Institute of International Bankers

Global Survey 2000

Regulatory and Market Developments

Banking - Securities - Insurance
Covering 46 Countries and the EU

September 2000

OVERVIEW

The Institute of International Bankers is an association whose mission is to represent internationally headquartered financial firms that engage in banking, securities and/or insurance activities in the United States. This thirteenth annual *Global Survey of Regulatory and Market Developments in Banking, Securities and Insurance* is part of the Institute's efforts to contribute to the understanding of the trends toward globalization of financial markets and convergence of regulatory systems around the world. This year's Global Survey covers developments during the period from July 1, 1999 to June 30, 2000 in 46 countries and the European Union (EU) and is published with the cooperation of banking associations and financial services supervisory authorities from those countries and the EU.

The most significant development during this period was also the most anti-climactic: the changeover to the Year 2000. The country chapters testify to the success achieved through the combined cooperative efforts of the public and private sectors to address the Year 2000 problem both within individual countries and internationally. None of the countries participating in this year's Survey reported any significant disruptions in the operation of their financial systems as a result of the Year 2000. Indeed, there are strong indicators that the intensive efforts by banks and other financial institutions to renovate and test their systems and develop contingency plans for the Year 2000 yielded a number of important collateral benefits, including a better understanding and increased enhancement of their information technology systems and improvements in their business continuity planning.

Another development with important ramifications for the international financial markets is the implementation of a single currency, the euro, by the eleven countries comprising the Economic and Monetary Union (EMU). Although the euro's trading value has declined since its inception, the country chapters indicate that so far the operational transition to the euro has been accomplished smoothly. Much work still remains to prepare consumers in EMU countries for the transition to the ultimate disappearance of their local currencies in favor of euro banknotes and coins as legal tender for cash transactions, which is scheduled to occur by January 1, 2002.

A number of countries continue to grapple with how to reform their domestic regulatory systems to enable them to meet the challenges presented by the formation of complex financial groups that are engaged in a diverse array of activities both at home and abroad. For example, Japan has established a new Financial Services Agency, which will assume the responsibilities previously exercised by the Financial Supervisory Agency, the Financial Planning Bureau of the Ministry of Finance and, when its mandate expires in January 2001, the Financial Reconstruction Commission.

Reviews of existing regulatory and supervisory relationships are underway in South Africa and Switzerland, while Belgium and the Netherlands are striving to strengthen cooperation among existing authorities. Elsewhere, significant changes in the allocation of supervisory responsibilities within the financial sector have been legislated in Latvia (where a new "Financial and Capital Markets Committee" will assume responsibility for consolidated supervision of the financial system starting July 1, 2001), Turkey (which has vested bank supervisory authority in a new "Banking Auditing and Regulation Institute") and Venezuela (where a "Financial Regulation Board" has been established to oversee the financial system).

The global trend clearly is in the direction of some form of "umbrella" oversight, but there remains as yet no international consensus on what governmental authority or authorities should exercise this responsibility.

In the United States, the Federal Reserve Board has been vested with statutory responsibility for "umbrella" oversight of "financial holding companies" established under the Gramm-Leach-Bliley (GLB) Act, which was enacted in November 1999. Culminating the twenty-year effort to pass comprehensive financial modernization legislation, the GLB Act repeals provisions of the Glass-Steagall Act that for more than six decades restricted affiliations between commercial and investment banks and permits financial holding companies to own commercial banks and engage through separate, nonbank subsidiaries in securities underwriting, insurance underwriting, merchant banking and other types of activities that are financial in nature. To qualify for these expanded powers, a financial holding company must ensure that each of its depository institution subsidiaries are (and remain) "well capitalized" – i.e., a minimum Tier 1 and total risk-based capital ratio of 6% and 10% respectively, and a minimum leverage ratio (Tier 1 capital to total assets unadjusted for risk) of 5% – and "well managed" and have at least a "satisfactory" rating in addressing the financial needs of their community under the Community Reinvestment Act (CRA). The appropriate primary bank regulators (e.g., the Office of the Comptroller of the Currency (OCC) in the case of national banks and the state banking agencies in the case of state-chartered banks) and functional regulators (e.g., the Securities and Exchange Commission in the case of securities broker-dealers, and state insurance commissioners in the case of insurance companies) oversee the component operations of a financial holding company, with umbrella oversight of the consolidated group entrusted to the Board.

The GLB Act also authorizes national banks, with the approval of the OCC, to engage through "financial subsidiaries" in the expanded financial activities that are permissible for financial holding companies, except merchant banking and insurance underwriting. Among other conditions for the establishment of a financial subsidiary, the national bank must be (and remain) "well capitalized" and "well managed" and have at least a "satisfactory" CRA rating. The activities of national banks and their financial subsidiaries are overseen on a consolidated basis by the OCC, with the appropriate functional regulator responsible for oversight of individual financial subsidiaries.

International banks are eligible under the GLB Act to be treated as financial holding companies and thus engage in the expanded financial activities permissible for financial holding companies, subject to capital and management standards "comparable" to those required for domestic institutions. The GLB Act directs that these standards be applied by the Board, "giving due regard to the principle of national treatment and equality of competitive opportunity." In its exercise of this authority, the Board has adopted a regulation requiring that international banks that seek to become financial holding companies have a Tier 1 and total risk-based capital ratio of at least 6% and 10%, respectively (for banks from countries that have adopted risk-based capital standards consistent with the Basel Accord, this determination is made on the basis of home country standards), and a minimum leverage ratio (Tier 1 capital to total assets unadjusted for risk) of 3%. International banks that do not satisfy these criteria nevertheless may become financial holding companies if the Board, in its discretion, determines that their capital is "otherwise comparable to the capital that would be required for a U.S. bank owned by a financial holding company." In addition, the Board's regulation calls for a finding by the Board that the management of an international bank as a global entity "meets standards comparable to those required of a U.S. bank owned by a financial holding company."

While the Board has been flexible in applying these standards to international banks, the requirements it has imposed in its regulation have been the source of considerable debate and comment. The Institute, the European Commission and others have raised particular concerns regarding the Board's imposition of a leverage test on international banks, regardless of whether an international bank is subject to any such test under its home country capital standards. In this connection, it has been suggested that the "well capitalized" standard applied to international banks under the GLB Act should be based entirely on the internationally agreed upon Basel risk-based capital methodology and that international banks should not be subject to a leverage requirement as a condition to expanding their nonbanking activities in the United States unless and until such a requirement were incorporated into the Basel Accord.

To provide an international comparative perspective on these matters, contributors to this year's Survey were asked to discuss whether the appropriate banking authority in their country, in its capacity as a host country regulator, independently assesses the capital of a non-domestic banking organization as a global entity on the basis of standards comparable to those applied to domestic banking organizations (even if in excess of minimum international standards) in connection with the expansion of the non-domestic banking organization's nonbanking activities in the host country. Among the countries covered by this year's Survey, this approach was found only in the United States (see the new table appearing at page 1 of the Survey).

A second matter selected for special attention in this year's Survey is the extent to which branches of non-domestic banking organizations as a general matter are subject under host country law to any type of asset pledge requirement whereby they must maintain on deposit with local custodian banks a specified minimum amount (determined, for example, as a percentage of the branch's total liabilities to third parties) of liquid assets such as domestic government securities that would be available to the appropriate host country authority in connection with the liquidation of the branch. Such requirements are distinguished from (i) minimum "endowment capital" requirements, pursuant to which a branch must be established with a minimum amount of freely available funds as prescribed by the host country, and (ii) "asset maintenance" requirements, pursuant to which a host country regulator may require branches of non-domestic banking organizations to maintain in the host country a certain level of assets in relation to liabilities.

This topic relates directly to continuing efforts by the Institute to achieve comprehensive reform of the asset pledge requirements applicable to U.S. branches and agencies of international banks under state and federal law. To provide an international comparative perspective on practices in the United States, contributors were asked whether the branches of U.S. and other non-domestic banking organizations operating in their country are subject to any such requirement. As reported in another new table appearing at the beginning of the Survey, asset pledge requirements were found to exist in only the United States and Canada.

As in past years, the Survey includes an updated table on permissible se curities, insurance and real estate activities of banking organizations in various countries. In addition, this year's Survey includes updated charts on the permissibility of merchant banking activities, supervision of financial conglomerates, host country supervision of non-domestic banks' branches, host country "umbrella" supervision of non-domestic banking organizations, and implementation of capital adequacy requirements for market risk.

