers, No 108. Report submitted by a study group established by the BIS CCA Consultative Group of Directors of Financial Stability (CGDFS) and chaired by Pamela Cardozo, Bank of the Republic, Colombia. Monetary and Economic Department, February 2020.

Since the Great Financial Crisis, bank supervisors and central banks have greatly increased and intensified their use of stress tests.

The literature on stress testing has also expanded, but it generally focuses on the practice of policymakers in advanced economies and the challenges they face.

Less is known about stress testing in emerging market economies and Latin American countries in particular.

The purpose of this report is to fill this gap.

The report is based on the information gathered by a study group on stress testing formed by the Consultative Group of Directors of Financial Stability (CGDFS) and comprising selected central banks in the Americas.

The study group held several meetings in person and through video conferences, conducted surveys and undertook a common exercise.

The common stress-testing exercise proved particularly informative.

Each participating jurisdiction ran their typical top-down stress tests under an agreed common scenario, making it easier to compare methodologies and approaches.

To the best of our knowledge, this is the first report that systematically compares the stress test methodologies of Latin American central banks.

The report finds that the main type of test run by central banks is a top-down solvency stress test.

Supervisory agencies conduct banking stress tests independently, usually of the bottom-up type.

Coordination between the central bank and the supervisory agency, usually informal, is widespread.

It takes place regularly, with the aim of facilitating the efficient exchange of information and opinions, the comparison of stress test results, and the provision of feedback on methodologies.

Central bank stress tests focus mainly on banks, including all banking system participants.

In some cases, they also include other deposit-taking institutions.

The number of entities covered, as well as the sample composition, varies greatly between jurisdictions.

Credit and market risks are the main risk categories assessed, usually over a horizon of two or three years.

Some jurisdictions also cover other risks or the strength of transmission channels using specific models distinct from the main stress test engine.

Central banks rely on supervisory bank-level data to run their stress tests, sometimes disaggregating loans by sector and using banks' income statements.

Credit risk assessment requires data on loans, charge-offs and loan loss provisions for commercial, consumer and mortgage loans at a system level as well as data on credit portfolios using broad and historic information on defaults at the bank/category levels.

The assessment of market risk usually requires individual bank information, such as detailed portfolio holdings by institution, and financial market data such as interest rate curves and exchange rates.

Assessing the strength of contagion requires detailed information on interbank exposure.

The frequency of the data used in the stress tests usually depends on their availability.

As baseline scenarios, central banks typically use market surveys or projections produced by other central bank departments.

The design of the stressed scenarios involves specifying the magnitude, direction and dynamics of the shocks to the key macroeconomic variables. The methodologies used include multivariate econometric models, replication of historical events or statistical rules applied to some or all variables in the scenario.

In addition, central banks commonly use expert judgment, and in some cases, also the financial and macroeconomic risks identified by private sector.

To read more: https://www.bis.org/publ/bppdf/bispap108.pdf

Objectives of top-down stress testing — Table 1

	Argentina	Brazil[3]	Chile[4]	Colombia	Mexico	Peru	Uruguay
Surveillance (macroprudential)[1]							
Solvency							
Authorities' own assumptions, by individual bank		•		•	•		•
Authorities' own assumptions, by group of banks		•				•	
Authorities' own assumptions, system-wide		•	•			•	•
Liquidity							
Authorities' own assumptions, by individual bank		•	•	•			•
Authorities' own assumptions, by group of banks							
Authorities' own assumptions, system-wide		•					•
Supervisory (microprudential)[2]							
Solvency	•	•				•	•
Liquidity	•	•					•

2019 Annual report

The U.S. economy has continued to perform well since the publication of the previous report of the Council in December 2018.

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Economic growth remains robust, unemployment rates are at a fifty year low, corporate and consumer delinquency and default rates are low, and financial conditions are broadly stable.

Stock prices have increased over the past year. Prices for commercial and residential real estate have also increased albeit at a somewhat slower rate than in previous years.

However, some uncertainty regarding future economic performance has emerged. This uncertainty prompted the Federal Reserve to shift to a more accommodative monetary policy stance over the past year.

Overall, risks to U.S. financial stability remain moderate. Much of the uncertainty in the economic outlook stems from events overseas.

A slowdown in economic growth in the euro area and China may affect economic conditions in the United States though the effects on financial stability, if any, are likely to be modest.

The potential for a disorderly withdrawal of the United Kingdom from the European Union (EU) remains.

Such an event could impact global markets and have a further negative impact on European economic growth.

Domestically, the growth in corporate borrowing remains a key area of focus for the Council.

While firms are able to service their obligations in the current economic environment, high levels of debt and leverage in the corporate sector could exacerbate the effects of a sharp reversal in economic conditions. Maintaining a resilient financial system is important.

The economic well-being of Americans depends on the ability of the financial system to provide capital to businesses and individuals, to provide vehicles for savings, and to intermediate financial transactions even in the face of adverse events.

Post-crisis regulatory reforms have strengthened the ability of the financial system to withstand a shock or an economic downturn.

However, the financial services industry and financial regulators must continue to adapt to changing circumstances.

One change in the near future is the anticipated cessation or degradation of LIBOR as a reference rate for financial contracts.

Widespread failure of market participants to adequately adapt could result in a reduction in liquidity in markets for several types of financial contracts and could potentially adversely impact financial stability.

The Council is closely monitoring developments in this area and remains vigilant regarding other potential emerging threats to financial stability.

The report:
https://home.treasury.gov/system/files/261/FSOC2019AnnualReport.pdf

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FINANCIAL STABILITY OVERSIGHT COUNCIL

EBA consults on revised guidelines on money laundering and terrorist financing risk factors

JOINT COMMITTEE OF THE EUROPEAN SUPERVISORY AUTHORITIES

The EBA has issued a public consultation on revised money laundering and terrorist financing (ML/TF) risk factors Guidelines as part of a broader communication on AML/CFT issues.

This update takes into account changes to the EU Anti Money Laundering and Counter Terrorism Financing (AML/CFT) legal framework and new ML/TF risks, including those identified by the EBA's implementation reviews.

These Guidelines are central to the EBA's work to lead, coordinate and monitor the fight against money laundering and terrorist financing, explained in the accompanying factsheet.

The consultation runs until 5 May 2020.

These Guidelines, which are addressed to both financial institutions and supervisors, set out factors that institutions should consider when assessing the ML/TF risk associated with a business relationship or occasional transaction.

In addition, they provide guidance on how financial institutions can adjust their customer due diligence measures to mitigate the ML/TF risk they have identified.

Finally, they support competent authorities' AML/CFT supervision efforts when assessing the adequacy of firms' risk assessments and AML/CFT policies and procedures.

In its revised version, the EBA is proposing key changes, including new guidance on compliance with the provisions on enhanced customer due diligence related to high-risk third countries.

New sectoral guidelines have been added on crowdfunding platforms, corporate finance, payment initiation services providers (PISPs) and account information service providers (AISPs) and for firms providing activities of currency exchanges offices.

The revised Guidelines also provide more details on terrorist financing risk factors and customer due diligence (CDD) measures including on the identification of the beneficial owner, the use of innovative solutions to identify and verify the customers' identity.

In addition, they set clear regulatory expectations of firms' business-wide and individual ML/TF risk assessments.

The proposed changes will significantly strengthen Europe's AML/CFT defences and foster greater convergence of supervisory practices in areas where supervisory effectiveness has been hampered, so far, by divergent approaches in the implementation of the same European legal requirements.

To read more: https://eba.europa.eu/eba-consults-revised-guidelines-money-laundering-and-terrorist-financing-risk-factors

Running on Empty: A Proposal to Fill the Gap Between Regulation and Decentralization

Commissioner Hester Peirce, Chicago, IL.

Thank you George [Chikovani] for that kind introduction. I appreciate the opportunity to be with all of you today. Before beginning, I have to remind you that the views I express are my own and do not necessarily represent those of the Securities and Exchange Commission or my fellow Commissioners.

Indeed, the views I will express today are not fully formed in my own mind and may not reflect my own opinions in the months to come. To that end, I welcome the feedback of all of you and anyone else with an interest in the regulation of digital assets.

These issues are difficult, and many bright minds on the Commission's staff and outside are trying hard to develop a reasonable framework. As I thought about talking with you today, a story—one that predates my career as a regulator, but nevertheless informs it—bubbled out of my memory.

More than two decades ago, I was on a road trip. I was lost. I did not have a cell phone. It was very late at night. It was pouring. The gas gauge was on empty. There was no gas station in sight. I was distraught until two things happened.

First, I saw the lights of a lone gas station blinking in the not-too-far distance.

Second, I realized that I was in New Jersey! Recalling something a college friend had told me, I would not have wanted to be anywhere else on a stormy night with an empty gas tank.

This friend, who had grown up in New Jersey, had never pumped gas in her life—a deficiency she attributed to a New Jersey law that allowed only gas station employees to pump gas. Everybody else was prohibited from pumping gas.

That law sounded a little silly at the time, but now that I was in New Jersey about to enjoy this mandated luxury on a rain-drenched night, it sounded just wonderful.

Relieved that the fumes in my tank got me to the station, I pulled up to the pump, which, incidentally, was not under a roof substantial enough for even a rain shower, let alone this downpour.

There it was—the unequivocal sign saying that it was illegal for anyone other than a gas station attendant to pump gas. I waited expectantly for the station attendant, roused from a comfortable slumber by my arrival, to emerge from his booth and start the pump.

