KPMG

Banking Briefing

Q2 2015

Risk reporting | FATCA | UCITS V | Hot topics

Welcome

Welcome to the second edition of the KPMG Banking Briefing, your insights into the challenges that banks will be facing in the near future.

This Banking Briefing contains information of professional interest to the Luxembourg Banking community, organised under three or four megatrends or hot topics, along with an insightful interview with a banking expert.

Megatrends and hot topics aim to address the following questions:

- **Who are the stakeholders of the future challenge ?**
- **What is the context ?**
- **What are the challenges ?**
- **What is the impact for your organisation ?**

For this second edition, our special guest - Laure Morsy - BGL BNP Paribas Luxembourg's COO, member of the Management Board and Head of Corporate and Investment Banking (CIB) - shares how her bank is adapting to the banking, legal and regulatory challenges.

We have also chosen the following 4 topics which have - or will - have a tremendous impact on the banking industry:

- **Risk reporting :**
  Basel Committee principles for "effective risk data aggregation and risk reporting" (BCBS 239).
- **FATCA :**
  Get the FATCA ball rolling in Q2 with our mini how-to-guide.
- **UCITS V:**
  Shedding light on independence requirements between depositaries and management companies.
- **MiFID 2:**
  Discussing a smart approach to document management.

By the time you finish reading this issue of Banking Briefing, we will be about to install 150 tons of sand in front of our 39 JFK headquarters and share simple pleasures on the first beach in Luxembourg city, called "KPMG Plage". If you are in Kirchberg between 3 and 19 June, do not hesitate to come by around lunch to pick up a "bratwurst", "gelato" or a glass of "cremant"and exchange a couple of ideas on the future of the banking industry in Luxembourg.

Last but not least, our annual Banking Insight 2014 study will be published just in time for your summer holidays.

Stanislas Chambourdon

Head of Banking

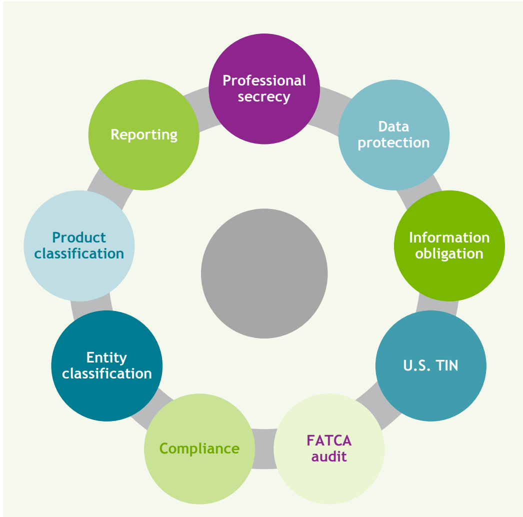
Get the FATCA ball rolling in Q2

FATCA: where we stand

Long awaited Luxembourg FATCA law adopted by Parliament

First reporting deadline for financial institutions on 30 June 2015

High penalties foreseen in case of absence of compliance



For further details refer to our FATCA newsletters...
FATCA-eAlerts

To do in Q2 2015

What?	How?
Entity classification If you have not yet done so, you need to confirm your FATCA status with an expert to check whether you have reporting obligations.	KPMG can provide you with a detailed analysis of your status and its practical consequences. and assist you in the completion of the self-certification documentation.
Registration Reporting financial institutions that have not yet registered with the IRS – the U.S. tax authorities - must do so via their portal as soon as possible, so as to receive a FATCA identification number (known as a GIIN).	Registering on the IRS portal is not a complex process if you are familiar with FATCA procedures and terminology. KPMG can help train the person that will become your financial institutions' "point of contact" for the IRS.
Compliance The Luxembourg tax authorities will perform checks to ensure that diligence rules are established; that compliance mechanisms are fully functioning; and that financial institutions do not establish practices to circumvent the exchange of information.	Ensuring that your processes and procedures are compliant is key. KPMG can help by conducting FATCA audits and health checks, which covers areas including procedure review, process checks and sampling of accounts.
Reporting The first reporting deadline for financial institutions falls on 30 June 2015: all information for 2014 will need to be submitted by this date. **The existence of an obligation to file "zero" or "nil" reporting is confirmed.**	You will need to choose a reporting tool and begin the reporting process as soon as possible. For a smaller number of accounts, manual reporting can make sense. KPMG can help in this respect. Contact us now to find out how.

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BCBS 239: the next storm

Risk reporting

From January 2016, the risk governance for many banks will change as the Basel Committee principles for "effective risk data aggregation and risk reporting (BCBS 239)" come into force. These principles, which were laid out in January 2013, will constitute an integral part of a sound risk governance framework going forward.