The Survey also describes a number of other significant developments occurring in global financial markets. Deposit insurance schemes have been strengthened in several countries, including France, Ireland and Japan. A number of countries, including Brazil, China, Panama and Turkey, instituted changes to enhance their banks' practices regarding classification of assets and loan loss provisions. Measures to improve banks' assessment of their country risks have been introduced in Latvia and the Netherlands, while efforts to promote risk management practices within banks in general have been initiated in India and Israel. Corporate governance issues have received increasing attention in several jurisdictions, including Australia, Hong Kong and Singapore. Reforms in accounting and financial reporting practices to bring them up to the level of international standards have been adopted in Bahrain, the Philippines and South Africa.

A theme common to many country chapters is the extensive efforts that are underway to adapt banking and other financial services to developments in the "new economy". For example, the chapters on Germany and Sweden describe initiatives to promote Internet payment systems and virtual banking. The European Union (EU) has issued a Directive establishing the legal framework for electronic signatures. Similarly, legislation on this subject has been enacted in countries such as Australia, Colombia and the United States. The EU has also taken a lead in authorizing nonbanks to issue electronic money through the formation of electronic money institutions (ELMIs).

Further actions have been taken, or are under consideration, in a number of countries to combat money laundering. Legislation prohibiting money laundering was introduced in Israel, while in other countries, including Italy and Japan, measures to expand the predicate crimes that can give rise to money laundering violations have been enacted. Actions to enhance the effectiveness of suspicious activity reporting have been instituted in Canada and Colombia. At the international level, the Financial Action Task Force on Money Laundering in June 2000 issued a report identifying fifteen jurisdictions whose existing measures to combat money laundering are deemed to be inadequate.

Privatization of banks continues in a number of countries, including the Czech Republic and Poland. Pressures for in-market consolidations intensified, as evidenced in Asia by the agreements among several of the largest banks in Japan to combine into new financial groups and in Europe by the formation of Banco Bilbao Vizcaya Argentaria from two of the larger Spanish banks and the merger discussions that have been conducted among the largest German banks. Cross-border merger activity has also continued, as witnessed by the recently announced merger of HypoVereinsbank and Bank Austria and the continuing integration occurring within the Nordic region.

In the securities area, advances in information and communications technology have sparked the emergence of electronic communications networks (ECNs), which in turn has placed growing competitive pressures on traditional exchanges. In Europe, this dynamic has combined with the adoption of the euro as the single currency throughout the EMU to encourage the consolidation of exchanges. For example, the Brussels, Paris and Amsterdam Exchanges are combining into a new exchange named "Euronext". The five exchanges and clearing houses in Hong Kong have merged into a new public company, Hong Kong Exchanges and Clearing Limited. In addition, new markets for trading in shares of "new economy" and other previously unlisted companies have been established in several countries, including Italy (the "Nuovo Mercato"), Japan ("NASDAQ Japan") and Korea (the "Third Market"). The problems that can arise in connection with cross-border consolidations of exchanges were illustrated by the experience of the London Stock Exchange, which in September 2000 withdrew from a proposed merger with the Deutsche Börse, citing the need to defend against the hostile bid made in late August by Sweden's OM Gruppen.

The country chapters thus attest to not only the continuing challenges confronting the international financial community as it enters the new millenium, but also, and in a critical sense more importantly, the rich variety of the efforts by financial institutions and their regulators to adapt to a constantly changing environment.

In closing, we express the Institute's deep gratitude to the banking associations and financial services supervisory authorities that have contributed to this year's Survey and without whose assistance this publication would not be possible.

Gonzalo de Las Heras
Chairman

Lawrence R. Uhlick
Executive Director and
General Counsel

For further information contact:

Institute of International Bankers
299 Park Avenue
New York, New York 10171
Tel: (212) 421-1611
Fax: (212) 421-1119
E-Mail: IIB@IIB.org
http://www.iib.org

TABLE OF CONTENTS

INDEPENDENT ASSESSMENT OF THE CAPITAL OF A NON-DOMESTIC BANKING ORGANIZATION AS A GLOBAL ENTITY BY A HOST COUNTRY REGULATOR ON THE BASIS OF STANDARDS COMPARABLE TO THOSE APPLIED TO DOMESTIC BANKING ORGANIZATIONS (EVEN IF IN EXCESS OF MINIMUM INTERNATIONAL STANDARDS) IN CONNECTION WITH THE NON-DOMESTIC BANKING ORGANIZATON'S EXPANSION OF ITS NON-BANKING ACTIVITIES IN THE HOST COUNTRY

Host Country Regulator Makes Such an Independent Assessment of the Capital of a Non-Domestic Banking Organization in connection with Expansion of Its Non-Banking Activities in the Host Country	**Host Country Regulator Does *Not* Make Such an Independent Assessment of the Capital of a Non-Domestic Banking Organization in connection with Expansion of Its Non-Banking Activities in the Host Country**	
United States[1]	Argentina	Korea
	Australia[2]	Latvia
	Bahrain	Luxembourg
	Belgium	Netherlands
	Bermuda	Norway
	Canada	Panama
	Denmark	Philippines
	Finland	Poland
	France	Portugal
	Germany	Spain
	Hong Kong	Sweden
	Ireland	Turkey
	Italy	United Kingdom
	Japan	Venezuela

1 In the United States, an international bank that operates U.S. branches or agencies may engage in the expanded financial activities permissible for financial holding companies under the Gramm-Leach-Bliley Act (such as securities underwriting, insurance underwriting and merchant banking), provided that the bank meets a capital standard "comparable" to the "well capitalized" standard that applies to the conduct of such activities by domestic financial holding companies – i.e., each depository institution subsidiary of a financial holding company must have a minimum Tier 1 and total risk-based capital ratio of 6% and 10% respectively, and a minimum leverage ratio (Tier 1 capital to total assets unadjusted for risk) of 5%. As applied by the Federal Reserve Board to international banks, the "comparable" capital standard calls for an international bank that seeks treatment as a financial holding company to have and maintain a Tier 1 and total risk-based capital ratio (as determined under home country standards where consistent with the Basel Accord) of at least 6% and 10%, respectively, as well as a leverage ratio (Tier 1 capital to total assets unadjusted for risk) equal to at least 3%. The 3% minimum leverage ratio applies regardless of whether an international bank's home country supervisor requires it to meet any leverage ratio. An international bank that does not satisfy these criteria may request a prior determination from the Board that its capital is "otherwise comparable to the capital that would be required of a U.S. bank owned by a financial holding company."

2 Where the expansion of non-banking activities involves insurance operations, authorization from the Australian Prudential Regulation Authority, the regulator of the insurance industry in Australia, is required. Any decision to grant an authority would involve an assessment of the standing of a non-domestic banking organization, including its capital adequacy, but this would not entail application of Australian capital standards to the banking organization.

APPLICABILITY OF ASSET PLEDGE REQUIREMENTS TO BRANCHES OF NON-DOMESTIC BANKING ORGANIZATIONS OPERATING IN A HOST COUNTRY[1]

Branches Are Subject to Asset Pledge Requirements	Branches Are Not Subject to Asset Pledge Requirements	
Canada	Argentina	Korea
United States[2]	Australia	Latvia
	Bahrain	Luxembourg
	Belgium	Netherlands
	Cayman Islands	Norway
	Denmark	Panama
	Finland	Philippines
	France	Poland
	Germany	Portugal
	Hong Kong	Spain
	India	Sweden
	Ireland	Turkey
	Italy	United Kingdom
	Japan	

1 Asset pledge requirements refer to any host country law or regulation that as a general matter requires branches of non-domestic banking organizations to maintain on deposit with local custodian banks a specified minimum amount (determined, for example, as a percentage of the branch's total liabilities to third parties) of liquid assets such as domestic government securities that would be available to the appropriate host country authority in connection with the liquidation of the branch. Such requirements are distinguished from (i) minimum "endowment capital" requirements, pursuant to which a branch must be established with a minimum amount of freely available funds as prescribed by the host country, and (ii) "asset maintenance" requirements, pursuant to which a host country regulator may require branches of non-domestic banking organizations to maintain in the host country a certain level of assets in relation to liabilities. Among the surveyed countries, Bermuda and Colombia do not permit non-domestic banking organizations to operate through branches, and therefore the issue does not arise.