He looked at me. I looked at him. He pointed at me. He pointed at the pump. His message was clear—forget the law, there would be no full service on that dark and stormy night.

I will not tell you what choice I made, but let's just say that the soundtrack for that drive was Bruce Springsteen's State Trooper: "New Jersey Turnpike ridin' on a wet night 'neath the refinery's glow . . . I got a clear conscience 'bout things I done. Mister state trooper, please don't stop me."

A sensible regulatory framework would have not prevented my pumping the gas rather than being stranded in the rainy dark of night. Perhaps the New Jersey law had a hardship exemption to cover just such situations, but the empty gas tank and sign prohibiting me from filling it seemed irreconcilable at the time.

In any case, the memory of that incident brought with it a basic lesson as I think about regulation of digital assets. It is important to write rules that well-intentioned people can follow.

When we see people struggling to find a way both to comply with the law and accomplish their laudable objectives, we need to ask ourselves whether the law should change to enable them to pursue their efforts in confidence that they are doing so legally.

Entrepreneurs across the crypto landscape are facing just such a scenario in their attempts to develop worthwhile and beneficial products.

Whether it is issuing tokens to be used in a network, launching an exchange-traded product based on bitcoin, providing custody for crypto assets, operating a broker-dealer that handles crypto transactions, or setting up an alternative trading system where people can trade crypto assets, our securities laws stand in the way of innovation.

While I look forward to working with people in the community to develop solutions to each of these problems, today, I am going to focus on how to address the regulatory difficulties faced by people who want to build functioning token networks.

Before detailing my proposal for a safe harbor, I will first outline the problem. Many crypto entrepreneurs are seeking to build decentralized networks in which a token serves as a means of exchange on, or provides access to a function of the network.

In the course of building out the network, they need to get the tokens into the hands of other people. But these efforts can be stymied by concerns that such efforts may fall within the ambit of federal securities laws.

The fear of running afoul of the securities laws is real. Given the SEC's enforcement activity in this area, these fears are not unfounded.

The SEC has scrutinized token sales through the lens of SEC v. Howey, a now infamous case describing what an investment contract is. An investment contract is one type of security under our federal securities laws.

The Howey case dealt with the sale of orange groves, and subsequent cases have involved the sale of a host of other esoteric assets.

In the Howey case, purchasers of units in the orange grove were deemed to be purchasing securities because they were buying the managerial efforts of others along with their piece of the orange grove.

The SEC has tried to apply the Howey analysis to crypto, but doing so is not particularly easy.

For example, some commentators have pointed out that we have elided the distinction between the token and the investment contract.

The "contract, transaction or scheme" by which the token is sold may constitute an investment contract; but, the object of the investment contract—the token—may not bear the hallmarks of a security.

Conflating the two concepts has limited secondary trading and has had disastrous consequences for the ability of token networks to become functional.

Also of concern, suggesting that tokens will increase in value, combined with securing secondary market trading, can trigger a conclusion that those tokens are being sold pursuant to an investment contract.

There are circumstances in which the security label fits, but, in other cases, promises made about tokens increasing in value are nothing more than expressions of the hope that a network will succeed and be used by lots of people.

I would argue that the analysis should focus on the objective nature of the thing offered to the purchasers.

If the token seller is simply discussing the potential for an increase in the value of a token in the same manner that a seller of any number of other consumer products might appeal to purchasers' desire to buy a product of lasting or even increasing value, it there an investment contract? The subjective intent of any particular purchaser should not be controlling.

If it were, then is there any end to the Commission's authority? How would that logic apply to a shoe company, which, as it sells you a pair of sneakers, promises to hire some prominent athletes to promote the brand, thus focusing your mind on how sky high the price will go on StockX rather than on how high your new kicks will enable you to jump on the basketball court?

The SEC's approach in these cases has made it extremely difficult for a company to distribute a token—a process that typically includes planning for a future in which people use the network and talking positively about its prospects for success—without running into a charge that the company is engaged in a securities offering.

We have even hinted that a token airdrop in which tokens are given out freely might constitute an offering of securities. How is a person supposed to get a network up and running when she cannot even give away the tokens necessary to use the network?

One option is to stay far away from the securities laws by simply releasing a white paper, publishing the open source code, mining the genesis block, and then stepping back to allow a network of users blossom organically. Other entrepreneurs, however, might choose to remain actively and publicly involved in building a network for some time.

Some of these people have chosen to proceed with their token offerings as planned in the hopes that they can avoid scrutiny under the securities laws and perhaps convince the SEC that their networks are sufficiently functional to avoid the securities label.

This approach is risky because proving that tokens have utility prior to being distributed to a widespread user base is difficult.
Another option is for the developers to sell the tokens in a registered offering or pursuant to an exemption from registration. To date, no registered offering of tokens has been conducted in the United States.

Many token offerings have proceeded under exemptions from registration, typically Regulation D exemptions that require tokens be sold exclusively to accredited investors with transfer restrictions.

Given the limited pool of persons qualifying as accredited investors based on the current wealth and income tests, it can be difficult for these projects' networks to take off.

Several issuers of tokens have opted for conducting exempt offerings pursuant to Regulation A. However, the costs of conducting one of these so-called "mini-IPOs" can be prohibitive. Even if a team has the financial resources to take this route, once the token is a security, it must trade as a security.

A core benefit of a token network is its non-reliance on intermediaries; people transact directly with one another. Having to buy or sell tokens through a registered broker-dealer or on a registered exchange certainly puts a damper on the development of a thriving, decentralized crypto network.

Particular problems arise because there are unique challenges related to broker-dealers and exchanges handling digital assets.

Other projects have sought to sever any ties with the United States to avoid the reach of our securities laws. This approach is risky because invariably some activity occurs in the United States.

Moreover, this approach is detrimental to the US economy because it prevents American citizens from participating in budding token networks. It is evident that any route chosen by a team to distribute tokens into the hands of potential users is fraught with uncertainty under the securities laws.

We have created a regulatory Catch 22. Would-be networks cannot get their tokens out into people's hands because their tokens are potentially subject to the securities laws.

However, would-be networks cannot mature into a functional or decentralized network that is not dependent upon a single person or group to carry out the essential managerial or entrepreneurial efforts unless the tokens are distributed to and freely transferable among potential users, developers, and participants of the network. The securities laws cannot be ignored, but neither can we as securities regulators ignore the conundrum our laws create.

There is, I think, a way to address the uncertainty of the application of the securities laws to tokens.

The safe harbor I am laying out this morning recognizes the need to achieve the investor protection objectives of the securities laws, as well as

the need to provide the regulatory flexibility that allows innovation to flourish.

Accordingly, the safe harbor protects token purchasers by requiring disclosures tailored to their needs, preserving the application of the antifraud provisions of the securities laws, and giving them an ability to participate in networks of interest to them.

The safe harbor also provides network entrepreneurs sufficient time to build their networks before having to measure themselves against a decentralization or functionality yardstick.

I have spoken openly about my intention to sketch out a safe harbor, and in response, I have gotten some very helpful feedback. But before detailing the specifics of my proposal, I want to emphasize that this remains a work in progress.

I look forward to additional input, and, if I am able eventually to convince my colleagues to add consideration of such an approach to the SEC rulemaking agenda, many other voices, I hope, will weigh in.

For now, the text of the proposed safe harbor is available for viewing as an appendix to this speech at sec.gov and will be posted on social media so that unfiltered critics can apply their editorial hacksaws to it.

You also can give me a call, send me an email, stop by my office, or provide feedback at FinHub. After all, I am very much a believer in the value of drawing on the creativity and ingenuity of as many people as possible.

That is why I find decentralized networks such a powerful phenomenon, and one that will allow society to benefit from the talents of people who—because of societal or geographic barriers—have heretofore been excluded.

I call particular attention to the definitions section of the safe harbor. I am a securities regulator, not a technologist, and am eager to learn how the definitions can be improved.
The challenge is accurately capturing the technology without baking-in terminology that will become outdated in a short period of time.

One struggle I have had in constructing this safe harbor is the appropriate scope. My core concern is for projects that are looking to build a decentralized network, but have difficulty bridging the legal gap.

Additionally, our staff has issued no-action letters to centralized networks.

While sales of tokens intended for these networks seem much less likely to implicate the securities laws, the existence of the no-action letters could be

interpreted to suggest otherwise. Hence, I am suggesting that the safe harbor be available for these types of projects also.

Another unsettled matter is that the safe harbor could take the form of a rule or a Commission-level no-action position. In taking a no-action position, the Commission would pledge not to bring enforcement actions against project developers that fall within the parameters laid out in the position.

A no-action position may be preferable to a rule because it would not concede that the token sales it covers fall within or outside of our securities laws. Such grey areas are an appropriate place for no-action relief.

On the other hand, a rule-based approach would be more durable and would make clear that state laws do not apply. For purposes of this discussion, I will lay out the safe harbor as a rule.

Getting into the specifics of the proposal, the safe harbor would provide network developers with a three-year grace period within which they could facilitate participation in and the development of a functional or decentralized network, exempted from the registration provisions of the federal securities laws, so long as the conditions are met.

This objective is accomplished by exempting

(1) the offer and sale of tokens from the provisions of the Securities Act of 1933, other than the antifraud provisions,

(2) the tokens from registration under the Securities Exchange Act of 1934, and

(3) persons engaged in certain token transactions from the definitions of "exchange," "broker," and "dealer" under the 1934 Act.

The initial development team would have to meet certain conditions, which I will lay out briefly before addressing several in more depth.

