



Newsletter – Financial services

SUMMER 2020

The lockdown measures of Spring 2020 merely confirmed the relevance of digitalization of financial services, even if such digitalization (i) finds its limits in the need for face to face relationships and (ii) entails a possible increase in fraud and identity theft. It is therefore not by chance that digital identity is rather “in vogue” and the development of tracing applications (to fight against covid19) found significant echo in democratic concerns.

At the same time, the inclusion of environmental, social and governance (ESG) criteria is becoming increasingly important as many are convinced that the pandemic is rooted in their insufficient consideration.

The crises can also show shortcomings in the supervision of authorities (public or private): the first bankruptcy filing in the history of the DAX 30 (Wirecard) is a mere confirmation. Thus the collapse proves that short sellers were correct before anyone else, as they had identified flaws that are now proving to be frauds, despite the German supervisor's protection against short selling strategies.

France finally published its Decree for the open data of court decisions, in addition to the recent implementation of the so-called “Datajust” data processing (on predictive justice). We enter into summer with so much to say in relation to the financial sector...

1. **Impacts of the outbreak**

1.1 **Findings**

As the European Banking Authority (EBA) highlighted in its recent analysis of the impact of the pandemic on the banking sector¹ the increase of non-performing loans (NPLs) is putting banks under pressure, despite:

- state loan guarantees widely implemented in Europe² ; and
- flexibility shown by the EBA in its guidance on legislative and non-legislative moratoria on loan repayments applied in response to the pandemic³.

This latest guidance is to be read together with another one on the granting of credit and their monitoring⁴, which harmonizes internal governance in this area and addresses the (i) use of automated models, (ii) assessment of the creditworthiness of borrowers and processing of data to assess the borrowers' creditworthiness⁵.

¹ Preliminary analysis of the impact of covid19 on EU banks (25 May 2020).

² In France, a Ruling of 6 May 2020 enabled crowdfunding platforms to offer such type of loan. Currently, while more than 80% of the loans have benefited SMEs, some twenty groups with more than 5,000 employees and a turnover > €1.5 billion have also been granted such loans. The estimate of outstanding loans by the end of 2020 could reach €150bn, i.e. half of the initial amount that was announced.

³ Effective on 4 April. The ACPR applies them and has even extended their application to national financial companies (*sociétés de financement*). The EBA provides a framework for the prudential easing measures granted in Europe as part of the pandemic management; when the moratoria meet certain conditions, the loan portfolio is not *ipso facto* reclassified as renegotiated/defaulting exposures, which has a positive impact on own funds.

⁴ Published on 29 May 2020 but applicable as of 30 June 2021.

⁵ One may wonder why such guidelines were released ahead of ECB's report of 10 June 2020, which listed the credit granting practices of banks and highlighted certain weaknesses in ways these loans are granted.



1.2 Responses of Authorities

On the macroeconomic front, Authorities (ECB, national authorities, etc.) took various measures to support the economy as soon as the lockdown measures became apparent. In France, the Government:

- issued a myriad of fast track laws (which sometimes have been amended - a handful directly impacting the financial sector⁶). In particular, they have (i) suspended legal time limits to delay litigation and (ii) granted certain defaulting debtors some form of moratorium, during a period initially tied to the period of the health emergency before such period was set as a “legally protected period”; and
- launched various measures to support the financial sector (in addition to the guaranteed loan scheme), such as on credit insurance (implementation of a public reinsurance program).

In mid-May, noting a gradual normalization of risk indicators in the French market, the French securities regulator (AMF) decided to end its exceptional ban on short selling.

2. Fight against money laundering (AML/CFT)

2.1 European developments

In addition to the cross-cutting actions of Authorities in response to the pandemic, there are sectoral initiatives such as the AML/CFT, with several reports⁷ warning of risks that could arise during to the pandemic or subsequently.

While unveiling its action plan for a more effective EU wide AML/CFT⁸, the European Commission listed third countries that it perceives to be at high risk (of money laundering/terrorist financing). This list was published at the same time as the new methodology supporting creation of the list. By 1 October 2020, the most significant impacts likely to be triggered will include financial flows with Mauritius or the Bahamas.

The EBA's feedback⁹ / its conclusions on the responsibilities of the financial sector on criticized dividend arbitrage strategies¹⁰ was published as expected. The EBA sets out the underlying idea that multiple claims for the same withholding tax on such dividends is likely to trigger a tax offence in some Member States. This raises questions about (i) the role of the financial institutions involved and (ii) the proceeds of such transactions from the AML/CFT's point of view.

On another level, the European Commission seldom provides guidance on Regulations: its recent opinion¹¹ on one of the many black list Regulations is therefore worth looking at. It provides objective criteria from which it can be inferred that a legal person is “controlled” by a black listed person (without being the beneficial owner) and specifies the due diligence expected of financial institutions with regard to direct debits in or out of the accounts of a “controlled” organization/company.

It should be noted that in its guidance on digital identity published on 6 March 2020, the Financial Action Task Force (FATF) considers that situations of limited risk may justify the use of digital identity schemes

⁶ These include #2020-303/304/305/306, 2020-341 or 2020-534 (on contactless payment).