2 U.S. branches and agencies of international banks are subject to asset pledge requirements under applicable federal and state law. At the federal level, the International Banking Act of 1978 provides that branches and agencies licensed by the Office of the Comptroller of the Currency must maintain a "capital equivalency deposit" equal to at least 5% of their total liabilities. Requirements under state laws vary. For example, branches and agencies licensed by the State of Illinois are not required as a general matter to pledge assets, although the Commissioner retains the discretion to impose an asset pledge requirement when deemed "necessary and appropriate". New York-licensed branches and agencies are currently subject to a 5% asset pledge requirement with respect to their third-party liabilities.

PERMISSIBILITY OF MERCHANT BANKING ACTIVITIES[1]

Banking Organizations Are Prohibited from Conducting Merchant Banking[2]	Merchant Banking Is Permissible for Banks Pursuant To Their General Authority To Invest in Non-Financial Companies		Merchant Banking Is Permissible for Nonbank Affiliates of Banks or Specially Licensed Entities
Chile	Australia	Italy	Canada
China	Austria	Latvia	Egypt
Colombia	Bahrain	Luxembourg	Indonesia
Poland	Belgium	Netherlands	Israel[7]
Uruguay	Bermuda	Norway	Japan[8]
	Brazil	Panama[4]	Korea
	Cayman Islands	Philippines[5]	Nigeria[9]
	Czech Republic	Portugal	United States[10]
	Denmark	Singapore[6]	
	Estonia	South Africa	
	Finland	Spain	
	France	Sweden	
	Germany	Switzerland	
	Hong Kong[3]	United Kingdom	
	Ireland	Venezuela	

1 As used in this table, "merchant banking" is the business of investing for one's own account, either directly or indirectly through an affiliate, in the shares or other ownership interests of non-financial companies for the purpose of capital appreciation and ultimate resale or disposition and is understood to be different from making permanent investments in non-financial companies to diversify the investor's business activities.

2 Merchant banking is either expressly prohibited by law or is not otherwise permissible under applicable statutory and regulatory provisions.

3 The holding of shares by Hong Kong banks is subject to restrictions based on the capital of the bank.

4 Although the law in Panama does not contemplate a special "merchant banking" license, a bank may obtain a banking license for the sole purpose of conducting such business.

5 Philippine banks may invest in both financial and non-financial allied undertakings. Expanded commercial banks are also authorized to exercise the powers of investment houses, to invest in the equity of non-allied undertakings and to own up to 100 percent of the equity of a financial intermediary other than a commercial bank.

6 Generally, in Singapore merchant banking investments should not exceed 20 percent of the shares of any company, unless the acquisition is by way of fulfilling an investor's obligations under an underwriting agreement.

7 Merchant banking is permissible for separately licensed "banks for business promotion".

8 In Japan, merchant banking is permissible for securities subsidiaries of banks.

9 Merchant banking is permissible for separately licensed "merchant banks".

10 The Glass-Steagall Act generally prohibits U.S. banks from owning equity interests in other companies, but they may conduct limited merchant banking activities outside the United States through Edge Act subsidiaries. Under the Gramm-Leach-Bliley Act, financial holding companies that have securities affiliates may engage in merchant banking activities (including the acquisition of controlling interests in non-financial companies) subject to certain regulatory restrictions prescribed by the Federal Reserve Board (e.g., limits on aggregate amounts of merchant banking investments and restricted holding periods). Bank holding companies that do not satisfy the criteria for becoming a financial holding company are subject to strict limitations on their investments in non-financial companies, including the following: (i) the bank holding company may not own in the aggregate more than 5 percent of any class of the voting shares of a non-financial company and 25 percent or more of any such company's total equity (voting and non-voting) and (ii) such investments must be held on a passive, noncontrolling basis.

REGULATION OF FINANCIAL CONGLOMERATES

A Single Regulator Oversees the Activities of All Financial Conglomerates as a Whole	Identity of the Lead Regulator for A Financial Conglomerate Is Determined on the Basis of the Financial Conglomerate's Principal Activity	Financial Conglomerates Operate Without A Single or Lead Regulator
Australia Bolivia Canada[1] Cayman Islands Colombia Denmark Japan Korea Norway Peru Singapore Sweden United Kingdom	Argentina[2] Austria Estonia[3] Greece Ireland Israel Latvia[4] Philippines[5] Spain United States[6] Venezuela	Bahrain Belgium Chile Czech Republic Finland France Germany Hong Kong Italy Luxembourg Netherlands Panama[7] Poland Portugal Romania South Africa Switzerland Turkey Uruguay[8]

For purposes of this chart, a "financial conglomerate" is a group of companies under common control that engage exclusively or predominantly in financial services in two or more financial sectors such as banking, securities and insurance. See "The Supervision of Financial Conglomerates," A Report by the Tripartite Group of Bank, Securities and Insurance Regulators (July 1995).

See the text of the footnotes on the next page for additional explanatory information.

[1] In Canada, the Office of the Superintendent of Financial Services oversees the operations of financial conglomerates at the federal level. Certain companies within a financial conglomerate (e.g., securities firms and insurance companies) may also be subject to supervision by provincial authorities.

[2] In Argentina, only financial conglomerates headed by banks are subject to consolidated regulation.

[3] The Estonian Central Bank is the lead regulator of financial conglomerates that include banks. Financial conglomerates that do not include banks do not have a lead regulator.

[4] Effective January 1, 1999, but only with respect to conglomerates headed by a bank or financial holding company registered in Latvia, in which case the Bank of Latvia is the lead regulator.

[5] In the Philippines, the Central Bank has supervisory authority over banks and their subsidiaries and affiliates, as well as nonbank financial institutions with quasi-banking or trust authority. The Office of the Insurance Commissioner supervises insurance companies that are subsidiaries or affiliates of banks. Nonbank financial institutions that are subsidiaries and affiliates of banks and other financial institutions where their charter provides that they will be under the Central Bank's supervision are regulated jointly by the Central Bank and the Securities and Exchange Commission (SEC). The SEC regulates other nonbank financial institutions that do not fall under these classifications.

[6] In the United States, financial conglomerates that include banks and that are organized as bank holding companies (or whose bank holding company qualifies for treatment as a "financial holding company" under the Gramm-Leach-Bliley Act) are subject to umbrella supervision by the Federal Reserve Board, with the activities of subsidiaries of the bank/financial holding company regulated by the appropriate primary bank and "functional" regulators (e.g., the Office of the Comptroller of the Currency (OCC) in the case of national banks, a state banking agency in the case of state-chartered banks, the Securities and Exchange Commission in the case of securities firms, and a state insurance commission in the case of insurance companies). Nonbank financial conglomerates (i.e., those comprised of only nonbank financial institutions such as securities firms, insurance companies and commercial finance companies) are not regulated at the group level, although the Securities and Exchange Commission requires registered broker-dealers to file with it quarterly risk assessment reports regarding their material affiliates. The Gramm-Leach-Bliley Act for the first time permits national banks, with the approval of the OCC, to establish "financial subsidiaries" through which they may engage in financial activities that are permissible for financial holding companies (including securities underwriting and dealing but excluding insurance underwriting and merchant banking). The activities of national banks and their financial subsidiaries are subject to consolidated oversight by the OCC, with the appropriate functional regulator responsible for oversight of individual financial subsidiaries.

[7] In Panama, only financial conglomerates that include banks are regulated on a group-wide basis.

[8] The Central Bank of Uruguay regulates separate companies within a financial conglomerate (e.g., banks, insurance companies, investment fund managers and pension fund managers) but not the group as a whole.