First, the team must intend for the network on which the token functions to reach network maturity—defined as either decentralization or token functionality—within three years of the date of the first token sale and undertake good faith and reasonable efforts to achieve that goal.

Second, the team would have to disclose key information on a freely accessible public website.

Third, the token must be offered and sold for the purpose of facilitating access to, participation on, or the development of the network.

Fourth, the team would have to undertake good faith and reasonable efforts to create liquidity for users. Finally, the team would have to file a notice of reliance.

The first requirement—that the initial development team must intend for the network to reach network maturity within three years—is intended to focus project teams' minds.

At the end of three years, token transactions would not be securities transactions if the network has matured into a decentralized or functioning network on which the token is in active use for the exchange of goods or services.

To assess decentralization, the team must consider whether the network is not controlled and is not reasonably likely to be controlled, or unilaterally changed, by any single person, group of persons, or entities under common control.

The mere theoretical possibility of a 51% attack, for example, would not prevent a team from determining that the network is decentralized under this definition.

Nor would the participation of the team in a network alteration achieved through a predetermined procedure in the source code that involves other network participants prevent a team from determining that the network is decentralized.

To assess functionality at the end of three years, the team must consider whether holders can use the tokens in a manner consistent with the utility of the network.

For example, can holders use the tokens for the transmission and storage of value, to prove control over the tokens, or to participate in an application running on the network?

The tests laid out in the safe harbor are meant as proxies for the considerations raised in the SEC's Howey analysis and attempt to bring clarity on when a token transaction should not be considered a securities transaction.

These tests should be easier to pass at the end of three years than when the network is first launched.

Once the network cannot be controlled or unilaterally changed by any single person, entity, or group of persons or entities under common control, the token that operates on that network will not look like a security.

Even for a network that remains centralized—think of the networks outlined in the TurnKey Jet and Pocketful of Quarters no-action letters—once the tokens are actually in use to buy and sell the services for which they were intended, the securities laws will be clearly inapplicable.

Three years is a long time and token purchasers need certain protections during this grace period, which brings me to the second requirement detailing the disclosure that must be provided.

The disclosure requirement of the safe harbor addresses information asymmetry concerns and mandates that certain information be provided on a freely accessible public website.

The team launching a token project knows details about the project that would be useful for potential token buyers to know. Of primary importance is the source code and transaction history.

The safe harbor requires this information to be publicly available and encourages the development of a block explorer, or similar tool, for verifying the transaction history.

Token purchasers also need to understand the purpose and mechanics of the network.

For example, the team would have to explain the launch and supply process, including the number of tokens to be issued in the initial allocation, the total number of tokens to be created, the release schedule for the tokens, and the total number of tokens outstanding.

Public disclosure also would include information about how tokens are generated or mined, the process for burning tokens, the process for validating transactions, and the consensus mechanism.

The team also would have to explain the governance mechanisms for implementing changes to the protocol.

Another key disclosure would be the plan of development, including the current state and timeline for the development of the network that provides a roadmap to how and when the initial development team plans to achieve network maturity.

To demonstrate how realistic these plans are, a team could explain, for example, how the network development will be financed and who is on the development team.

To provide insight on the initial development team, the names and relevant experience, qualifications, attributes, or skills of each person that is a member of the team must be disclosed.

Required disclosure also includes the number of tokens owned by each member of the team, a description of any limitations or restrictions on the transferability of tokens held by such persons, and a description of the team members' rights to receive tokens in the future.

In addition, teams would need to disclose any time that a member sells five percent or more of her originally held tokens over any period of time, which would help to guard against fraud.

Additionally, team token sales could be an indication of flagging commitment to the project.

To further demonstrate their commitment to building a functioning network, teams will be required to update the posted disclosures to reflect any material changes.

Changes affecting the token economics, the network's functionality, or the team developing the network will be of great interest to potential users of the network.

A team committed to building a widely used network likely would provide these updates regardless of whether we mandated it.

The third condition is that the token must be offered and sold for the purpose of facilitating access to, participation on, or the development of the network. This condition, along with the definition of token, is meant to clarify that the safe harbor is not appropriate for debt or equity securities masquerading as tokens.

The safe harbor's fourth condition requires the team to attest that it intends to, and will undertake, good faith and reasonable efforts to create liquidity for users.

To the extent the team attempts to secure secondary trading of the token on a trading platform, the safe harbor requires the team to seek a trading platform that can demonstrate compliance with all applicable federal and state law, as well as regulations relating to money transmission, anti-money laundering, and consumer protection.

Moreover, to alleviate existing regulatory uncertainty on the applicability of securities laws to the secondary trading of tokens, the safe harbor would exempt persons engaged in certain token transactions from the definitions of "exchange," "broker," and "dealer" under the 1934 Act.

Admittedly, the liquidity condition may surprise observers of SEC staff positions in which attempts to facilitate secondary trading have been viewed as indicia of a securities offering.

In the context of the safe harbor, by contrast, secondary trading is recognized as necessary both to get tokens into the hands of people that will use them and offer developers and people who provide services on the network a way to exchange their tokens for fiat or crypto currency.

To the extent it is aware, the team would disclose any secondary trading platforms on which the token trades.

The final condition is the need for the team to file a notice of reliance on EDGAR within fifteen days of the date of the first token sale in reliance on the safe harbor.

As part of the filing, a member of the team would have to attest that all the conditions of the safe harbor are satisfied.

The notice filing would also include the website where the required disclosure may be accessed. None of the disclosures required by the safe harbor would be provided in the notice filing on EDGAR.

Having outlined the conditions of the safe harbor, I would like to emphasize a few points concerning its scope. SEC enforcement has played an important role in combatting fraud in connection with token sales. The safe harbor would not provide immunity from such actions.

First, the safe harbor would not be available to a team if one or more members of the team is subject to disqualification as a bad actor under the securities laws.

Second, the safe harbor would reserve the SEC's antifraud authority with respect to token sales under the safe harbor.

Although the safe harbor would preempt state securities laws, it would not stand in the way of state antifraud actions.

If anyone lied in connection with selling tokens pursuant to the safe harbor, the SEC or a state could bring an enforcement action.

This provision is not directed at teams that set forth a plan for a network and work earnestly toward building it, but fail to bring it to fruition.

Rather, it is designed to ensure that the SEC can bring suit against a team that sets out to defraud token purchasers by materially misrepresenting or

omitting key information. We all know that there are plenty of those kinds of "projects" polluting the crypto space.

It is also important to note that the safe harbor would be available for tokens that were previously sold in a registered offering or pursuant to a valid exemption under the Securities Act.

These teams may need the safe harbor in order to permit secondary trading to occur and to distribute their tokens more widely into the hands of potential users.

Tokens that already are in widespread use on a decentralized network presumably are not securities and, therefore, would not need to take advantage of the safe harbor.

It is during the development phase that questions about the securities/non-securities line seem to be most difficult to resolve. Once a token network is up and running, few people would advocate application of the securities laws.

By essentially buying time for this question to be answered, the safe harbor makes it much more likely that the question as to whether something is a security can be answered in the negative.

Now that I have outlined the safe harbor, I suspect some of you are asking, "Who cares?" I get the point. I am one of five Commissioners. I cannot write rules unilaterally. However, to quote another of the Boss's songs: "you can't start a fire without a spark."

It does not hurt to get the ball rolling. People change their minds. Moreover, if we are going to do something like what I suggest today, I want to get it right.

Getting it right means that I need people like those of you in the audience or reading this speech to weigh in and tell me what I have gotten right and what I have gotten wrong. Don't be that guy in New Jersey telling me I have to do this all by myself.

Executive Order on Strengthening National Resilience through Responsible Use of Positioning, Navigation, and Timing Services

By the authority vested in me as President by the Constitution and the laws of the United States of America, it is hereby ordered as follows:

Section 1. Purpose. The national and economic security of the United States depends on the reliable and efficient functioning of critical infrastructure.

Since the United States made the Global Positioning System available worldwide, positioning, navigation, and timing (PNT) services provided by space-based systems have become a largely invisible utility for technology and infrastructure, including the electrical power grid, communications infrastructure and mobile devices, all modes of transportation, precision agriculture, weather forecasting, and emergency response.

Because of the widespread adoption of PNT services, the disruption or manipulation of these services has the potential to adversely affect the national and economic security of the United States. To strengthen national resilience, the Federal Government must foster the responsible use of PNT services by critical infrastructure owners and operators.

Sec. 2. Definitions. As used in this order:

(a) "PNT services" means any system, network, or capability that provides a reference to calculate or augment the calculation of longitude, latitude, altitude, or transmission of time or frequency data, or any combination thereof.

(b) "Responsible use of PNT services" means the deliberate, risk-informed use of PNT services, including their acquisition, integration, and deployment, such that disruption or manipulation of PNT services minimally affects national security, the economy, public health, and the critical functions of the Federal Government.

(c) "Critical infrastructure" means systems and assets, whether physical or virtual, so vital to the United States that the incapacity or destruction of such systems and assets would have a debilitating impact on national security, national economic security, national public health or safety, or on any combination of those matters.

(d) "PNT profile" means a description of the responsible use of PNT services — aligned to standards, guidelines, and sector-specific requirements — selected for a particular system to address the potential disruption or manipulation of PNT services.

(e) "Sector-Specific Agency" (SSA) is the executive department or agency that is responsible for providing institutional knowledge and specialized expertise as well as leading, facilitating, or supporting the security and resilience programs and associated activities of its designated critical infrastructure sector in the all-hazards environment.

