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In this newsletter: summaries and brief updates

Summary – Financial lobby puts down shadow banking regulation

By Markus Henn

The regulation of shadow banking advances step by step. While some international recommendations are still in the making, the EU has started with some laws for implementation. The first proposal, dealing with money market funds, has been stopped by the financial lobby in the Parliament. Arguing that the proposal – already watered-down compared to international recommendations – would close down all such funds, the lobby was successful and the committee decided to take the law off the agenda two weeks ago. Another issue is shadow banking activities such as the lending of securities. A new law proposal by the European Commission aims for more transparency of these activities and prior consent by the actual owner of the securities. It remains to be seen if the financial lobby will also bring down this law.

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Brief update: Investment funds regulation amended (UCITS V)

The Council of EU Finance Ministers and the European Parliament [agreed on the revision of the 'UCITS' directive](#) on 25 February 2014. UCITS, which stands for Undertakings for Collective Investments in Transferable Securities, are the main type of investment funds available to individuals and regulated by the EU. The UCITS framework has been changed several times already to adapt to the changes in the financial markets. The revision now agreed on ('UCITS V') will:

- Extend and harmonize how national authorities can sanction misbehavior by the funds. Administrative sanctions of up to €5 million or 10 per cent of the turnover of the corporation will be introduced. Criminal sanctions are not part of the revision but member states can introduce them within two years after the revised directive enters into force.
- Introduce remuneration practices that do not encourage excessive risk-taking by UCITS managers. However, the provisions do not apply to managers from third countries to whom functions were delegated, nor are fees covered that are based on the performance.

Brief update: Banking Union almost finalised

On the road to a European Banking Union (for details see [November 2013 Newsletter](#)), there was a breakthrough in the negotiations. After [supervision of credit institutions by the European Central Bank](#) had already been agreed on, the European Parliament (EP) and the European Council also agreed on the Single Resolution Mechanism (SRM), which sets the rules for how to deal with failing banks at EU level, [on 20 March 2014](#). The mechanism will include a board with participation of the European Council, European Commission, European Central Bank and national authorities that can shut down banks facing heavy financial difficulties. The payments needed in a resolution shall be covered by a fund

financed by the banks. The fund will need to collect up to 55 billion Euros in the next eight years before becoming fully operational. The EP, however, will only be voting on a regulation covering the main aspects of the mechanism while there will be an intergovernmental agreement related to some aspects of the fund. The exclusion of the EP from the resolution board and the fund is the reason for [serious concerns over its legality](#).



Photo from Flickr by Cesar Pics

Brief update: Big and small steps with tackling tax evasion



Individuals will face more difficulties to evade taxes as the heads of EU member states in the [European Council finally amended](#) the EU's [Savings Tax Directive](#). The directive so far mainly requires automatic information exchange on interest gains between EU states (for details see [May 2013 Newsletter](#)). Now after years of resistance, Luxembourg and Austria, which so far have not applied the exchange, accepted to fully

join the directive and exchange data – but probably only by 2017. Furthermore, the exchange was extended to [more kinds of capital gains](#). The decision was [welcomed by tax justice campaigners](#).

To prevent corporate tax avoidance, the OECD further coordinates the implementation of a G20 action plan. The latest issue open for public comments was transparency of ‘transfer prices’, i.e. the prices that corporations set internally for transactions between their affiliates and that can also be used for tax avoidance (see a [civil society comment](#)). In the meantime, the EU is further reviewing its Parent-Subsidiary Directive which is about taxing the profits of trans-European corporations (for details see [December 2013 Newsletter](#)). The European Parliament’s ECON committee voted on its position on 18 March 2014, supporting the Commission’s proposals for general anti-abuse clauses and against a particular form of tax avoidance through certain types of loans. More stringent proposals by some MEPs like a minimum taxation level were rejected by the majority of the committee.

The parliament’s position is only an opinion. The ultimate decision on tax policy still lies with the Member States. The Council of EU Finance Ministers is discussing its position and plans to come to an agreement during its meeting on 20 June 2014.

Brief update: Parliament votes for ownership transparency to tackle money laundering

The EU’s Anti-Money Laundering Directive is still in the legislative review process (for an overview see [December 2013 Newsletter](#)). The European Parliament voted on its [position](#) on 11 March 2014.

One rather controversial issue dealt with in the directive is transparency of the so-called

beneficial owners, i.e. the natural person getting the ultimate benefit from a legal entity such as a company or a trust. According to the parliament’s position, which was taken with a large majority, companies and other legal entities such as trusts would have to ‘retain information on their beneficial ownership and make adequate, accurate and up-to-date information available through central public registers’. This decision was [strongly applauded by civil society’s Financial Transparency Coalition](#) as such a register can help to fight money laundering more effectively.