HOST COUNTRY SUPERVISION OF BRANCHES OF NON-DOMESTIC BANKS[1]

Host Country Generally Relies on Global Supervision by the Home Country[2]	Host Country Applies Its Supervisory Standards Apart from the Home Country[5]		
Bahrain	Argentina	France	Philippines
Cayman Islands	Australia	Germany	Poland
Hong Kong[3]	Austria	Greece	Portugal
Panama[4]	Belgium	Indonesia	Singapore
Romania	Bolivia	Ireland	South Africa
	Brazil	Italy	Spain
	Chile	Japan[7]	Sweden
	China	Korea	Switzerland
	Colombia	Latvia	Turkey
	Czech Republic	Luxembourg	United States[8]
	Denmark	Netherlands	United Kingdom
	Estonia[6]	Nigeria	Uruguay
	Finland	Norway	Venezuela
		Peru	

[1] Host country supervisory practices may be subject to cooperative agreements with the banking authority in a home country.
[2] The host country may impose special limitations on branches of non-domestic banks that are not subject to global supervision by the home country.
[3] Hong Kong applies to branches of non-domestic banks certain requirements, including those relating to liquidity, approval of the chief executive of the branch, and provision of information to the Hong Kong Monetary Authority.
[4] Branches of non-domestic banks in Panama are subject to host counting supervision under Panamanian law, but home country requirements for liquidity, capital adequacy and other conditions apply. Home country supervisors may request information from the Superintendency of Bank only for supervisory purposes.
[5] Member States of the European Union (EU) are listed on the basis of their supervisory practices with respect to non-domestic banks from outside the EU. Within the EU, relationships among bank supervisors are governed by the Second Banking Directive, which establishes a "home country" supervisory system for banks incorporated in a Member State. Under these arrangements, (i) the banking license of a bank from a Member State permits the bank to branch throughout the EU without obtaining approval of the host country, and (ii) the supervisory authority of the Member State where a bank is incorporated (i.e., the home country) has primary responsibility for the operations of the bank throughout the EU. An EU Member State also can apply the home country principle applied to EU banks in whole or in part to banks from non-EU countries if there is reciprocity, close cooperation between the supervisory authorities of both countries, and a high standard of home country supervision. Otherwise, the EU Member State makes its own assessment of banks from non-EU countries and applies capital standards consistent with EU standards. By agreement, these arrangements have been extended throughout the European Economic Area to include, in addition to the 15 EU Member States, Iceland, Lichtenstein and Norway.
[6] Estonia applies the EU's "home country" supervisory system to banks from EU Member States, although it is not itself an EU Member State.
[7] In Japan, the supervision of the capital adequacy of non-domestic banks relies on consolidated supervision by the home country, but Japanese standards are applied to the other aspects of the branches of non-domestic banks.
[8] The Office of the Comptroller of the Currency is the primary regulator for federal branches and agencies and the states are the primary regulator for branches and agencies licensed under their laws. The Federal Reserve has examination authority over the combined U.S. operations of international banks, including their branches and agencies. U.S. branches and agencies of international banks are subject to supervisory standards regarding risk management, asset quality, operational controls and compliance with laws and regulations.

HOST COUNTRY "UMBRELLA" SUPERVISION OF NON-DOMESTIC BANKING ORGANIZATIONS[1]

Host Country Financial Authorities Apply Their Umbrella Supervision To Non-Domestic Banking Organizations	Host Country Financial Authorities Do Not Apply Their Umbrella Supervision To Non-Domestic Banking Organizations	Host Country Financial Authorities Do Not Apply Umbrella Supervision To Domestic or Non-Domestic Banking Organizations
United Kingdom	Australia[2]	Colombia
United States[3]	Austria	Czech Republic
	Bahrain	Finland
	Belgium	France
	Bermuda	Germany
	Canada[4]	Hong Kong
	Cayman Islands	Korea
	Chile	Latvia
	Denmark[5]	Luxembourg
	Estonia[6]	Netherlands
	Ireland	Poland
	Japan	Portugal
	Norway	Romania
	Philippines	Switzerland
	Singapore[7]	Turkey
	South Africa	Uruguay
	Spain	Venezuela
	Sweden	

1 For purposes of this chart, "umbrella supervision" refers to oversight of a non-domestic banking organization's banking and nonbanking activities in a host country as a whole. It does not encompass the oversight of activities of individual nonbank affiliates that may be subject to a host country's separate regulation (e.g., bank subsidiaries, securities firms and insurance companies). The first two columns in this chart report whether a host country that exercises umbrella supervision over domestic institutions also applies such supervision to non-domestic banking organizations.

2 In Australia, umbrella supervision is not undertaken provided that the Australian Prudential Authority is satisfied a non-domestic banking organization is subject to group supervision broadly equivalent to that applied to domestic conglomerate groups which include an authorized deposit-taking institution.

3 International banks with U.S. branches or agencies are treated under U.S. law as bank holding companies, and the safety and soundness of their U.S. operations as a whole are subject to the Federal Reserve Board's oversight. Under the Gramm-Leach-Bliley Act, international banks with U.S. branches and agencies may engage in the expanded nonbank activities permissible for financial holding companies (e.g., securities underwriting and dealing, insurance underwriting and merchant banking) if they meet capital and management standards "comparable" to the "well capitalized" and "well managed" standards applied to the conduct of such activities by domestic financial holding companies. In applying these standards to an international bank, the Board treats the bank as a global entity. Thus, under the Board's regulations, an international bank meets the well capitalized standard if its capital "is comparable to the capital required for a U.S. bank owned by a financial holding company". This standard includes application of a leverage ratio (Tier 1 capital to total assets unadjusted for risk) to the bank regardless of whether the bank's home country capital standards apply any leverage ratio. The bank meets the well managed standard if its management "meets standards comparable to those required of a U.S. bank owned by a financial holding company." [Footnotes are continued on the next page.]

[4] In Canada, the establishment of nonbank affiliates by non-domestic banks is subject to the approval of the Office of the Superintendent of Financial Services (OFSI), but the OFSI does not supervise such affiliates on an ongoing basis.

[5] Although Denmark does not exercise umbrella supervision over non-domestic banking organizations' nonbank affiliates, such affiliates may be subject to the approval and supervision of the Danish Supervisory Authority of Financial Affairs on an individual basis.

[6] In Estonia, formulation of guidelines for host country supervision of nonbank affiliates of non-domestic banks will be considered subsequent to finalization of pending changes to the Law on Credit Institutions.

[7] In Singapore, the establishment of affiliates by non-domestic banking organizations requires approval of the Monetary Authority of Singapore (MAS). MAS may impose prudential requirements in granting this approval.

MARKET RISK CAPITAL REQUIREMENTS

Banks subject to Risk-based capital Requirements for market risk	Nonbank financial institutions (such as securities Or insurance firms) subject to risk-based capital requirements for market risk	Banks permitted to use Internal models to Measure market risk for risk-based capital adequacy requirements
Argentina	Australia (securities and insurance firms)	Australia
Austria	Austria (securities firms)	Austria
Australia	Belgium (securities firms)	Bahrain
Bahrain	Bermuda (securities firms)	Belgium
Belgium	Brazil (securities firms)	Canada
Bermuda	Denmark (securities firms)	Cayman Islands
Brazil	European Union (securities firms)	Colombia
Canada	Finland (securities firms)	Czech Republic
Cayman Islands	France (securities firms)	Estonia[3]
Colombia	Germany (securities firms)	European Union[4]
Czech Republic	Greece (securities firms)	Finland
Denmark	Ireland (securities firms)	France
Estonia	Italy (securities firms)	Germany
European Union	Korea (securities firms)	Hong Kong
Finland	Luxembourg (securities firms)	Indonesia
France	Mexico (securities firms)	Ireland
Germany	Norway (securities firms)	Italy
Greece	Philippines[2]	Japan
Hong Kong	Poland (securities firms)	Latvia[5]
Indonesia	Portugal (securities firms)	Luxembourg
Ireland	Singapore (securities firms; futures brokers)	Netherlands
Israel	South Africa (securities firms)	Norway
Italy	Spain (securities firms)	Pakistan
Japan	Sweden (securities firms)	Poland
Latvia[1]	Switzerland (securities firms)	Singapore
Luxembourg	United Kingdom (securities firms)	South Africa[6]
Mexico	Venezuela (securities firms)	Spain
Netherlands		Sweden
Norway		Switzerland
Peru		United Kingdom
Philippines[2]		United States
Poland		
Portugal		
Singapore		
South Africa		
Spain		
Sweden		
Switzerland		
United Kingdom		
United States		
Venezuela		

See the text of the footnotes on the next page for additional explanatory information.

[1] In Latvia, the captial requirement for fx risk applies from July 1, 2000, while for other market risks it applies from January 1, 2000.

[2] In the Philippines, banks are not formally subject to the risk-based capital requirement for market risk prescribed under the Basel Accord, as this requires an amendment to the General Banking Act (the necessary statutory amendments were recently enacted but have not yet been implemented). However, since September 1993, banks have been required to submit to the Central Bank a quarterly report entitled "Computation of Capital to Risk Assets Ratio in Accordance with the [Basel] Accord." These reporting requirements apply to banks, as well as to investment houses and financing companies with quasi- banking functions.

[3] In Estonia, internal models can be used, provided the resulting capital requirement is <u>not</u> lower than that required under the EU Directives.

[4] EU-based banks will be able to use internal models to the extent permitted by the Basle Committee "Amendment on Capital Requirements for Market Risk" upon implementation of CAD II.

[5] Subject to prior written approval by the Registrar and a prescribed monitoring period.

[6] Use of VAR models is not allowed in Latvia. Delta-plus method for options can be used with the consent of the Bank of Latvia.