The SSAs are those identified in Presidential Policy Directive 21 of February 12, 2013 (Critical Infrastructure Security and Resilience).

Sec. 3. Policy. It is the policy of the United States to ensure that disruption or manipulation of PNT services does not undermine the reliable and efficient functioning of its critical infrastructure.

The Federal Government must increase the Nation's awareness of the extent to which critical infrastructure depends on, or is enhanced by, PNT services, and it must ensure critical infrastructure can withstand disruption or manipulation of PNT services.

To this end, the Federal Government shall engage the public and private sectors to identify and promote the responsible use of PNT services.

Sec. 4. Implementation. (a) Within 1 year of the date of this order, the Secretary of Commerce, in coordination with the heads of SSAs and in consultation, as appropriate, with the private sector, shall develop and make available, to at least the appropriate agencies and private sector users, PNT profiles.

The PNT profiles will enable the public and private sectors to identify systems, networks, and assets dependent on PNT services; identify appropriate PNT services; detect the disruption and manipulation of PNT services; and manage the associated risks to the systems, networks, and assets dependent on PNT services. Once made available, the PNT profiles shall be reviewed every 2 years and, as necessary, updated.

(b) The Secretary of Defense, Secretary of Transportation, and Secretary of Homeland Security shall refer to the PNT profiles created pursuant to subsection (a) of this section in updates to the Federal Radionavigation Plan.

(c) Within 1 year of the date of this order, the Secretary of Homeland Security, in coordination with the heads of SSAs, shall develop a plan to

test the vulnerabilities of critical infrastructure systems, networks, and assets in the event of disruption and manipulation of PNT services.

The results of the tests carried out under that plan shall be used to inform updates to the PNT profiles identified in subsection (a) of this section.

(d) Within 90 days of the PNT profiles being made available, the heads of SSAs and the heads of other executive departments and agencies (agencies), as appropriate, through the Secretary of Homeland Security, shall develop contractual language for inclusion of the relevant information from the PNT profiles in the requirements for Federal contracts for products, systems, and services that integrate or utilize PNT services, with the goal of encouraging the private sector to use additional PNT services and develop new robust and secure PNT services. The heads of SSAs and the heads of other agencies, as appropriate, shall update the requirements as necessary.

(e) Within 180 days of the completion of any of the duties described in subsection (d) of this section, and consistent with applicable law and to the maximum extent practicable, the Federal Acquisition Regulatory Council, in consultation with the heads of SSAs and the heads of other agencies, as appropriate, shall incorporate the requirements developed under subsection (d) of this section into Federal contracts for products, systems, and services that integrate or use PNT services.

(f) Within 1 year of the PNT profiles being made available, and biennially thereafter, the heads of SSAs and the heads of other agencies, as appropriate, through the Secretary of Homeland Security, shall submit a report to the Assistant to the President for National Security Affairs and the Director of the Office of Science and Technology Policy (OSTP) on the extent to which the PNT profiles have been adopted in their respective agencies' acquisitions and, to the extent possible, the extent to which PNT profiles have been adopted by owners and operators of critical infrastructure.

(g) Within 180 days of the date of this order, the Secretary of Transportation, Secretary of Energy, and Secretary of Homeland Security shall each develop plans to engage with critical infrastructure owners or operators to evaluate the responsible use of PNT services. Each pilot program shall be completed within 1 year of developing the plan, and the results shall be used to inform the development of the relevant PNT profile and research and development (R&D) opportunities.

(h) Within 1 year of the date of this order, the Director of OSTP shall coordinate the development of a national plan, which shall be informed by existing initiatives, for the R&D and pilot testing of additional, robust, and

secure PNT services that are not dependent on global navigation satellite systems (GNSS).

The plan shall also include approaches to integrate and use multiple PNT services to enhance the resilience of critical infrastructure. Once the plan is published, the Director of OSTP shall coordinate updates to the plan every 4 years, or as appropriate.

(i) Within 180 days of the date of this order, the Secretary of Commerce shall make available a GNSS-independent source of Coordinated Universal Time, to support the needs of critical infrastructure owners and operators, for the public and private sectors to access.

Sec. 5. General Provisions. (a) Nothing in this order shall be construed to impair or otherwise affect:

(i) the authority granted by law to an executive department or agency, or the head thereof; or

(ii) the functions of the Director of the Office of Management and Budget relating to budgetary, administrative, or legislative proposals.

(b) This order shall be implemented consistent with applicable law and subject to the availability of appropriations.

(c) This order is not intended to, and does not, create any right or benefit, substantive or procedural, enforceable at law or in equity by any party against the United States, its departments, agencies, or entities, its officers, employees, or agents, or any other person.

DONALD J. TRUMP
THE WHITE HOUSE,
February 12, 2020.

The green swan

Central banking and financial stability in the age of climate change (115 pages). Patrick BOLTON - Morgan DESPRES - Luiz Awazu PEREIRA DA SILVA Frédéric SAMAMA - Romain SVARTZMAN, January 2020

Climate change poses new challenges to central banks, regulators and supervisors. This book reviews ways of addressing these new risks within central banks' financial stability mandate.

However, integrating climate-related risk analysis into financial stability monitoring is particularly challenging because of the radical uncertainty associated with a physical, social and economic phenomenon that is constantly changing and involves complex dynamics and chain reactions.

Traditional backward-looking risk assessments and existing climate - economic models cannot anticipate accurately enough the form that climate-related risks will take.

These include what we call "green swan" risks: potentially extremely financially disruptive events that could be behind the next systemic financial crisis.

Central banks have a role to play in avoiding such an outcome, including by seeking to improve their understanding of climate-related risks through the development of forward-looking scenario-based analysis.

But central banks alone cannot mitigate climate change. This complex collective action problem requires coordinating actions among many players including governments, the private sector, civil society and the international community.

Central banks can therefore have an additional role to play in helping coordinate the measures to fight climate change. Those include climate mitigation policies such as carbon pricing, the integration of sustainability into financial practices and accounting frameworks, the search for appropriate policy mixes, and the development of new financial mechanisms at the international level.

All these actions will be complex to coordinate and could have significant redistributive consequences that should be adequately handled, yet they are essential to preserve long-term financial (and price) stability in the age of climate change.

To read more you may visit: https://www.bis.org/publ/othp31.pdf

EBA consults on the future of the EU-wide stress test framework

The European Banking Authority (EBA) launched today a public consultation on possible future changes to the EU-wide stress test.

This discussion paper aims to present the EBA's vision of the future of the EU-wide stress test and to collect comments and feedback from the different users.

The proposal envisages two components owned by supervisors and banks respectively: the supervisory leg and the bank leg.

The consultation runs until 30 April 2020.

> *"The framework we are proposing today aims at making the EU-wide stress test more informative, flexible, and cost-effective. It is the first time we embark on a comprehensive discussion on the future of EU stress testing and we are keen to receive feedback from a wide range of stakeholders."*
>
> **José Manuel Campa, EBA Chairperson**

Key features of the new framework

Since 2011, the EU-wide stress test has contributed to improving banks' resilience after the financial crisis, has enhanced transparency and has been instrumental in restoring trust in the EU banking sector.

The proposed new framework tries to balance the need to preserve comparability and conservatism, while allowing for more flexibility in order to identify banks' idiosyncratic risks.

The proposal envisages two components owned by supervisors and banks respectively: the supervisory leg and the bank leg.

The supervisory leg serves as the starting point for supervisory decisions and would be directly linked to the setting of Pillar 2 Guidance (P2G).

The bank leg, on the other hand, allows banks to communicate their own assessment of risks in an adverse scenario.

To ensure a certain level of comparability, both legs would use the same common scenarios and starting points for projecting the stress test results.

The supervisory leg would be based on a common EU methodology, in line with the current constrained bottom-up approach but with the possibility for competent authorities to adjust or replace banks' estimates based on top-down models or other benchmarking tools.

The methodology for the bank leg would be less prescriptive than today and give banks more discretion in calculating their projections.

In practice, banks would use the same common methodology as in the supervisory leg, but would be allowed to relax the methodological constraints to the extent they can explain and disclose the rationale and impact of such deviations.

The standards for the disclosure of the results should remain high.

For the bank leg, the proposed disclosure is as granular as it is today, including the overall outcome in terms of capital depletion, main risk drivers, and detailed data on exposures.

For the supervisory leg, granularity would be more limited in quantity, but very relevant in terms of supervisory decisions.

In particular, the discussion paper seeks views on three possibilities:

(i) disclosing P2G,

(ii) disclosing ranges of P2G or

(iii) disclosing not P2G but the CET1 capital depletion net of any supervisory adjustments so that the results are informative in terms of supervisory expectations regarding capital distribution.

As for the scenario design, the discussion paper is considering costs and benefits of multiple macroeconomic scenarios.

In addition, feedback is requested on the feasibility of introducing exploratory scenarios, which would focus on potential risks with very short realisations (e.g. liquidity risk) or coming from longer-term changes in the business environment (environmental, social and political) or in technology.

Consultation process

Comments to this consultation can be sent to the EBA by clicking on the "send your comments" button on the consultation page. Please note that the deadline for the submission of comments is 30 April 2020.