While the parliament was rather quick with its decision, the Council of Finance Ministers (ECOFIN) still has to deliberate and take its position. The ECOFIN could not come to an agreement in November, but it [‘confirmed the aim rapidly agreeing a general approach, so that agreement can be reached with the European Parliament before the end of its current term \(May 2014\)’](#). However, the fact that the directive is not scheduled for any official ECOFIN agenda until June 2014, could also be a contrary sign meaning that the Member States see no urgency in tackling money laundering.



Photo: "Money Laundering - Euros" by Images Money

Full articles

Financial lobby puts down shadow banking regulation

By Markus Henn

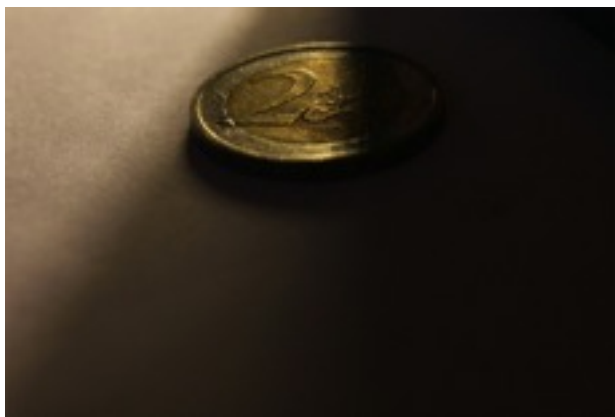


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Shadow banking remains high on the financial reform agenda as strict banking laws shift more lending and financial activities in the shadow banking system. One problem is to even define what shadow banking actually is and what part of it is dangerous (for some general information see [October 2013 Newsletter](#) and a [recent attempt by IMF economists](#)). Regardless of the exact definition, there is a consensus amongst economists as well as policy makers that some financial activities, that take place in the dark outside of the regular banking system, need to be brought to light and regulated.

The G20 Finance Ministers last month [renewed their commitment](#) to address shadow banking. As [detailed by the Financial Stability Board \(FSB\)](#), the G20's advisory body, some international standards are still being discussed at the international level. In the mean time, some states already ramp up their efforts to regulate activities that have already been addressed by the FSB or that are perceived by them as shadow banking. [Chinese authorities recently imposed capital requirements](#) on a new type of financial instrument that does not appear on the banks' balance sheets.

In the EU, the first shadow banking activity addressed was Money Market Funds (MMFs) (for an overview see [October 2013 Newsletter](#)). This step was recommended not only by the FSB but also by the European Systemic Risk Board (ESRB). Both [advised to regulate MMFs](#). The ESRB even recommended the prohibition of a certain kind of MMF that promises a so-called 'Constant Net Asset Value', i.e. the asset prices of the fund are promised to be constant to investors and are not adjusted permanently to market prices. While this sounds useful for investors, it also creates an incentive for them to leave the fund in case they believe the true value deviates significantly from the promised constant value. If many investors do this, the fund will quickly be insolvent. The prohibition of such funds also was [supported by the Finance Ministers of France and Germany](#).

When the European Commission last year released its [proposal for a Regulation on Money Market Funds](#) (for details see [October 2013 Newsletter](#)), it became clear that it had not followed a strong approach. It only proposed to require the funds to have a capital buffer (3 per cent of the fund's assets) and to hold financial instruments that can be converted into cash daily (10 per cent of the assets) or weekly (20 per cent).

Despite this lenient approach by the Commission, many financial lobbyists still heavily complained about it. Especially the MMF providers argued that the constant value funds would effectively be prohibited by the capital and cash requirements. This argument is rather telling as it admits that the funds could not sustain even a little capital buffer. It was reported that not only funds but also ['local authorities and charities across Europe'](#) were concerned about the proposal. A deeper look reveals that this lobbyism obviously does not come from local authorities and charities themselves but from investment firms specialised in advising them on investments like [CCLA Investment Management](#). This is a striking example of the deep interconnectedness of the state and the

financial sector, which the financial lobby has actively created and which it can now exploit to sabotage any regulation.

The complaints were fruitful. In the second week of March, the Economic and Monetary Affairs (ECON) Committee of the European Parliament [abandoned](#) the Commission's proposal. During the committee session, Belgian MEP Philippe Lamberts (Greens) [accused other MEPs of 'delaying tactics'](#) and said: 'I am not a finance person but I know enough to tell truth from bullshit. As a legislator, surrendering to the bullying of the industry, I won't take it.' His comment, however, could not beat the financial lobby, as the majority of the Committee was in favour of stopping the law. Only the new parliament elected in May could now again try to regulate money market funds.