Although only globally systemically important banks (G-SIBs) are required to implement the principles, the Basel Committee has recommended that other banks, such as domestic systemically important banks, also integrate them into their risk framework. As such, national supervisors may choose to widen the scope to include a larger range of banks in a way that fits the size, nature and complexity of their operations.

As the ECB and other regulators have identified sound risk governance as a top priority, these principles will occupy an important place in banks' risk governance framework.

Overall, BCBS and other regulators regard the improvement of risk data architecture and reporting systems as a fundamental prerequisite for a strong risk management and risk governance framework.

IT architecture
- Risk data models unified or automatically reconcilable across banking group with unified naming conventions
- Unified level of detail of data across the group to enable fully flexible reporting
- Risk and accounting data to be reconciled
- High degree of automation for risk data aggregation, manual steps as an exception only
- Strive for single source of risk data per risk type

Data quality framework
- Effective data quality management including automated measurement methods and escalation procedures
- Comprehensive data governance for risk data including data owners from business and IT
- Documentation of reporting and reconciliation processes
- Automatic and manual quality checks in the reporting process

How to reduce 14 risk governance principles to 4 key objectives …

14 principles of data aggregation and risk reporting defined in BCBS 239

These principles translate into four key areas of objectives

Risk reporting
- Adaptable and ad-hoc reporting capability with drill-down into various risk dimensions, stress testing
- Comprehensive, timely, dependable and adaptable risk reporting capability across all units and all material risks

Organisation and IT management
- Risk reporting and aggregation to be mapped into IT strategy / implementation roadmap
- Independent validation of standard compliance
- Full business continuity capability for risk reporting

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“Adapting to the new legal and regulatory framework”


Laure Morsy

BGL BNP Paribas

Laure Morsy, BGL BNP Paribas in Luxembourg, member of the Management Board, Chief Operating Officer (COO) and Head of Corporate and Investment Banking (CIB).

Laure’s experience includes:
- management of the Financial Institutions Coverage department including the teams of Senior Bankers in charge of Financial Institutions clients worldwide;
- contribution to BNP Paribas strategy;
- management of capital allocation to clients and Counterparty Risk management and;
- promoting the exchange of best practices/ innovative solutions, client knowledge accross the teams.

> What are the main regulatory implications arising from the 2008 banking crisis?

Following the 2008 financial crisis, the European banking industry has been facing successive waves of legal and regulatory reforms which put strain not only on the business model of the players but on their operational model as well.

MIFID2/MIFIR, AEoI, BCBS 239 are still on the roadmap of projects to be implemented and raise many challenges for a universal and G-SIB bank such as BNP Paribas.

> Talking about challenges, what are the biggest obstacles you are facing in terms of regulation? How will BCBS 239 (Basel Committee on Banking Supervision “Principles for effective risk data aggregation and risk reporting”) impact BGL BNP Paribas in Luxembourg?

The first challenge is linked to the diversity of the businesses that BNP Paribas is performing in Luxembourg across different legal entities.

BNP Paribas Securities Services, Cardif Lux Vie, BNP Paribas Investment Partners and BGL have all sorts of businesses and client interactions which lead them, at a certain point in time, to ensure consistency of views on the way they implement the new set of regulations. Just to mention one of many examples - the difficulty we are going to encounter in the implementation of BCBS 239 rules is that the legal entities operating in Luxembourg do not use the same client referential.

Legal entities will have to work together to build risk data models which are unified or automatically reconciliable across entities with unified naming conventions.

> How do you manage this regulatory avalanche in terms of timing and project management?

The timetable for the implementation of the new regulations is another challenge that the whole banking industry is facing as all the projects are coming at the same time. In our view, this situation requires a strong and efficient Project Management Office organization in order to perform the gap analysis, design and monitor the transformation plans.

In 2013, BGL moved towards a single unified PMO structure serving all the businesses and functions of the bank. This organization is proving to be particularly well adapted to the current environment as regulatory projects are transversal. Having a unified PMO structure is fostering consistency and harmonization of approaches between business lines. It is helping us as well to identify the common requirements across the different regulatory projects in order to avoid duplication of work to be done.

All these factors constitute a good lever to optimize the cost of these projects which are now consuming a large part of the change budget of the bank.

> Banks are facing a myriad of issues around data quality and management. How do you cope with this? What impact will new regulatons have on your data management and IT systems?

The set of new regulations which is underway is also pushing the banking industry to completely reconsider the way they deal with their data framework. Volume and granularity of data to be exchanged will increase dramatically.