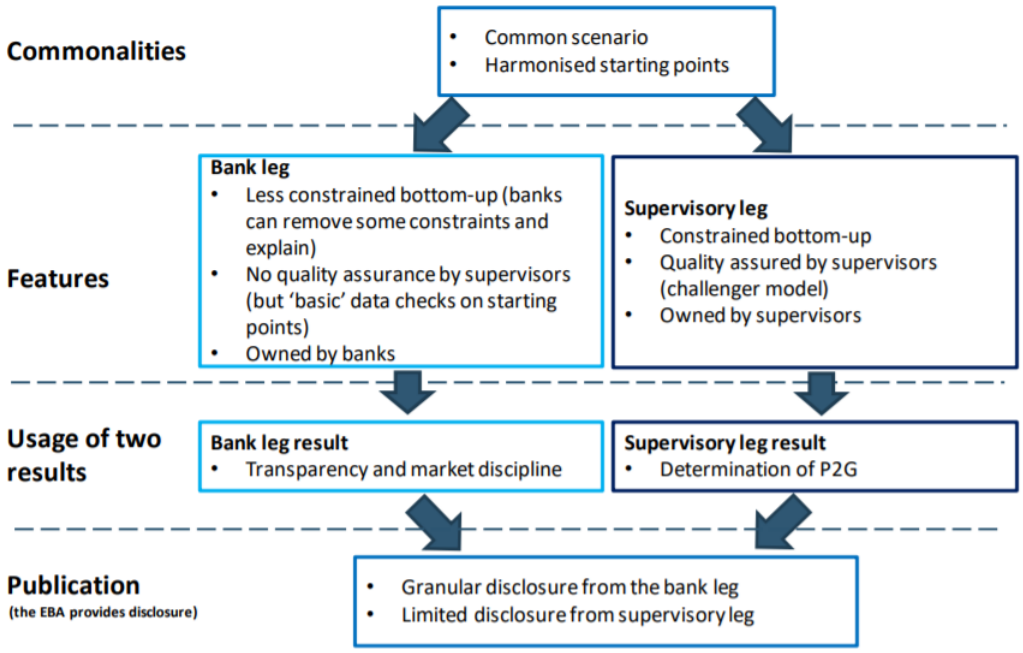
A public hearing will take place at the EBA premises on 21 February 2020 from 10:30 to 12:30 CET. All contributions received will be published following the end of the consultation, unless requested otherwise.

Note

The 2020 EU-wide stress test will be conducted according to the current framework and its results will be published in July 2020.

To read more: https://eba.europa.eu/calendar/discussion-paper-future-changes-eu-wide-stress-test

Figure 1: Proposed framework for a EU-wide stress test with a two-legged approach



The presentations, from the 26th IAIS Annual Conference, Supervision in a Digital Era, Abu Dhabi, UAE

International Association of Insurance Supervisors (IAIS)

26th IAIS Annual Conference
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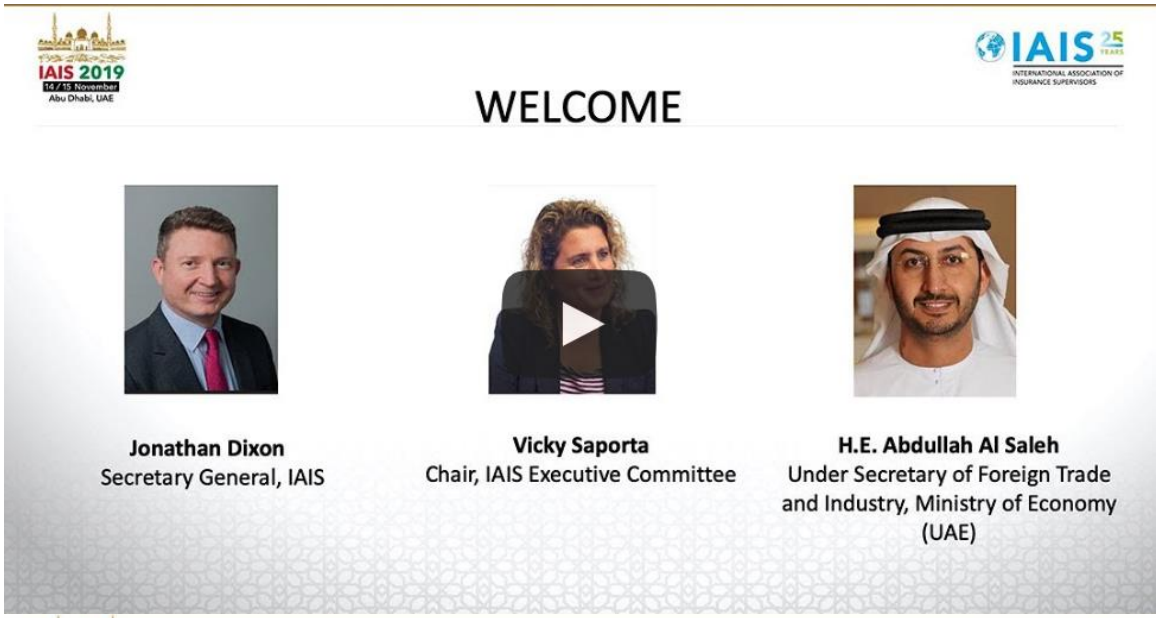

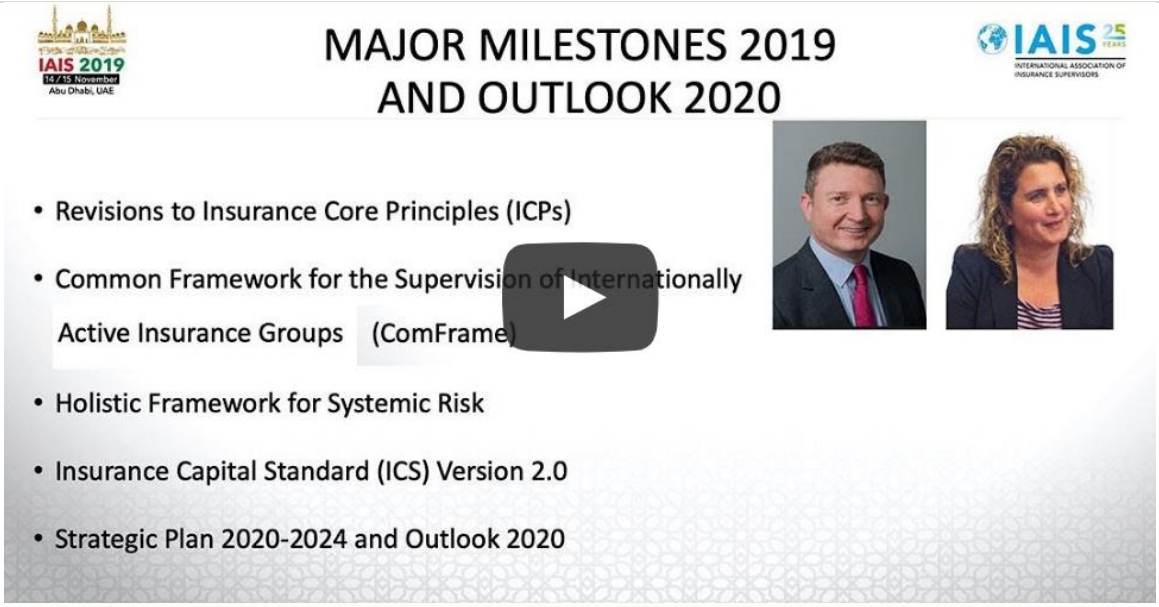
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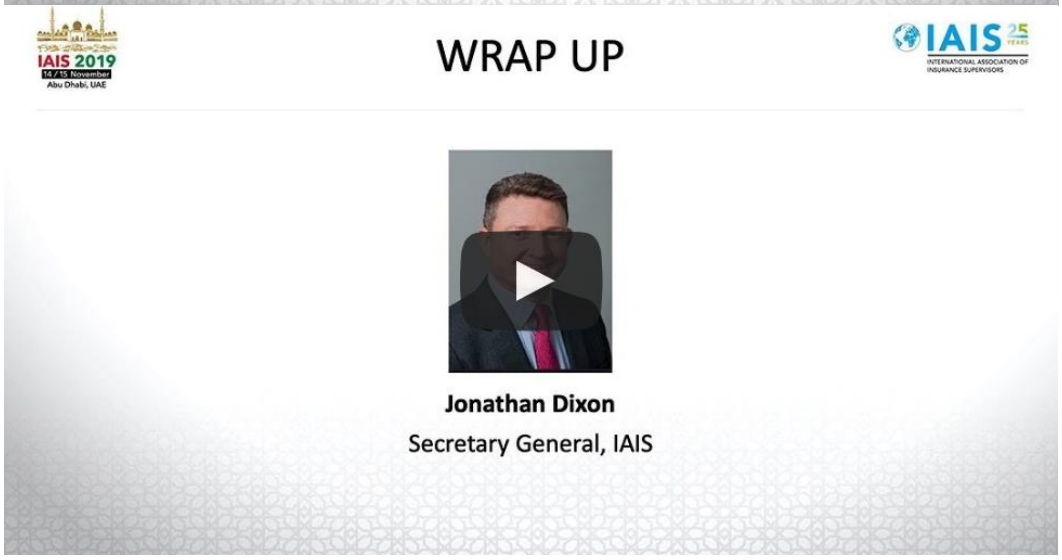

The videos: https://www.iaisweb.org/page/events/annual-conference/annual-conference-2019/annual-conference-videos

Spontaneity and Order: Transparency, Accountability, and Fairness in Bank Supervision

Vice Chair for Supervision Randal K. Quarles, at the American Bar Association Banking Law Committee Meeting 2020, Washington, D.C.