PERMISSIBLE ACTIVITIES[1] FOR BANKING ORGANIZATIONS IN VARIOUS FINANCIAL CENTERS

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Argentina	Permitted	Permitted, but only with regard to pension fund affiliates	Limited; based on bank capital and investment	Limited	Permitted but subject to prior approval of authorities
Australia	Permitted	Permitted through subsidiaries or sister companies, subject to controls under the insurance laws	Limited	A bank can make equity investments in non-financial businesses up to an aggregate amount equal to 5% of its Tier 1 capital without prior reference to the Prudential Authority. Individual investments are generally subject to a limit equal to 0.25% of Tier 1 capital.	Shareholdings of more than 15% in a bank need the approval of the Treasurer. The Treasurer has signalled a willingness to consider an association between a bank and a non-financial company where a sound case can be presented. This policy will be applied conservatively.
Austria	Permitted	Permitted through subsidiaries	Permitted	Permitted, but subject to limits based on the bank's capital	Permitted, but subject to notification and prohibition under certain circumstances

[1] With respect to the activities described, the chart indicates which types of financial activities are permitted. The chart is not intended to summarize the complete range of prudential restrictions which may apply to any such activities.
[2] Securities activities include underwriting, dealing and brokering all kinds of securities and all aspects of the mutual fund business.
[3] Insurance activities include underwriting and selling insurance as principal and as agent.
[4] Real estate activities include real estate investment, development and management.
[5] Including investments through holding company structures.

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Bahrain	Permitted, but limited to banks	Selling as agent is permitted	Generally limited to own premises. Management or development on behalf of customers is permitted.	Subject to large exposure limits (15% of capital) and generally limited to holdings of marketable securities	No legal restriction, but subject to "fit and proper" regulations of the Bahrain Monetary Agency
Belgium	Permitted	Permitted through subsidiaries	Generally limited to holding bank premises	Single qualifying holding may not exceed 15% of bank's own funds and such holdings on an aggregate basis may not exceed 45% of own funds	Permitted, but subject to prior approval of authorities
Bermuda	Permitted	Permitted through subsidiaries	Permitted through subsidiaries	Permitted, subject to regulatory consent	Permitted, subject to regulatory vetting of business
Bolivia	Permitted	Permitted through subsidiaries	Not permitted	Not permitted	No legal restriction, but subject to approval of banking authorities
Brazil	Permitted through subsidiaries	Permitted through subsidiaries	Generally limited to holding bank premises	Limited to suppliers to the bank	Permitted

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Canada	Permitted through subsidiaries	Permitted through subsidiaries	Permitted through subsidiaries	Permitted up to 10% interest in industrial firm	Permitted to hold up to 10% interest
Cayman Islands	Permitted	Permitted upon issuance of an insurance license	Permitted	Not restricted by law	Permitted, but subject to consultations with authorities
Chile	Permitted	Insurance brokerage permitted	Not permitted	Not permitted	Permitted up to 10% of a bank's shares, after which the Superintendent's prior approval is required
China	Not permitted	Not permitted	Not permitted	Not permitted	Not permitted
Colombia	Permitted through subsidiaries	Not permitted	Permitted through subsidiaries	Not permitted, except in connection with the resolution of debts previously contracted in good faith	Permitted
Czech Republic	Subject to authorization by the Securities Commission	Selling of insurance policies as an agent is permitted; other activities permitted through independent subsidiaries with the approval of the Ministry of Finance	Permitted	Controlling interests (i.e., in excess of 50%) are prohibited. "Qualified" interests (i.e., in excess of 10% but not controlling) are permitted but may not exceed (i) individually, 15% and (ii) in the aggregate, 60% of the investing bank's capital	Subject to regulatory approval for acquisitions of voting shares equal to or in excess of 10, 20, 33 and 50%

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Denmark	Permitted	Permitted through subsidiaries	Permitted up to 20% of the bank's capital	Permitted with restrictions; permanent controlling holdings in industrial companies are prohibited	Not prohibited, but such investments are generally not made
Egypt	Permitted through subsidiaries	Permitted through subsidiaries	Generally limited to holding bank premises	Limited to 40% of the capital of the company and in the aggregate may not exceed the bank's capital	The consent of the central Bank of Egypt's Board of Directors is a pre-requisite for the ownership of more than 10% of a bank's issued capital; ownership through heritage is exempted
Estonia	Permitted	Permitted through affiliates	Permitted, but as of July 1, 1998 total investments in fixed assets may not exceed 60% of own funds	Permitted, but each shareholding may not exceed 15% of the bank's own funds and such holdings in the aggregate may not exceed 60% of own funds	Permitted

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
European Union[6]	Not applicable; permissibility is subject to home country authorization and limited to host country regulation	Not applicable; permissibility is subject to home country and host country regulation	Not applicable; permissibility is subject to home country and host country regulation	Each 10% or more share-holding may not exceed 15% of the bank's own funds and such shareholdings on an aggregate basis may not exceed 60% of own funds	No general restrictions; does not allow investments of 10% or more if home country supervisor is not satisfied with the suitability of the shareholder
Finland	Permitted	Only selling of insurance policies as an agent is permitted	Permitted to hold real estate and shares in real estate companies up to 13% of the bank's total assets	Permitted, subject to the EU directive on qualified companies	Permitted
France	Permitted	Permitted; usually through subsidiaries	Permitted	Permitted, but limited to 15% of the bank's capital; in the aggregate limited to 60% of the bank's capital	Not prohibited

[6] The Second Banking Directive contains a long list of securities and commercial banking activities that EU "credit institutions" (i.e., entities engaged in deposit-taking and lending) may conduct directly or through branches throughout the EU so long as their home countries authorize the activities. Subsidiaries of credit institutions governed by the law of the same member state may also conduct activities on the list throughout the EU, subject to conditions which include 90% ownership and a guarantee of commitments by the parent credit institutions. Insurance and real estate activities are not on the list and are therefore determined by home country and host country regulations.

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Germany	Permitted	Permitted, but only through insurance subsidiaries	Permitted, but subject to limits based on the bank's capital; unlimited through subsidiaries	Permitted, but limited to 15% of the bank's capital; in the aggregate limited to 60% of the bank's capital	Permitted, subject to regulatory consent based on the suitability of the shareholder
Greece	Underwriting permitted with consent of Bank of Greece; dealing and brokerage permitted through subsidiaries	Permitted to hold shares in insurance companies subject to limits based on the bank's capital and insurance company's capital	Generally permitted	Permitted, subject to the EU Directive on qualified holdings	Permitted, subject to the EU Directive on qualified holdings
Hong Kong	Permitted, subject to limits based on the capital of the bank	Permitted, subject to limits based on the capital of the bank	Permitted, subject to limits based on the capital of the bank	Permitted, subject to limits based on the capital of the bank	Permitted, subject to regulatory consent based on suitability of the shareholder
India	Underwriting permitted; trading activities through subsidiaries	Not permitted	Generally limited to holding bank premises	Limited to 30% of the capital funds of the bank	Permitted up to 30% of the capital and reserve of the investing company subject to approval of RBI of the transfer of 1% or more of the bank's capital
Indonesia	Permitted through subsidiaries	Permitted through subsidiaries	Not permitted	Not permitted	Permitted

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Ireland	Permitted; usually conducted through a subsidiary	Permitted to engage in agency and certain life assurance activities through a subsidiary, which must be separate and independent	Permitted	Acquisition of more than 10% of voting rights of a firm requires Central Bank approval	Permitted, but subject to prior notification to the Central Bank for acquisition of more than 5% of total bank shares
Israel	Permitted; brokerage and investment advice by banks directly, other activities through subsidiaries	Not permitted	Permitted on a limited basis	Permitted on a limited basis	Permitted, but subject to prior approval of the Bank of Israel

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Italy	Permitted	Limited to 10% of own funds for each insurance company and 20% aggregate investment in insurance companies	Generally limited to holding bank premises	Permitted, up to 15% of the bank's capital, subject to approval of the Bank of Italy	Permitted, up to 5% of shares of the bank, subject to the approval of the Bank of Italy
Japan	Permitted through subsidiaries, but not for equity securities for the time being[7]	Permitted through subsidiaries[8]	Generally limited to holding bank premises	Limited to holding 5% interest[9]	Permitted, provided total investment does not exceed investing firm's capital or net assets
Korea	Permitted through affiliates	Permitted through affiliates	Generally limited to holding bank premises and to 60% of bank capital	Subject to prior approval for investments in excess of 15%	Permitted, up to 100% of the bank's capital, but subject to prior approval based on suitability of the shareholder
Latvia	Permitted	Permitted through subsidiaries	Permitted; together with the investments in industrial firms must not be more than full amount of the bank's capital	Permitted, but limited to 15% of bank's capital; in the aggregate limited to 60% of the bank's capital	Subject to regulatory approval for acquisitions of voting shares equal to or in excess of 10, 20, 33 and 50%

[7] Restrictions on the business of securities subsidiaries will be abolished in October 1999. Selling of securities investment trusts (mutual funds) by banks was permitted on December 1, 1997.
[8] Acquisitions of insurance companies by banks is limited to failed insurance companies until October 1, 2000. Selling of insurance policies in connection with housing loans will be permissible commencing April 1, 2001.
[9] Bank holding companies and their subsidiaries are allowed to hold in the aggregate up to 15% of the total shares of non-financial companies.