⁷ EBA statement of 31 March 2020, Europol report of 30 April 2020, FATF report of May 2020, typological analysis by the French financial intelligence unit (TRACFIN) of 28 May 2020.

⁸ 7 May 2020. It mentions (i) a possible future European Authority (instead of the EBA that was appointed in 2019 through a Regulation) or (ii) the possibility of legislation through Regulations rather than Directives (our [last newsletter](#)), which should materialize as early as the Q1 of 2021. Highly colored by the Danske bank affair, the aims of this action plan proves necessary given the recent sanction of the Swedbank (released on 19 March).

⁹ Report of 28 April 2020 (so-called “cum cum” and “cum ex” strategies).

¹⁰ For the record, arbitrage strategies consist in taking advantage of market inefficiency, which is reflected in a price differential between the theoretical value of an asset and its quoted market price.

¹¹ Released on 19 June 2020.



with a low level of guarantee, when they allow better financial inclusion of those customers facing difficulty in proving their identity. This is to keep in mind in light of the Payment Account Directive.

Finally, a form of deferral of the reporting obligations of the Directive on the exchange of information (DAC6) due to the Covid19 crisis is to be welcomed¹².

2.2 National developments

Subsequent to the 5th AMLD implementation, a Decree of 24 April 2020 included “payment accounts” as well as safes in the French national registrar of declared accounts (known as the “FICOBA”).

Furthermore, from a practical point of view, access to the register of beneficial owners has been simplified as access is now possible through to the National Institute of Industrial Property (INPI). Professionals can now access the register via an application programming interface (API) for the largest reporting institutions, or via a mere user interface (HMI), sufficient for smaller reporting institutions.

Finally, the ACPR has now put in place a new AML questionnaire for insurance and/or banking brokers.

3. Digital identity

France is partially responsible for the relative failure of European interoperability and mutual legal recognition of national digital identity schemes (better known under the acronym “eIDAS”)¹³, given it is the only major EU country that has yet to notify its national scheme to date¹⁴. This is obviously detrimental to the identification solutions that are highly valued by the financial sector.

However, fully aware that this digital identity is part of the fight against document fraud and identity theft, France actively shows interest on such subject matter. This is demonstrated through the deployment of its national mobile identification solution (AliceM) whose launch is expected in the fall of 2020, or its federated identity solutions portal (France Connect)¹⁵ and more recently:

- the release of a major report by the National Digital Council¹⁶, which sets the stage for the success of the national digital identity¹⁷ and announced an “orientation” law; et
- a public consultation of the National Assembly closed on 31 May 2020, which also announced an “orientation” law and aimed at promoting the success of the above-mentioned AliceM application;
- the recognition of private digital identity providers in support of the financial sector¹⁸, even if the framework for their certification has yet to be specified by Decree; and
- the deployment of a framework specific to certain sectoral electronic identification deployments¹⁹.

¹² Directive 2020/876 of 24 June 2020 amending Directive 2011/16/EU, as amended (DAC6).

¹³ A European Regulation, a revised draft of which is expected by the end of the year.

¹⁴ That is to say, three years after the first notification by Germany.

¹⁵ In addition to the “La Poste” digital identity, which has become the first French electronic identity with a “substantial” level of security, other identity providers of the same level, private or public, are currently in the process of certification. The development is notably in line with an order of 11 May 2020 launching an experiment whose purpose is to determine the new sectors of activity that would benefit from using France Connect, including the health sector or the rental of real estate or vehicles.

¹⁶ Published on 15 June 2020 (Digital identities, keystones of digital citizenship).

¹⁷ See for details our comments [published on LinkedIn](#) in which we called for the creation of a national digital identity as an opportunity to simplify the aggregation of citizens’ personal data through a unique identifier.

¹⁸ Allows online / secure confirmation of an Internet user’s identity by using their identity documents in the digital world in a reliable, practical and privacy-friendly way (e.g. BPI / Ubbly partnership).

¹⁹ Draft Ordinance on Electronic Identification in Telemedicine (consultation closed on 31 May 2020).



The EU is not lagging behind on this issue with the publication of a European system to detect false documents online²⁰.

4. **Brexit**

While the European Commission released on 18 March the draft Agreement to be used for its negotiation during its 2nd quarter sessions²¹, the French Parliament has taken into account the risk of no-deal, once the transition period lapses: it empowers the Government to legislate through fast track laws²². This should enable, at the level of the financial sector:

- to provide time for unit-holders of UK funds lodged in French equity savings plans (PEA) to redeem their units without the haste associated with the expected loss of the tax incentive;
- UK insurers deprived of the European passport may continue serving French policyholders until the contractual term agreed before 31 December 2020 (i.e. beyond the transition period); and more generally
- to deal with the situation of companies/organizations established on either side of the channel which carry on an economic activity in the other country.