It's a great pleasure to be with you today at the ABA Banking Law Committee's annual meeting.

I left the practice of law—and immersion in the company of lawyers—closing in on 20 years ago now, but there have been many times during my long sojourn among businessmen and economists that I have reflected with fondness and some nostalgia on the famous adage of Harrison Tweed (the "Tweed" of Milbank, Tweed, a reformer of the bar, the "most democratic of aristocrats," and the last man to unironically wear a cape in the lobby of the Chase Manhattan Plaza) which most of you can no doubt recite by heart: "I have a high opinion of lawyers.

With all their faults, they stack up well against those in every other occupation or profession. They are better to work with or play with or fight with or drink with than most other varieties of mankind." Speaking here feels a lot like coming home.

This afternoon, I would like to talk with you about the outwardly mundane but increasingly consequential topic of bank supervision.

Twenty years ago, when I would have been among your number at this meeting, this would have been my cue to pull out my Blackberry and start checking my emails.

The structure and content of regulation was both intellectually interesting and professionally meaningful; I considered bank supervision, by contrast, as both too workaday and too straightforward to merit the commitment of much legal horsepower or personal attention.

I could perhaps have been excused by the callowness of youth, yet it was a common view at the time.
Having now been immersed for the last two years both in the practice of supervision and in the complementary relationship between the regulatory

and supervisory processes, I realize that this wasn't true then, and is certainly not true now.

It is not a drafting accident that the Dodd-Frank Act gave my position at the Federal Reserve the title of Vice Chairman for Supervision.

Notwithstanding the extensive reform of bank regulation after the crisis, which has had much consequence for the industry (most of it salutary) it is the process of examination and supervision that constitutes the bulk of our ongoing engagement with the industry and through which our policy objectives are given effect.

This division of labor is important for lawyers and policymakers to think about deeply because the processes of regulation and supervision are necessarily different in crucial respects.

Regulation establishes a binding public framework implementing relevant statutory imperatives. Because a rule is designed to apply generally, rules must be based on general principles intended to achieve general aims, rather than reverse-engineered to generate specific effects for specific institutions.

Given their general applicability, there must be a general process for all those with an interest—industry, academics, citizens, Congress—to have notice of, and opportunity to comment on all rules, ensuring that all potential effects and points of view are taken into account in the rule's crafting. And given their general function, rules must be clear and public: Those affected must know what to expect and what is expected.

Supervision, by contrast, implements the regulatory framework through close engagement with the particular facts about particular firms: their individual capital and liquidity positions, the diverse composition of their distinct portfolios of assets, their business strategies, the nature of their operations, the strengths and weaknesses of their management.

Much of the granular information used by supervisors is, accordingly, proprietary and confidential, and many of their judgments and decisions are closely tailored to specific circumstances.

Given the strong public interest in the safe, sound, and efficient operation of the financial industry and the potential for hair-raising and widespread adverse social consequences of private misjudgment or misconduct in that industry, close and regular supervision of this sort can help us all sleep restfully. Yet, the confidential and tailored nature of supervision sits uncomfortably with the responsibilities of government in a democracy. In the United States, we have a long-standing, well-articulated framework for

ensuring that regulations conform with the principles of generality, predictability, publicity, and consultation described above.

Supervision—for good reason, in my view—is not subject to this formal framework. But it is currently not subject to any specific process constraint promoting publicity or universality. This leaves it open to the charge, and sometimes to the fact, of capriciousness, unaccountability, unequal application, and excessive burden.

Here, then, is a conundrum. We have a public interest in a confidential, tailored, rapid-acting and closely informed system of bank supervision. And we have a public interest in all governmental processes being fair, predictable, efficient, and accountable.

How do we square this circle? In my time with you today, we will not do more than scratch the surface of this question. It is a complex and consequential issue that, for decades now, has received far too little attention from practitioners, academics, policymakers and the public.

Evaluating this question will be a significant focus of mine going forward, and I hope that there will be much discussion in many fora from which we at the Fed, and at other regulators, can learn. So today, I simply want to open the exploration of some these conceptual issues, and then offer some specific suggestions—by no means comprehensive—on some obvious and immediate ways that supervision can become more transparent, efficient, and effective.

The Importance of Transparency

Let me begin by delving a little more deeply into the distinction between regulation and supervision and the process applicable to both. In delegating to agencies such as the Fed the significant power to write regulations, Congress has codified a regulatory process that emphasizes transparency.

This process was born in the 1930s, in the tumult of government expansion that was the New Deal, when Congress began a decade-long debate over how to manage the new regulatory state.

The result, the Administrative Procedure Act (APA), was, I should note, developed with the active involvement of the American Bar Association. The APA continues to serve as the basis for the public disclosure and participation required for agency rule-writing and for the judicial review affected parties are guaranteed to challenge rules.

This transparency is intended to prevent arbitrary, capricious, and thus ineffective regulation by inviting broad public participation and mandating a deliberate public debate over the content of proposed rules. One obvious purpose of this transparency is to provide clarity and predictability: it helps make clear how agencies are considering exercising their discretion.

The significant process protections in laws such as the APA are also meant to ensure fairness. The wisdom behind this approach is that fairness both helps bring forth more considered and effective regulations and builds respect for and adherence to the law, which is essential for enforcement. Transparency is central to our ability to assert that our rules are fair.

Not everything that government does, however, can be accomplished in exactly the same way that regulations are written. One of these things is bank supervision.

Bank Supervision

Banks are subjected to supervision, in addition to regulation, as an additional form of government oversight because of their complexity, opacity, vulnerability to runs, and indispensable role in the economy, enabling payments, transmitting monetary policy, and providing credit.

The government provides a safety net to banks in the form of deposit insurance, and in return, banks are subject to government oversight that mimics some of the monitoring that the private sector would provide, absent the government safety net.

The bank regulatory framework sets the core architectural requirements for the banking system, but it isn't enough to set the rules and walk away like Voltaire's god.

The potential consequences of disruption in the financial system are so far-reaching, and the erosion of market discipline resulting from the government safety net sufficiently material, that it is neither safe nor reasonable to rely entirely on after-the-fact enforcement to ensure regulatory compliance.

Supervisors are in a good position to monitor individual firms' idiosyncratic risks. And in addition to what they do at individual banks, supervisors monitor for risk that may be building among clusters of banks or across the banking system.

These "horizontal" exams across multiple banks help highlight new or emerging risks and help examiners understand how banks are managing these risks.

Through their engagement with banks, supervisors promote good risk management and thus help banks preemptively avert excessive risk taking that would be costly and inefficient to correct after the fact.

Where banks fall materially out of compliance with a regulatory framework or act in a manner that poses a threat to their safety and soundness, supervisors can act rapidly to address the failures that led to the lack of compliance or threat to safety and soundness.

This is a crucial point: Supervision is most effective when expectations are clear and supervision promotes an approach to risk management that deters bad behavior and decisions by banks.

Clearly communicating those expectations is essential to effective supervision, and in a larger sense, clear two-way communication is the essence of effective supervision.

Supervisors rely on banks to be frank and forthcoming, and supervisors in turn can help secure that frankness by explaining what their expectations are and why their expectations are reasonable, not arbitrary or capricious.

Greater transparency in supervision about the content of our expectations and about how we form our expectations and judgments can make supervision more effective by building trust and respect for the fairness and rationality of supervision.

I don't believe the Federal Reserve has communicated as clearly as it could with the banks we supervise. More transparency and more clarity about what we want to achieve as supervisors and how we approach our work will improve supervision, and I have several specific proposals.

Broadly speaking, these actions fall into three categories:

(1) large bank supervision,
(2) transparency improvements, and
(3) overall supervisory process improvements.

Large Bank Supervision

Last fall, we completed a cornerstone of the recent banking legislation to tailor our rules for regional banks. This was entirely consistent with a principle at the heart of our existing work: Firms that pose greater risks should meet higher standards and receive more scrutiny. Our previous rules relied heavily on a firm's total assets as a proxy for these risks and for the costs the financial system would incur if a firm failed.

This simple asset proxy was clear and critical, rough and ready, but neither risk sensitive nor complete. Our new rules employ a broader set of indicators, like short-term wholesale funding and off-balance-sheet exposures, to assess the need for greater supervisory scrutiny.

That said, the composition of our supervisory portfolios has not yet been aligned with our recent tailoring rules. For example, the Large Institution Supervision Coordinating Committee (LISCC) portfolio includes all Category I firms, which have the greatest risk profile, along with certain Category II and Category III firms, which are less systemic.

Other Category II and Category III firms, on the other hand, are supervised under our large and foreign banking organizations (LFBO) portfolio.

Since the crisis, we have been giving significant thought to the composition of our supervisory portfolios, and, in particular to whether and how we should address the significant decrease in size and risk profile of the foreign firms in the LISCC portfolio over the past decade.

Because of these changes, which I will describe in more detail momentarily, I believe there is a compelling justification to make changes today to the composition of the foreign banks in the LISCC portfolio.

Separately and in keeping with the goal of transparency, I think it is important that all the Fed's supervisory portfolios have a clear and transparent definition.

Today nearly all of our supervisory portfolios have such a crisp and clear formulaic definition specified in the public domain, but the LISCC portfolio does not.

My goal is to develop, prospectively, a clear and transparent standard for identifying LISCC firms. My preferred approach for achieving this objective would be to align the LISCC portfolio with our recent tailoring categorizations.