Next to the funds, there are still other shadow banking issues on the agenda of the international regulatory bodies. The FSB intends to release recommendations on two types of activities:

1. 'repos', agreements to purchase and later re-purchase a financial product, mainly used to have short-term cash available;
2. 'securities lending', which is when a bank or other firm lends its securities to others, a practice that is often used for short selling (i.e. bets on falling prices).

In parallel the Basel Committee is working on banks' interactions with shadow banks. The European Commission has now already addressed these issues under the label of "Securities Transaction Financing" (STFs). It released a respective [proposal for a Regulation](#) on 29 January 2014. The proposal foresees new transparency for such transactions at two levels: Firstly, by reporting them to a central official database, and secondly by stating them in the funds' investor reports and pre-investment documents. Furthermore, the proposal addresses the so-called 'rehypothecation', which is for example if a collateral (e.g. cash) deposited by an investor at a bank is used by this bank for its own investment purposes. For this activity, the law proposal sets certain minimum standards, particularly the prior consent of the initial collateral depositor. With the additional information and the better management of rehypothecation, the Commission thinks that supervisors will be empowered to better regulate this type of shadow

banking. However, apart from the prior consent, there is no rule going beyond transparency and changing the business models. It is also likely that the financial lobby will do its best to bring down even this weak law.

Calendar of official events

For background to the official agenda of European institutions, see the following websites:

- The [European Commission \(EC\)](#)
- The [Economic and Financial Affairs Council \(ECOFIN\)](#)
- The [European Council](#)
- The [Economics and Monetary Affairs Committee \(ECON\) of the European Parliament](#)
- The [Financial Stability Board](#)

The links below give the website with updates and overviews of documents and dates related to the EU decision making process.

2014

March

- **24-25, ECON (Brussels):** Meeting
- **28-29, Conference (Helsinki):** [Global Green-Left Conference on the Future of the Union: "Alter-EU: Beyond the Social Dimension of the EMU"](#)

April

- **1, ECON (Brussels):** Meeting
- **1-2, ECOFIN (Athens):** Informal meeting
- **2-3, EP (Brussels):** Plenary
- **7, ECON (Brussels):** Meeting
- **10-11, G20 (Washington):** Finance Deputies, Ministers and Central Bank Governors meeting
- **12-13, World Bank / IMF (Washington):** Spring Meeting
- **14-17, EP (Strasbourg):** Last plenary session before elections
- **15, EP (Strasbourg):** Plenary, 1st reading/ single reading on [European Long-term Investment Funds](#)
- **16, EP (Strasbourg):** Plenary, 1st reading/ single reading on [Recovery and resolution of credit institutions and investment firms](#) and on [Taxation of parent companies and subsidiaries](#)

May

- **6, ECOFIN (Brussels):** Meeting, possible agreement on FTT
- **15-16, European Council (Brussels):** Meeting
- **19-23, TTIP (Washington):** 5th round of negotiations

- **15-25, Blockupy (Frankfurt):** Days of Action 'Solidarity Beyond Borders – Building Democracy From Below'
- **22-25, EP (Europe):** Elections

June

- **20, ECOFIN (Brussels):** Meeting, possible agreement on taxation of parent companies and subsidiaries; discussion on common consolidated corporate tax base, and single supervisory mechanism, fiscal pact
- **20-21, C20 (Melbourne, Australia):** [Summit civil society organisations in the G20 process](#)
- **22-23, G20 (Melbourne, Australia):** [Finance and Central Bank Deputies meeting](#)
- **26-27, European Council (Brussels):** Meeting of EU heads of state

July

- **22, ECON (Brussels):** Meeting

August

- **19-23, Attac (Paris):** Summer Academy

September

- **3-4, ECON (Brussels):** Meeting
- **18-21, G20 (Cairns, Australia):** [Finance and Central Bank Deputies meeting](#)
- **22-23, ECON (Brussels):** Meeting
- **30, ECON (Brussels):** Meeting

October

- **7, ECON (Brussels):** Meeting
- **13, ECON (Brussels):** Meeting

November

- **3-4, ECON (Brussels):** Meeting
- **11, ECON (Brussels):** Meeting
- **13-15, G20 (Brisbane, Australia):** [Possible Deputy Finance Ministers and Central Banks communiqué drafting](#)
- **15-16, G20 (Brisbane, Australia):** [Heads of State Summit](#)
- **17, ECON (Brussels):** Meeting

December

- **1-2, ECON (Brussels):** Meeting
- **8, ECON (Brussels):** Meeting

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This newsletter is produced by SOMO and WEED and is intended for wide circulation to interested parties. We appreciate receiving feedback as well as announcements of research reports, campaign actions, and meetings, which can be sent to m.vander.stichele@somo.nl.