The scope of the network in which the information has to be exchanged is also becoming more and more complex (reporting to fiscal authorities and to multiple regulatory bodies in Europe but also in the US, increased disclosure of information to clients …).

Due to unflexible legacy systems, most of the banking industry IT architecture is currently not designed to comply with such significant requirements. This is why BGL has set investing in simplifying and renovating its core banking system and, as a result, lowering IT running costs as a priority.

This is the only way to be able to move swiftly and at the most appropriate cost towards meeting regulatory standards that we expect to evolve continuously over time.

The ability of the Luxembourg finance centre to evolve towards a more flexible banking secrecy regulation would certainly help in the solutions BGL is exploring to achieve this objective.

> All change management processes involve people. What measures have been taken by the bank to ensure that your people are up-to-speed with new requirements and operational challenges?

Adapting to the new legal and regulatory framework also leads to broadening the scope of responsibilities that are endorsed by banking officers. This should not be underestimated as it might put staff at risk. On our roadmap, we know we have to deal with the complexity of the information to be mastered both in functions and business lines.

Complexity is stemming from our business model: a universal and integrated bank. We are dealing with all types of clients (international high networth clients, domestic private clients, large and mid-sized corporates, financial institutions). We are confronted by divergences between regulations (FATCA/CRS/EUDAC, European/US rules on sanctions and embargos).

The revised policies on KYC and KYT are also more granular in the detail of information required from our clients.

Resources and tools have to be further developed in order to train efficiently our staff to master their new environment.

This has to be considered as well from a client management standpoint as you cannot envisage educating your clients if you have not first educated your own staff.

> Clients are the "raison d'être" for banks . Some banks are still struggling to rebuild a relationship of trust with their customers and adapt to commercial, digital and regulatory challenges at the same time. How do you remain client-focused despite these challenges?

We are putting great emphasis on trying to manage in the best possible way the impact for our clients. The regulatory challenges should not be perceived negatively by our clients. If it is easy to say it in principle, it is much more complex to turn it into reality. Nevertheless, the Management Committee as well as the Board of Directors of BGL is strongly committed to achieving this objective. We are working on all options which can help preserve the time our commercial teams dedicate to serve their clients.

We need to find the right balance between the information requiring intimacy with clients (which relies firstly on relationship managers) and information which can be extracted automatically from the big data framework.

We are also considering the set-up of competence centers, mutualized across businesses, to address the issue of mastering complex and continuously evolving regulations.

This being said, there is a long way ahead of us to digest the bulk of the regulation.

Talking independence under UCITS V

Management company and depositary independence is still in the air and we will only be reassured of the final rules once the level 2 measures are issued.

However, we have high hopes that ESMA's advice, as described below, will be taken up by the European Commission.

Appointing independent directors in both structures will be a strict requirement.

What is ESMA suggesting?

Regarding cross-shareholding, ESMA chose to follow Option 2 of the Consultation Paper. The management company/ investment company and the depositary should therefore be allowed to be part of the same group. Cross-shareholding of over 10% of capital or of the voting rights or enabling the exercise of a significant influence on the held entity are allowed as well, provided safeguards to avoid conflicts of interest have been put in place.

In addition, the Final Advice requires that the following arrangements are put in place by the management company/investment company:

- Prove to the competent authority of its home Member State that the depositary has been appointed in the sole interest of the UCITS and its investors, after comparing the entity and its competitors on cost and qualitative aspects;
- Disclose to the investors the existing link to the depositary.

Where the management company/ investment company and the depositary are part of the same group, the Final Report requires minimum thresholds of independent members in the management bodies of the entities or where applicable, in the body in charge of the supervisory functions.

The Final Report further provides elements to assess the independence of the members of the management body (where applicable, the members of the body in charge of the supervisory functions) of the management/ investment company and of the depositary. They can be considered as independent if they do not cumulate their mandate with additional memberships of management bodies, of bodies in charge of the supervisory functions, or with a position as employee in another entity within the Group. Business, family or other relationships within the Group can be considered as having an impact on independence.

What are the consequences of all these discussions around independence?