I believe we should draw the LISCC line to coincide with Category I. The justification for this line-drawing is that Category I firms pose the most systemic risk and require the most supervisory attention.

In this state of the world, Category II and III firms would remain subject to heightened supervisory standards that are commensurate with their risk profile.

Allow me to draw out what this approach could mean for the foreign banks that currently are in the LISCC portfolio.

Since 2010, these four banks have significantly shrunk their U.S. footprint, and their U.S. operations are much less risky than they used to be.

Since 2008, the size of the LISCC FBOs' combined U.S. assets has shrunk by about 50 percent, and they have reduced the assets at their broker-dealers from a peak of $1.9 trillion in 2008 to $340 billion today, a reduction of over 80%.

In addition, the estimated systemic impact of the LISCC FBOs today is much smaller than the U.S. GSIBs. The average method 1 GSIB score of the combined U.S. operations of the LISCC FBOs is less than a quarter of the average GSIB score of the six non-processing U.S. GSIBs.

Thus, if any foreign banks move out of the LISCC portfolio based on this de-risking, they would move into the LFBO portfolio, where they would be supervised alongside other foreign and domestic firms with similar risk profiles.

Notably, this change in supervisory portfolio would have no effect on the regulatory capital or liquidity requirements that currently apply to the four LISCC FBOs. Similarly, the change would not result in a loss of insight into the activities of these firms.

In the same spirit, I think we should consider publishing the internal procedural materials that the Fed uses to supervise the LISCC firms, sometimes referred to as the Program Manual.

The Manual contains a description of the main supervisory processes for identifying risks and our approach for addressing them. Publishing the Manual would help the public and the banks better understand why we take the actions that we take as supervisors and would demystify some of our processes.

If we took these two simple steps—defining LISCC firms and publishing the Program Manual that governs our supervisory approach—it would go a long way in helping to make our supervisory practices more understandable and accessible without undermining supervisory effectiveness.

Let me now turn to the ratings framework that applies to all large holding companies. A firm's supervisory rating, which is confidential, is important because it affects things such as the firm's ability to engage in mergers and acquisitions and to enter new lines of business.

Just over a year ago, the Board began implementing a new ratings framework for large holding companies called the large financial institutions (LFI) ratings framework.

The LFI ratings framework focuses on three components of a firm's operations: capital, liquidity, and governance and controls. We inaugurated the LFI ratings framework for LISCC firms in January 2019 and for other large holding companies at the beginning of this year.

As we gain more experience with LFI, we will be paying close attention to how the new rating system is working and whether it is achieving its intended purpose. There are two features of the ratings system that I will be particularly interested to monitor, and which may well require adjustment.

These are the embedding of qualitative "risk management" standards in the capital and liquidity components of the ratings (as opposed to standardized quantitative measures of capital and liquidity adequacy) and the ascetic principle by which a firm's "well managed" status is determined by its lowest component rating, no matter how good the bank is at everything else.

Regarding our stress tests under the Comprehensive Capital Analysis and Review (CCAR), I continue to look for ways to make the tests more transparent without making them game-able and without diluting their potency as a supervisory tool. I will mention three of these transparency-enhancing ideas.

First, I expect that we will continue to provide more transparency on the models used in CCAR. We started providing improved transparency on models last year, and as I have previously said, we will remain on that path until we have released substantial details on all of our key models.

We also continue to consider ways to increase the transparency around the scenarios we use in CCAR, including, for example, by modifying our scenario design policy statement to provide greater transparency on the design of the global market shock component of the stress tests.

Second, I expect that as part of the stress capital buffer, we will give banks significantly more time to review their stress test results and understand their capital requirements before we demand their final capital plan. Firms are currently permitted to revise and resubmit their capital plans after receiving their stress test results. But it is done on a short timeframe, and allowing additional time would produce better results without in any way reducing the stringency of the stress tests.

Fundamentally, I think banks will be better able to do intelligent capital planning if we provide them with their complete set of regulatory capital requirements before we require submission of a capital plan.

Third and finally, we continue to look for ways to reduce the volatility of stress-test requirements from year to year. We are considering a number of options, such as averaging outcomes over multiple years or averaging the results of the current year's stress test with the results of one or more previous years.

Again, the goal here is not to make the tests less strenuous but to give banks a greater opportunity to plan for them and to meet our expectations ex ante rather than through an ex post remedial process.

Transparency Improvements

The next three actions I'm proposing also relate to improved transparency, and they would improve our processes for supervising all banks. The first would be to create a word-searchable database on the Board's website with the historical interpretations by the Board and its staff of all significant rules.

Regulatory interpretations by Board staff have grown piecemeal over the decades and haven't consistently been treated as the valuable resource they are. The Board's website has select interpretations of many laws but does not provide a comprehensive, user-friendly collection of regulatory interpretations, FAQs, and commentary.

This project will require some effort of course, as well as vigilance to keep the interpretations up to date, but I believe that the end result will be well worth it.

The second of these transparency actions would be putting significant supervisory guidance out for public comment. The Board already invites comments on its regulations, as required under the APA, and regularly invites comment on some supervisory guidance and statements of policy.

This practice of seeking comment on guidance leads to better, more informed supervision and better engagement by banks. I would like the Board to seek comment on more supervisory guidance going forward. Third and finally, as another improvement related to guidance, I support submitting significant supervisory guidance to Congress for purposes of the Congressional Review Act.

Currently, the Fed does this for rules but not guidance. I support doing so for significant guidance because significant guidance, though nonbinding, can still have a material impact on bank behavior. I believe this step would enhance the Fed's accountability and help build support for supervisory guidance.

Overall Supervisory Process Improvements

The last category of proposals includes five areas of improvement that all relate to what we call the "supervisory process"—how we go about conducting our responsibilities. Like my other suggestions, these are all rooted in common sense with a view toward maintaining firm and fair supervision.

The first is to increase the ability of supervised firms to share Federal Reserve confidential supervisory information (CSI) with employees, affiliates, service providers, and other government agencies to promote greater compliance with laws and facilitate the response to enforcement actions.

We have received feedback that our rules can prevent banks from sharing CSI with a wide variety of relevant parties who need to know this information in order to help the bank remediate identified supervisory issues. We issued a proposal last year to address this shortcoming in our CSI rules, and I expect the Board will be able to issue a final CSI rule later this year.

The second process improvement is having the Board adopt a rule on how we use guidance in the supervisory process. I would expect the rule to state that the Board will follow and respect the limits of administrative law in carrying out its supervisory responsibilities.

In particular, consistent with the September 2018 interagency statement on guidance, we would affirm the sensible principles that guidance is not binding and "non-compliance" with guidance may not form the basis for an enforcement action (such as a cease-and-desist order) or supervisory criticism (such as a Matter Requiring Attention (MRA)).

This rule would be binding on the Board and on all staff of the Federal Reserve System, including bank examiners.

The third and fourth process improvements relate to supervisory communication. The third improvement is to restore the "supervisory observation" category for lesser safety and soundness issues.

This approach would provide supervisors with a tool—supervisory recommendations—for continuing to raise concerns about less pressing supervisory matters while focusing a bank's attention on the most urgent matters, those that would receive MRAs.

We removed this category of supervisory commentary in 2013 to better focus bank management on deficiencies found during the supervision

process. (By way of comparison, both the FDIC and OCC retained this tool.) On reflection, I think there is value in supervisory observations. They allow an examiner to give notice about a supervisory concern even if that concern has not risen to the level of an MRA.

The fourth process improvement would be limiting future MRAs to violations of law, violations of regulation, and material safety and soundness issues. MRAs are supervisory communications that identify areas where banks are out of compliance with applicable legal standards or otherwise are engaged in practices that create substantial safety and soundness risks.

MRAs identify the source of the compliance failure, deficiency, or safety and soundness weakness and generally include an expected timeframe for remediation. MRAs are not legally binding and are not enforcement actions.

Nevertheless, MRAs carry weight because they can affect a bank's supervisory rating. In limiting MRAs to legal violations and significant supervisory concerns, we would take care to clearly define the breadth of what constitutes a "material safety and soundness issue." This distinction is important as a matter of fairness.

Banks should be able to understand the line between MRAs significant enough to affect the bank's supervisory rating and less significant matters that don't affect a bank's supervisory rating but raise concerns that should be considered by banks.

Greater fairness contributes to greater supervisory effectiveness. Together, the third and fourth process improvements would be calibrated to improve communications so that banks can focus on remediating key weaknesses while maintaining awareness of emerging ones. Ultimately, a bank that promptly corrects its material safety and soundness weaknesses will be better able to serve its customers and intermediate credit through a range of scenarios, including under stress.

The final process improvement is to make routine our existing practice of having an independent review of important supervisory communications and guidance documents. We want to make sure that our supervisory communications, including MRAs, focus on violations of law and material safety and soundness issues and that these communications don't mistakenly give the impression that supervisory guidance is binding.

We already closely scrutinize MRAs issued to the LISCC firms and in horizontal reviews of other large domestic and foreign banks. This extra scrutiny is a sensible practice that should be regularized and expanded across our supervisory portfolios.

With respect to prospectively assessing future guidance, the key goals here would include reassessing the scope of key guidance documents, removing inappropriate bright lines from guidance, and removing any mandatory language from guidance. I will discuss each of these goals in turn.

As I mentioned, the Board adopted a final tailoring rule last year that adjusted the regulatory standards applicable to banks, based on their risk profile. I think it would be useful for us to review our guidance in light of this tailoring exercise, such as guidance on stress testing and capital planning, and to update the scope of guidance where appropriate.