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Luxembourg	Permitted	Permitted through subsidiaries	Permitted	Permitted, but limited according to EU Directives	Permitted, but majority shareholdings are very restricted
Mexico	Permitted through affiliates	Permitted through affiliates	Generally limited to holding bank premises	Not permitted	Permitted up to 20% of the shares with approval
The Netherlands	Permitted	Permitted through subsidiaries	Permitted	Subject to regulatory approval for voting shares in excess of 10%	Subject to regulatory approval for voting shares in excess of 5%
New Zealand	Permitted; usually conducted through a subsidiary	Permitted; usually through subsidiaries	Permitted; usually through subsidiaries	Permitted	Permitted, but subject to approval of authorities

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Nigeria	Permitted	Permitted through subsidiaries	Mortgage finance permitted through subsidiaries	Limited to certain types of agricultural, industrial and venture capital companies. May not acquire more than 40% of a company's share capital. Each investment limited to 10% of the bank's capital; limited in the aggregate to 20% of capital for commercial banks and 50% of capital for merchant banks	Permitted
Norway	Permitted; the activities need no longer be conducted in separate subsidiaries; mutual fund management permitted through dedicated subsidiaries	Permitted through subsidiaries	Permitted, subject to restrictions based on total assets of the bank	Investments of up to 49% in single companies permitted; only 4% of total bank assets permitted to be invested in shares	Generally, there is a maximum ownership limit of 10% for any single owner of a financial institution; some exemptions, the most important relating to subsidiaries of foreign institutions and domestic financial groups

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Pakistan	Permitted, except for some specifically disallowed securities	Not permitted	Generally limited to holding bank premises	Permitted as a form of financing, subject to the Central Bank's prudential guidelines	Permitted
Panama	Permitted through subsidiaries	Not permitted	Not permitted	Permitted up to 25% of the bank's capital	Permitted
Peru	Permitted; dealing usually conducted through subsidiareis	Not permitted	Generally limited to holding bank premises	Generally not permitted	Permitted, subject to approval of Superintendent of Banks if investment exceeds 15% of bank's capital
Philippines	Permitted; expanded commercial banks may engage in securities activities directly or through a subsidiary; regular commercial banks may engage in securities activities through subsidiaries only	Insurance agency and brokerage permitted for unibanks through subsidiaries	Permitted for unibanks through subsidiaries	Permitted for unibanks with limitations	Permitted with limitations

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Poland	Permitted; dealing in publicly traded securities through subsidiaries	Permitted	Permitted	Permitted up to 25% of the bank's capital	Permitted
Portugal	Permitted; mutual funds only through subsidiaries	Permitted through subsidiaries	Generally limited to holding bank premises	Permitted up to 15% of bank's own funds (but not to exceed 25% of the voting rights of the company) and such investments may not in the aggregate exceed 60% of the bank's own funds	Subject to regulatory approval for acquisitions of voting shares equal to or in excess of 10, 20, 33 and 50%
Romania	Permitted; usually conducted through a subsidiary	Insurance brokerage permitted	Generally limited to holding bank premises	Interests of 20% or less are permitted subject to limits based on the bank’s capital	Acquisitions of 5% or more requires regulatory approval
Russia	Permitted	Not permitted	Not permitted	Permitted, but not more than in one financial-industrial group	Permitted, but acquisition of more than 25% of a bank’s shares requires the Central Bank of Russia’s prior approval

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Singapore	Banks may hold equity participation in stockbrokering firms with MAS approval	Locally incorporated banks may own insurance companies with MAS approval	Limited in the aggregate to 40% of bank's capital (excluding premises used for banking business)	Limited in the aggregate to 40% of the bank's capital	Acquisitions of 5% or more requires regulatory approval
South Africa	Generally permitted, but subject to financial reporting requirements	Banks may not hold more than 49% of a registered insurer	Bank may not hold more than 10% of their total liabilities in fixed assets, loans and advances to certain subsidiaries and investments in, and loans and advances to, certain associates	Banks require prior permission from the Registrar to establish subsidiaries within South Africa or to acquire an interest in companies outside of South Africa	Permission is required from the Registrar for holdings in excess of 15% and from the Minister of Finance for holdings in excess of 49%
Spain	Permitted; banks themselves allowed to become members of the stock exchange; mutual funds managed through separate affiliate	Marketing permitted directly and through subsidiaries	Permitted	Permitted, subject to capital-based limits under EU Directives	Acquisitions of 5% or more require the approval of the Bank of Spain
Sweden	Permitted	Permitted	Generally limited to holding banking premises	Limited	Not prohibited, but such investments are generally not made

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Switzerland	Permitted through specific license as securities dealer	Permitted through subsidiaries	Permitted	Permitted	Not prohibited, but such investments are generally not made
Turkey	Permitted	Permitted to act as agent but not permitted to act as principal	Not permitted unless specifically authorized by bank's charter	Limited to 15% of the bank's own funds and in the aggregate limited to 60% of the bank's own funds	Not prohibited
United Kingdom	Permitted; usually conducted through subsidiaries	Permitted through subsidiaries	Permitted	Permitted, subject to supervisory consultations	No statutory prohibition
United States	Permitted, but underwriting and dealing in corporate securities must be done through (1) a nonbank subsidiary of a bank holding company (subject to limits on revenue), (2) a nonbank subsidiary of a financial holding company (no revenue limits) or (3) a financial subsidiary of a national bank (no revenue limits)	Insurance underwriting and sales are permissible for nonbank subsidiaries of financial holding companies. National banks and their subsidiaries are generally restricted to agency sales activities.	Generally limited to holding bank premises	Permitted to hold up to 5% of voting shares through a BHC (bank holding company), but a BHC that is designated as a financial holding company and has a securities affiliate may exercise merchant banking powers to make controlling investments, subject to certain regulatory restrictions	Permitted to make noncontrolling investments up to 25% of the voting shares

Country	Securities[2]	Insurance[3]	Real Estate[4]	Bank Investments in Industrial Firms[5]	Industrial Firm Investments in Banks
Uruguay	Underwriting and brokering permitted; dealing limited to public debt; mutual funds permitted with Central Bank approval	Permitted through affiliates	Generally limited to holding bank premises	Not permitted	Permitted; subject to Central Bank approval
Venezuela	Permitted without restriction for universal banks; other types of banks limited to 20% of capital	Permitted through subsidiaries, subject to controls under the insurance laws	Limited	Limited to 20% of capital	Acquisitions of more than 10% of a bank's voting stock requires approval from the Superintendent

ARGENTINA

During the period under review, certain changes were made to capital adequacy requirements relating to the maturities of federal government bonds, loans to the non-financial public sector and loans guaranteed by the federal government. In addition, revisions were made to the rules for including loan loss provisions in tier 2 capital.

Financial institutions are prohibited from owning more than 12.5 percent of industrial, agricultural, commercial or other kinds of non-financial companies unless specifically approved by the Central Bank. Such approvals typically involve companies whose activities are considered to be complementary to a financial activity. In March 2000, the list of activities considered as services complementary to financial services was expanded. In some instances, the approval of the Superintendent of Financial Institutions is also now required to acquire more than 12.5 percent of such a company.

Beginning August 1, 1999, financial institutions are prohibited from owning shares in mutual funds, except (i) those funds comprised of instruments that satisfy prescribed minimum liquidity requirements and, (ii) new funds for which the financial institution acts as manager, depository, distributor or promoter.

Those financial entities that are branches or subsidiaries of foreign banks, whose functioning in Argentina is subject to the previous authorization of the Central Bank, must comply with the same minimum capital requirements as Argentine financial entities.