While recent failures in the supervision of branches in certain European countries²³ were able to point out shortcomings concerning their supervision by host authorities, the EBA amended the notification forms of the European passport²⁴ so that host authorities have a more granular knowledge of the activities actually carried out. Unfortunately, it does not clarify the question of whether branches from third countries can be involved in the deployment of the European passport, which is nevertheless of interest in the context of Brexit...

5. **Europe of Investment Services**

The French legislator initiated the implementation²⁵ of the overhauled prudential regime for investment firms²⁶. As the EBA delivered draft implementing measures²⁷, UK authorities expressed their wish to amend their own rules differently²⁸. This will inevitably have an impact on the availability of the European equivalence regime UK service providers may benefit from when deploying their European activities.

It is worth noting that given the above-mentioned European developments and Brexit, the equivalence of UK investment service providers operating from UK dependencies (Jersey, Guernsey...) are likely to be adversely impacted by the AML/CFT.

²⁰ Regulation of 30 March 2020 (False and Authentic Documents Online system - FADO).

²¹ The negotiations in May and June which concluded the 4 rounds of negotiations ended with discouraging rhetoric about the future of EU-UK relations.

²² Article 59 of Law n°2020-734 of 17 June 2020 (authorization valid until 18 June 2021), in the manner of the ordinances already adopted in 2019 prior to the transition agreement, in the case of hard Brexit.

²³ Cf. the Estonian branch of Danske bank and more recently in March 2020 Swedbank (although in the latter case it was a fully-fledged subsidiary of a Swedish bank).

²⁴ Amendment of technical regulatory/implementing standards (18 June 2020), prior to their formal adoption.

²⁵ Bill adapting French law to European Union law in the economic and financial field (to be adopted in the summer of 2020 - this is only an authorization to be transposed by fast track law).

²⁶ For the record, the European legislator dissociates the prudential regime for investment firms from that for credit institutions (see Directive 2019/2034 and Regulation 2019/2033). It also took the opportunity to amend the European equivalence regime.

²⁷ Level 2 regulations (RTS/ITS) published on 4 June 2020, before their final adoption by the European Commission and entry into force in June 2021.

²⁸ Public consultation launched on 23 June 2020 by the UK supervisory authority, the FCA.

Environment Social and Governance Criteria

It should be first noted that the two French supervisors (ACPR²⁹ and AMF) are significantly involved in supporting financial institutions despite an evolving regulatory framework to tackle climate risks.

At European level, a large number of draft Regulations have been released over the past quarter, including (i) draft implementing rules relating to one of the three main bodies of rules³⁰, namely the Regulation on the transparency of ESG criteria and (ii) opinions issued by the European securities regulator (ESMA) in connection with the Benchmark Regulation. As a follow-up to the release of the Green Deal at the end of 2019, the European Commission released its legal transcript, i.e. a draft Regulation aiming at carbon neutrality by 2050.

Other developments

The above European developments should not obscure the AMF's active role in other fields, whether in terms of its feedback on (i) client profiling and matching these profiles with recommended products, (ii) AIFM reporting, (iii) compliance of institutions with MiFID2 requirements, (iv) its overhaul of policy on side pockets, or (v) discussions on shareholder activism, including short selling strategies³¹.

6. Other national developments impacting financial services

In a noteworthy decision released on 25 March, the French Supreme Court (*Cour de Cassation*) ruled clearly on the question of whether the variability of the loan interest rate may lead the lender to have to pay the borrower interest when the rate becomes negative. Given the contractual situation at hand, it ruled against such outcome, suggesting that contractual freedom makes it possible to provide for such a situation, as long as there is an express provision to that effect. In other words, remuneration of borrowers cannot be solely inferred from the mere reference of the contractual interest rate.

As anticipated, the ACPR released the type of expected reporting rules reflecting the recent recommendation issued by the High Council on Financial Stability (HCSF) on the new prudential constraints for granting of mortgages³².

In addition, a bill bearing various provisions to implement European Union law in economic and financial matters is to be adopted shortly. The Parliament is also due to introduce a system of sanctions associated with unjustified geographic blocking (see our [summer 2018 newsletter](#)). For ease of reminder, the said Regulation prohibits (i) geographic blocking practices that artificially segment national markets and (ii) all forms of discrimination (e.g. means of payment).

Finally, a recent investigation lead by the French insurance regulator (ACPR) in connection with alleged failures by insurers to respond to pandemic-related business interruption claims evoked some media uproar³³.

²⁹ For example, through a pilot exercise started in 2020 to assess the vulnerabilities of the French financial sector (banks and insurance companies) to climate risk. See the ECB Guide on the same subject published in May.

³⁰ Known by the terms or acronyms "Benchmark", "SFDR" and "Taxonomy".

³¹ The latter study calls for a reform that will impact on the threshold notification regime.

³² ACPR Instruction of 3 April 2020 relating to the monitoring of the profitability of real estate loans in France.

³³ Cf. ACPR press release of 23 June 2020, which echoed what many policyholders had perceived as the insurance scandal. The ACPR surveyed contracts on the French market and identified a small minority of clauses covering an operating loss (3%) that could be activated in the context of the pandemic.