Regarding bright lines, bright lines tend to carry the implication that the standard they are delineating is binding. For this reason, rules often include bright lines so that it is clear how to stay in compliance with the rule. Putting bright lines in guidance, even when the bright line is phrased as a "should" rather than as a requirement, blurs the line between guidance and rules, and for this reason, it is a practice we should avoid.

For the same reason, it is inappropriate to put mandatory language in guidance. This practice can create the same distortions as the use of bright lines.

Conclusion

Obviously, the incremental changes to our supervisory processes described above do not completely answer the question with which I began my remarks today: How can we square the public interest in agile supervision with the public interest in transparency and accountability? This should be an ongoing question of high priority, both at the Fed and more broadly among those who care about our system of financial regulation.
Equally obviously, however, these suggestions would strengthen our practice of supervision and increase the vigor and credibility of our supervisors.

The changes to supervision since the crisis have made the financial system stronger and more resilient than it was before. The incremental changes I have outlined, to increase transparency, accountability, and fairness, would make supervision more efficient and effective, and our financial system stronger and more stable.

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The fast pace and wide dissemination of electronic communication can lead to mistaken transmissions; for example, emailing the wrong person, posting a private message publicly, or sharing the wrong video.

All of these examples of mistakes may be embarrassing and have unintended consequences.

However, intentional distortions of audio and/or visual representations can be far more damaging.

Members have a duty, and a First Amendment right, to contribute to the public discourse, including through parody and satire.

However, manipulation of images and videos that are intended to mislead the public can harm that discourse and reflect discreditably on the House.

Moreover, Members or their staff posting deep fakes “could erode public trust, affect public discourse, or sway an election.”

Accordingly, Members, officers, and employees posting deep fakes or other audio-visual distortions intended to mislead the public may be in violation of the Code of Official Conduct.

Prior to disseminating any image, video, or audio file by electronic means, including social media, Members and staff are expected to take reasonable efforts to consider whether such representations are deep fakes or are intentionally distorted to mislead the public.

The Committee has long held that Members are responsible for the actions of their staff.

Further, Members must take reasonable steps to ensure that any outside organization over which the Member exercises control—including a campaign entity—operates in compliance with applicable law.

Accordingly, Members should ensure their official and campaign staff are familiar with the rules and regulations regarding electronic communications that those staff are involved in preparing or disseminating.

If you have any questions regarding this guidance, please feel free to contact the Committee's Office of Advice and Education at (202) 225-7103.

Basel III: the implementation imperative

Keynote address by Pablo Hernández de Cos, Chair of the Basel Committee on Banking Supervision and Governor of the Bank of Spain, at the 15th BCBS-FSI High-level Meeting for Africa on Strengthening financial sector supervision and current regulatory priorities, Cape Town.

Good morning, and welcome to the 15th BCBS-FSI High-level Meeting for Africa. Let me start by thanking Governor Kganyago and the South African Reserve Bank (SARB) for hosting this meeting in Cape Town.

As the global standard setter for banks, the Basel Committee places great importance on reaching out to a wide range of stakeholders to inform its work.

Events such as these high-level meetings are of particular value to the Committee in seeking the views of central banks and supervisory authorities across different regions of the world.

With a population of over 1.2 billion and a median age of 19 years, Africa will play an increasingly important role in shaping the future world economy.

The average annual GDP growth in Africa has exceeded the global average over the past several years, and six of the world's 10 fastest-growing economies hail from this continent.

My remarks today will focus primarily on the imperative of implementing the Basel Committee's post-crisis reforms.

I'm pleased to note that the SARB takes this imperative seriously: it has a strong track record of implementing the Basel III standards in a timely and consistent manner.

And Governor Kganyago's chairmanship of the Financial Stability Board's Standing Committee on Standards Implementation underscores the SARB's commitment to this imperative.

I will frame my remarks around four questions:

- Why does implementation matter?
- What has the Basel Committee done to meet the implementation imperative?

- What have we seen to date among our members?

- Where does this leave us?

To read more:
https://www.bis.org/speeches/sp200130.pdf

Policy responses to fintech: a cross-country overview

Johannes Ehrentraud, Denise Garcia Ocampo, Lorena Garzoni, Mateo Piccolo, January 2020

Technological innovations in financial services (fintech) are increasingly transforming the way financial services are provided. This transformation opens opportunities but comes with potential risks to consumers and investors and, more broadly, to financial stability and integrity, which financial regulation seeks to mitigate.

As for opportunities, fintech can support potential growth and poverty reduction by strengthening financial development, inclusion and efficiency. In this context, financial authorities are adjusting their policy frameworks and providing guidance based on their assessments of the implications of emerging technologies for the financial sector.

The challenge for policymakers is to maximise the benefits of fintech while minimizing potential risks for the financial system. However, this is easier said than done as regulators face several challenges.

Fintech developments present issues that are beyond the traditional scope of financial authorities, and the speed of innovation makes it difficult for regulators to respond in a timely manner. Also, important trade-offs may arise between different policy objectives.

This paper surveys 31 jurisdictions on their policy responses to fintech developments. The key aim of our study is to provide a cross-country overview of the responses that financial authorities have pursued in relation to fintech.

The paper is based on responses to a survey conducted in early 2019 by the Financial Stability Institute (FSI), which was supplemented by a comprehensive review of published regulations and documents as well as the authors' own analysis.

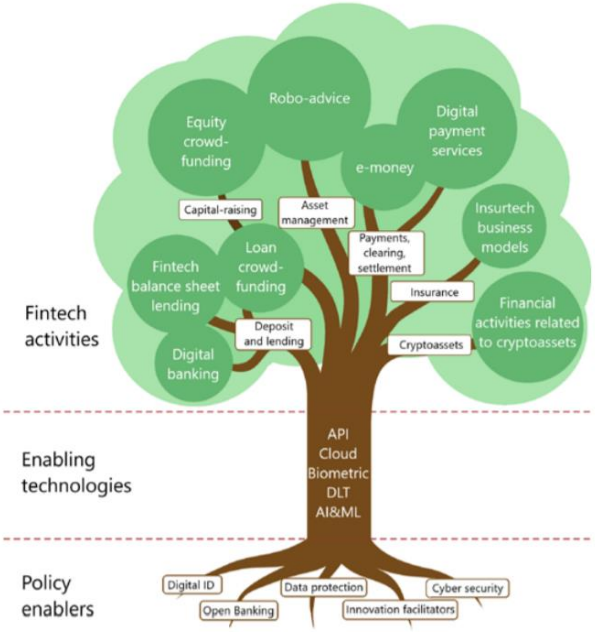
Building on the work by global standard-setting bodies and other international organisations, we propose a conceptual framework through which we analyse policy responses to fintech, referred to as the "fintech tree" (see chart on next page).

The fintech tree distinguishes three categories: fintech activities, enabling technologies and policy enablers. Fintech activities (eg digital banking or

robo-advice) can take various forms and may be performed in different sectors of the financial industry.

Enabling technologies (eg cloud computing or artificial intelligence) are those that make innovation possible in the provision of financial services and, as such, form the backbone of fintech activities. Policy enablers refer to public policy measures and initiatives (eg digital ID systems) that support
the development of fintech activities and the use of enabling technologies.

To read more:
https://www.bis.org/fsi/publ/insights23.pdf



Source: FSI staff.

Statement by the OECD/G20 Inclusive Framework on BEPS on the Two-Pillar Approach to Address the Tax Challenges Arising from the Digitalisation of the Economy

As approved by the OECD/G20 Inclusive Framework on BEPS
on 29-30 January 2020

1. In light of the strong support from the Inclusive Framework on BEPS (IF) members for reaching a multilateral agreement with respect to Pillar One and Pillar Two, and drawing on the technical work of the Working Parties, comments from the public consultation, as well as the discussion at a number of Steering Group meetings, and recognising the concurrent work on a without prejudice basis on the two pillars, members of the Inclusive Framework affirm their commitment to reach an agreement on a consensus-based solution by the end of 2020.

In further developing the two Pillars, the Inclusive Framework has therefore agreed upon an outline of the architecture of a Unified Approach on Pillar One as the basis for negotiations and welcomed the progress made on Pillar Two (which follows the outline of Pillar Two in the PoW) contained in Annexes 1 and 2 of this statement.

2. With respect to Pillar One, the IF endorses the Unified Approach (set out in Annex 1) as the basis for the negotiations of a consensus-based solution to be agreed in 2020.

The proposed reallocation of taxing rights under Pillar One would require improved tax certainty, including effective and binding dispute prevention and resolution mechanisms.

In the design and implementation of the solution, the IF also acknowledges the need to minimise complexity.

3. Members note the technical challenges to develop a workable solution as well as some areas where critical policy differences remain which will have to be resolved to reach an agreement.

They note a December 3 letter from the US Treasury Secretary to OECD Secretary-General Gurría reiterating the US political support for a multilateral solution and including a proposal to implement Pillar One on a 'safe harbour' basis.
Many IF Members express concerns that implementing Pillar One on a 'safe harbour' basis could raise major difficulties, increase uncertainty and fail to meet all of the policy objectives of the overall process.

The IF members note that, although the final decision on the matter will be taken only after the other elements of the consensus-based solution have been agreed upon, resolution of this issue is crucial to reaching consensus.

To read more: http://www.oecd.org/tax/beps/statement-by-the-oecd-g20-inclusive-framework-on-beps-january-2020.pdf

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