Such requirements are independent of those established by the authorities of the foreign bank’s home country, and compliance is based solely on the accountable net worth of the branch or subsidiary functioning in Argentina.

Non-domestic banking organizations that operate branches in Argentina are not subject to any type of asset pledge requirement.

AUSTRALIA

Regulatory Organization

The final stage in setting up the current regulatory framework, which first came into existence in July 1998, was completed in 1999.

On July 1, 1999, the responsibility for supervising building societies, credit unions and friendly societies was formally transferred from the States to the Commonwealth. The Australian Prudential Regulation Authority (APRA) took on the responsibility for the prudential supervision of these entities while the Australian Securities and Investments Commission (ASIC) became responsible for market integrity and consumer protection across the financial system.

Developments Regarding the Regulation and Supervision of Banks

At the time of transfer, building societies and credit unions remain under the prudential rules applicable under the previous state supervisory regime while banks are subject to a different set of prudential statements. It was noted at the time that, after a transition period, APRA will replace the two sets of prudential rules with a single set of prudential standards under the Banking Act 1959 to apply to all deposit-taking institutions (ADIs).

The process of harmonizing prudential requirements for ADIs started in late 1999. Since then a series of draft Prudential Standards (covering capital adequacy, liquidity, credit quality, large exposures, equity associations and audit arrangements) have been issued for public comment. Prudential requirements of the previous regimes are largely preserved in the draft harmonized standards, with changes limited to areas where inconsistencies need to be addressed. APRA expects the final set of harmonized standards for ADIs to be in place in mid-2000.

In September 1999, APRA amended its capital adequacy guidelines to permit banks, in certain circumstances, to recognise bilateral close-out netting agreements for capital adequacy purposes. The changes are consistent in all substantial aspects with the requirements on bilateral netting set out by the Basel Committee on Banking Supervision in April 1995 and subsequently implemented by G-10 and a number of other countries.

In March 2000, APRA issued its submission to the Basel Committee on Banking Supervision on the Committee's proposed changes to the Capital Accord. The submission is available on APRA's website (www.apra.gov.au).

In April 2000, APRA issued a policy framework for the prudential supervision of conglomerate groups containing ADIs. The policy framework expands the range of organizational structures which conglomerates may adopt, particularly in allowing ownership of ADIs by non-operating holding companies. The framework also liberalizes the range of activities that can be carried out within a conglomerate group containing an ADI. The policy framework will be implemented through changes to Prudential Standards over the next twelve months or so.

Also in April 2000, APRA released Guidance Notes on the capital adequacy treatment of credit derivatives transacted by ADIs. The Guidance Notes followed extensive industry consultation over the previous twelve months. The Guidance Notes apply only to the most commonly traded forms of credit derivatives.

Regulation of Friendly Societies

In July 1999, amendments were made to the Life Insurance Act 1995 to provide for the prudential supervision of benefit fund friendly societies by APRA. At the same time, a set of transitional actuarial standards, modelled on the pre-existing regime for these societies, came into effect. Work is now underway to produce a set of harmonized actuarial standards for all life companies and friendly societies.

Regulatory Reform of General Insurers

In April 2000, APRA released for comment a Policy Discussion Paper on proposed reforms to the prudential supervisory requirements for general insurers. This Paper, which is available from APRA's website, follows on from three discussion papers issued by APRA in September 1999. It sets out a refined version – though still in broad terms – of the reform proposals in the September papers, taking into account feedback from industry on those papers.

CLERP

The Australian Government continues to implement its Corporate Law Economic Reform Program (CLERP). CLERP Act 1999, which amended important parts of the Corporations Law, became effective in March 2000. The amendments incorporate major law reform in relation to:

- accounting standards;
- fundraising;
- directors' duties and corporate governance; and
- takeovers.

In February 2000, the Minister for Financial Services and Regulation released the Financial Services Reform Bill for public comment. The draft legislation will give effect to the proposals contained in an earlier consultation paper, and provides for an integrated licensing and regulation regime for financial service providers, financial markets and clearing and settlement facilities, as well as improved protection for retail investors. Key aspects of the draft legislation are:

- uniform regulation for all financial products;
- a single licensing framework for financial services providers;
- minimum standards of skills, competencies and conduct for financial services providers dealing with retail clients;
- uniform disclosure obligation for all financial products provided to retail clients; and
- flexibility for the authorization of market operators and clearing and settlement facilities.

The draft legislation is available from the Commonwealth Treasury's website (www.treasury.gov.au). The new legislation may commence as early as January 1, 2001 and will be administered by the Australian Securities and Investments Commission (ASIC) when it is enacted.

Developments Relating to Payment Systems, Electronic Commerce and Banking

In September 1999, the Payments System Board of the Reserve Bank and the Australian Competition and Consumer Commission announced they would undertake a joint study into interchange fees for debit and credit cards, and membership criteria for credit cards. The objectives of the joint study include assessing whether current interchange fees are encouraging efficient provision of debit and credit card services and obtaining information on current restrictions on credit card scheme membership.

The Commonwealth Government passed the Electronic Transactions Bill in November 1999. This legislation allows electronic communications and digital signatures to fulfil the existing legal requirements for writing, signatures, document production and retention of documents.

In November 1999, the Payments System Board issued further approvals under the Payment Systems and Netting Act 1998 designed to enhance the legal underpinnings of the Australian payments system. These approvals extend the protection of the Act to the multilateral netting performed by Austraclear and SWIFT-PDS in the event of a disruption to normal real time gross settlement (RTGS) operations.

In January 2000, ASIC released a second draft proposal to expand the existing Electronic Funds Transfer Code of Conduct (a voluntary code that deals with transactions initiated using a card and a PIN) to cover all forms of consumer technologies, including stored-value cards and other new electronic payment products. ASIC plans to have the expanded code finalized by mid-2000.

Experience Over the Year 2000 Date Change

The primary focus of APRA and the Reserve Bank of Australia (RBA) over the latter months of 1999 was to maintain public confidence. A joint APRA/RBA Communications Center was established in order to monitor developments and manage any problems arising over the date-change period.

In the event, the period leading up to the date change went relatively smoothly. There was very little evidence of customer concern about the Year 2000 – for example, large cash withdrawals, requests for bank checks or an increase in the number of requests for account statements. A very small number of institutions experienced minor date-related issues resulting from the inability of equipment and programs to correctly recognize the Year 2000, but these were fixed quickly and without any noticeable impact on customers.

Over the date-change period, most institutions set up communication / command centers to monitor and respond to any date-related issues as they arose. However, no major issues arose over this period. In fact, most institutions wound down these communications centers in the first week of January 2000 as it was considered unnecessary to keep them operating given the smooth transition process. As expected, the transition over the Leap Year period also went smoothly, with no problems reported.

Regulation and Supervision of Non-Domestic Banking Organizations

A non-domestic banking organization is not subject to an independent assessment by APRA prior to expanding its non-banking operations in Australia unless such activities are to be owned by a locally incorporated ADI subsidiary or by a locally incorporated Non-Operating

Holding Company. (In these instances approval by APRA may be required). APRA would expect a non-domestic banking organization to keep it informed of any new proposed activities. Should APRA form a view that such activities might adversely affect the safety and soundness of a related ADI in Australia it may review with the non-domestic banking organization the continued operations of the ADI in Australia.

Any acquisitions by non-domestic banking organizations of non-banking enterprises in Australia, depending on the type of enterprise, may require approval of the Treasurer under the Foreign Acquisitions and Takeovers Act.

Where an acquisition by a non-domestic banking organization, however, involves an Australian insurance company the Treasurer's approval under the Financial Sector (Shareholdings) Act would also be required. A non-domestic banking organization wishing to establish insurance or securities dealing operations in Australia would also require an authority from APRA (for insurance) or the Australian Securities and Investments Commission (for securities dealing). Any decision to grant an authority would involve an assessment of the standing of a non-domestic banking organization, including its capital adequacy.

APRA does not apply any local capital adequacy requirements to non-domestic banking organizations (with branch operations). APRA, however, requires such organizations to be subject to acceptable standards of prudential oversight, including compliance with Basel Core Principles. This would incorporate application of minimum capital adequacy requirements in line with the Basel Capital Accord. APRA would wish to be satisfied that such requirements are broadly consistent with the minimum capital requirements applied to domestic banking organisations. APRA does not impose a leverage test.

APRA does not impose any asset pledge requirement on non-domestic banking operations which operate through a branch in Australia.