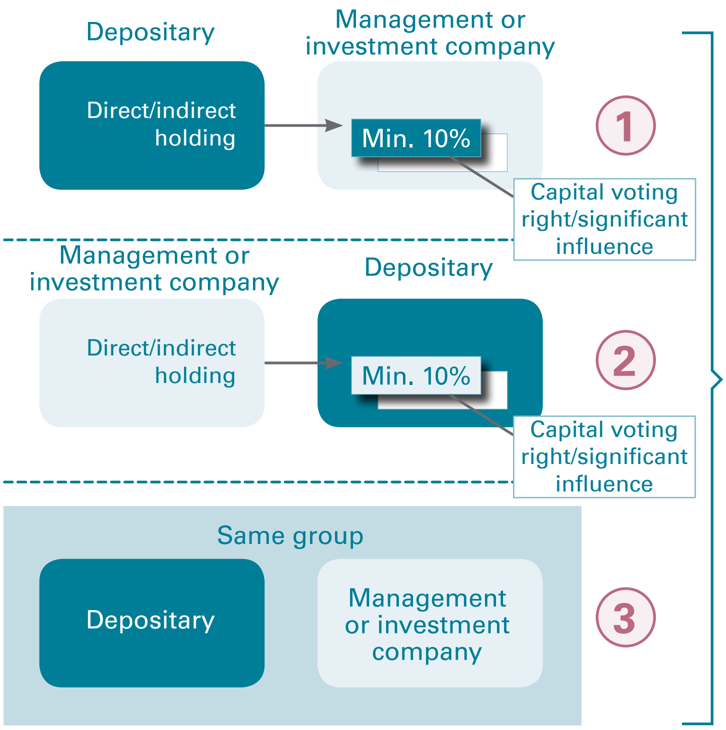
It is vital for all depositary banks to review and strengthen their conflicts of interest policy. Setting the tone in a policy will not be sufficient, the entire conflicts of interest management process needs to be improved to address effectively the key steps of a sound risk management process: identify, assess, mitigate and report.

UCITS V. Independence Rules

1) According to Level 1 of the new Directive, the management/ investment company and the depositary must act independently and solely in the interest of the UCITS and its investors
2) ESMA to opt for structural separation between the entities
3) In this respect, it will be crucial for the depositary to have detailed conflicts of interest policies and procedures, covering:
    - > Identification of conflicts
    - > Assessment of the risk of conflicts of interest
    - > Mitigating measures
    - > Ongoing monitoring
    - > Reporting/transparency

Independence requirements

Cross-shareholdings



What does the Management/ investment company have to do in cases 1, 2 and 3?

- > Avoid or identify, manage, monitor and disclose conflicts of interest
- > Demonstrate to national competent authority (CSSF) that the depositary has been appointed in the sole interest of the UCITS & investors
- > Disclose links Management/ investment company - Depositary to investors
- > Justification of the choice of the depositary to investors upon request
- > Additional safeguard for case 3: Independence rule, min.1/3 (33%) or 2, whichever is the lesser
- > In any case, for the choice of the UCITS depositary, management and investment companies need to have in place a robust decision-making process, focusing on the funds' and investors' interest and based on objective and predefined criteria.

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The smart approach to repapering

A structured approach when interacting with your clients

Banks are facing huge demands from regulators in their quest for:

- greater transparency
- increased investor protection
- efficient data gathering to manage systemic risks

It is the responsibility of bankers not to transfer all this complexity to their clients and to therefore organize the way they are collecting documents and information from new regulatory requirements.

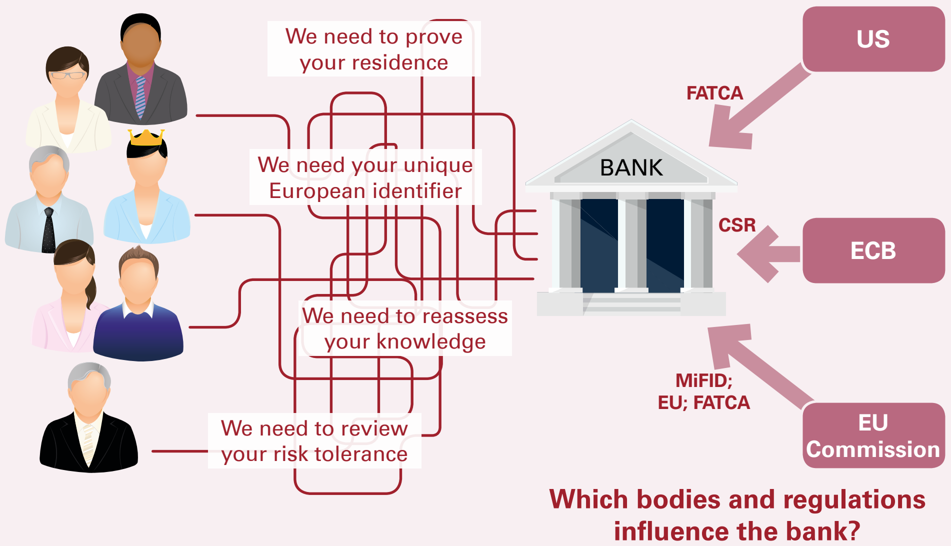
TODAY

What we see today is that banks are tending to address each regulation individually.

This is partly due to the fact that each has a different implementation deadline. However, in terms of client satisfaction, this is not the best option.

An incoherent client communication plan could lead to questions about the overall quality of information collected and about the process as a whole.

A piecemeal approach would not allow clients to see the bigger picture. This would not meet bankers' aims of educating clients and sharing the evolving rules with them in a transparent way.



Politically Exposed Persons

Key Messages

1) The regulatory burden you face should not be perceived negatively by your clients
2) Being structured in your communication with them is key for success
3) Explain what you need and why
4) Give them an important role to play in enhancing their protection
5) Put in place a tool to easily exchange info and data at their disposal
6) List all the identified needs and target dates
7) Contact your client once you have a clearer view
8) Coordinate all projects when it comes to direct contact with clients
9) Distinguish the MUST HAVE and the NICE TO HAVE
10) Explain, raise awareness, educate

TOMORROW

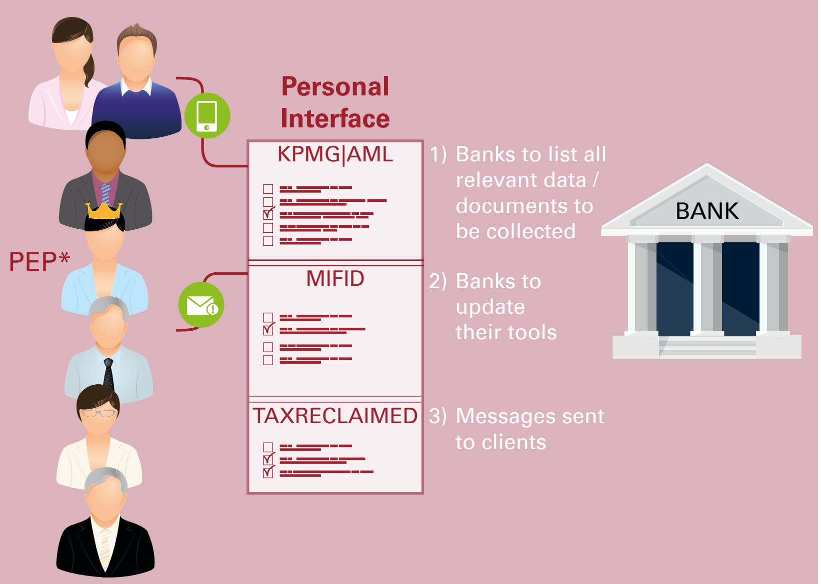
Breathe and take your time to structure your approach towards your clients before interacting with them from many angles at once.

You should only contact them once you have a clear view of what you need and when.

1. List all the identified needs (additional information, new documents for evidencing some of the qualitative data you already have, etc) **COORDINATION**
2. Link those required documents to implementation plans **PLANNING**
3. Put a **tool** to easily exchange data at clients' disposal, information **SYSTEMS**

It is key to your success that you explain what you need from them and why. You should give them an active role to play in enhancing the protection they will get from you.

Help them to understand the background of your request: explain, raise awareness, educate your people and your clients.



* Politically Exposed Persons

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Regulatory

Facing regulatory pressures on bank structures

The rules of the game have changed. The business model needs to change accordingly

Our new "Evolving banking regulation" publication discusses the following regulatory challenges faced by the banks:

- higher cost of doing business;

- constraints on balance sheet composition, business activities and legal and operational structure;

- impact of supervisory intervention on business models and strategy.

READ MORE >>

Accounting

Macro hedging

Preparing for the next phase of the project

The macro hedging project was the focus of the IASB's March 2015 meeting, with the Board discussing the remaining feedback received on its April 2014 discussion paper (DP).

READ MORE >>

IFRS-Newsletter Banking

Updates on IFRS developments impacting banks

READ MORE >>

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Tax

OECD FATCA

Common reporting standard

FATCA compliance will remain on top of the agenda of Luxembourg entities until at least 30 June 2015, i.e. the date of the first reporting under FATCA.

However, the Common reporting standard ("CSR"), sometimes nicknamed "OECD FATCA" will become the next hot topic in Q3 2015.

The deadline for CSR is December 31, 2015.

Time is flying by fast.

For further information, please visit www.kpmg.lu

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Upcoming events

3 - 19 June	KPMG Plage at 39JFK
18 June	Beach Insights for Bankers

If you would like more information, please send a note to events@kpmg.lu

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