AUSTRIA

Significant Bank Regulatory Developments

The Austrian Banking Law was amended to be in line with the requirements (and the timetable) of the amended Capital Adequacy Directive (CAD II) of the European Union.

Considerable effort was dedicated to the response of the Austrian banking industry to the EU Consultative Paper on Regulatory Capital Requirements. In principle, the assessment of the system proposed in the Consultative Paper was favorable, and support should be given to ensure that external ratings and the internal assessment of risks are recognized both simultaneously and as being of equal value for supervisory purposes. Although the more refined capturing and setting of capital charges for credit risks through the use of external ratings was welcomed in principle, the response pointed out that in Austria (as elsewhere in Europe) the external ratings that would be needed to implement such a system are not adequately available at the present time and will remain inadequately available in the foreseeable future. The response welcomed the proposal that institutions' internal ratings also should be recognized as a basis for assessment when setting capital charges. However, it was noted that the recognition of internal credit risk models must first be preceded by the definition of suitable criteria for the supervisory recognition of institutions' internal rating systems. Further, the prerequisites for supervisory recognition of internal ratings systems must be such that they can be satisfied by credit institutions on a broad basis.

Supervision of Non-Domestic Banking Organizations

Austria is a member of the European Union. Within the EU, relationships among bank supervisors are governed by the Second Banking Directive, which establishes a "home country" supervisory system for banks incorporated in a member state ("single license"). Under these arrangements, the banking license from a bank from a member state permits the bank to branch throughout the EU.

A license from the Federal Minister of Finance (Austrian Banking Supervision Authority) is required to conduct a banking business (including a securities business). The license application must include the following information and documentation: (1) corporate seal and legal form; (2) articles of association; (3) a business plan describing the type of business to be conducted, as well as its organization and the procedures for its internal control, and setting forth a budget calculation for the first three business years; (4) the amount of initial capital which is at the free disposal and unlimited disposal of the managers in Austria; (5) the identity and amount of the contribution of those owners that hold a qualifying participation in the credit institution, and information on the group, if those owners are members of the group; and (6) the names of the designated managers and their qualifications to operate the business.

If an application to establish a branch in Austria is submitted by a foreign credit institution (i.e., one headquartered outside of the European Economic Area) then, in addition to the information mentioned above in numbered items 1, 2, 3, 5, and 6, the following information and documentation must be submitted: (1) the three latest annual financial statements of the company; (2) the business conducted by the foreign company, as well as the locations at which they are conducted; (3) the amount of initial endowment in euros which is at the free and unlimited disposal of the managers in Austria (the minimum amount is 5 million euros); (4) the decision-making authority of the branch office management as well as the authorities of the head office whose consent must be obtained for specific internal decisions; and (5) a written declaration by the appropriate home country supervisory authority stating that it has no objections to the establishment of the branch office of the company in Austria.

BAHRAIN

Background

The regulation and supervision of banks by the Bahrain Monetary Agency (BMA) incorporates a number of different but interlocking aspects:

- A focus on corporate governance, asset quality and the adequacy of provisions (specific and general). Assessment is also made with regard to concentration by region, country and economic sector. Moreover, capital adequacy, large exposures, and other key prudential data are monitored on a quarterly basis.

- The BMA has fully subscribed to the internationally accepted principles of the Basel Accord with respect to capital adequacy, including the 1996 Amendment to the Basel Capital Accord to incorporate market risks. Locally incorporated banks are required to maintain a capital ratio of at least 12 percent.

- A predictive form of bank supervision that assists the BMA to identify problems at an early stage and initiate timely preventive action to avoid significant harm. This entails on-site inspection focusing on an evaluation of the quality of management, the bank's ability to control risk exposure, and the quality of the bank's system of internal controls.

- Off-site monitoring based on an analysis of the bank's report and statements submitted to the BMA. In this connection, it should be noted that locally-incorporated banks are required to follow international accounting standards (IAS), while the branches of foreign banks in Bahrain are required to adopt Generally Accepted Accounting Principles (GAAP) or to comply with the requirements of IAS (the majority of foreign bank branches follow IAS). In addition, the off-balance sheet operations of the banks have been brought under prudential regulation and are limited to twice the capital base.

- Since November 1993, a Deposit Protection Scheme has been in operation under which the deposits of both residents and non-residents with the Bahrain offices of full commercial banks in both local and foreign currencies are protected up to a designated amount in the event of the insolvency of such a bank. The domestic loan market has been deregulated since 1994. Bahraini Dinar interest rates are set by the banks according to prevailing market rates and conditions.

Regulatory Developments

New prudential reporting forms and requirements were introduced by the BMA in June 1999 following the adoption of the market risk amendments to the Basel Capital Accord at the start of 1999. Banks now submit all supervisory data electronically. Islamic banks are required to produce their accounts from 1999 onwards in accordance with the Islamic Accounting Standards adopted by the Accounting & Auditing Organisation for Islamic Financial Institutions. New prudential reporting forms are currently being developed for Islamic banks along with new large exposures regulations which will explicitly cover off balance sheet accounts.

As part of its efforts to promote transparency, the BMA has introduced a quarterly public disclosure requirement of profit and loss and balance sheet information by locally incorporated banks in accordance with International Accounting Standards and greater disclosure of risk information in the annual accounts along the lines recommended by the Basel Committee. Foreign full commercial banks are also required to publish semi-annual financial data for their Bahrain operations. As an additional measure to combat money laundering, all financial institutions are required to report any large or unusual transactions to the BMA.

New guidelines for advertising and public announcements for collective investment schemes and new regulations for margin trading were implemented in 1999. The BMA was pleased to note that all financial institutions had met its deadlines for Year 2000 preparations and no business interruptions were reported in 1999 or 2000 as a result of Y2K matters.

Concerning internal controls, with effect from 1999 all banks must have dedicated compliance personnel and all external audit partners are required to be changed on a five-year cycle. External auditors are also required to review quarterly prudential returns with effect from June 2000.

Financial Institutions Operating in Bahrain

As of April 30, 2000, there were 171 banks and other licensed financial institutions operating in Bahrain. At the end of 1999, there were 523 collective investment schemes operated by 40 Bahrain-based banks.

Access to Payments Systems and Lender of Last Resort

The BMA operates a twice daily clearinghouse for checks drawn on full commercial banks. This system is fully automated. The BMA is a member of SWIFT and also operates a tested telex system for transfers between full commercial banks. The BMA can, in appropriate circumstances, act as lender of last resort to the banking system. Whether it does so depends upon the circumstances of each particular case.

Currently, only full commercial banks have access to the BMA's clearinghouse and payments system. A “full commercial bank” is an entity that carries on both retail and wholesale banking activities in Bahraini Dinars and other currencies with residents and nonresidents of Bahrain and which is licensed by the Agency to do so in/from Bahrain.

Ordinarily, each commercial bank is required to ensure that its clearing account with the BMA is always in credit. However, the BMA can exercise its discretion to cover a bank's deficit for a very short period and, if it does so, it charges an interest penalty.

There are no specific regulations in Bahrain concerning the issuance of third party instruments. However, because such instruments are likely to involve an extension of credit, the BMA would need to determine whether the issuing entities would be subject to licensing and/or supervision by the BMA. Currently, only banks and other financial institutions licensed by the BMA issue third-party instruments.

The BMA continues to review the involvement of all relevant parties in the banking and financial sector in the payments system. The ATM shared network/switch system, first introduced and managed by the Agency, is now owned and managed by a private company collectively owned by the participating banks. The ATM network in Bahrain is now fully linked with Kuwait, Qatar and UAE Switch networks. The linkage process with Saudi Arabia and Oman is underway.

Supervision of Non-Domestic Banking Organizations

Bahrain generally relies on global supervision by the home country. However, branches of full commercial banks are subject to Bahrain liquidity requirements and must publicly disclose balance sheet and profitability information, as well as provide quarterly provisioning and other data to the BMA. All senior branch staff are subject to BMA fitness requirements.

A non-domestic bank may expand its non-banking activities without reference to the BMA. Foreign branches are not required to maintain special deposits with the BMA. However they are subject to the same liquidity requirements as their locally incorporated counterparts.

BELGIUM

Supervisory Developments

The cooperation protocol between the Banking and Finance Commission (CBF), the control authority of banks and securities firms, and the Office de Contrôle de Assurances (OCA), the authority of insurance companies, has been updated, although details have not been released.

Year 2000 Date Change

No significant problems were experienced in the banking industry in connection with the Year 2000 date change. Banks prepared intensively for the event, and the Banking and Finance Commission closely supervised their preparations. In addition, there was extensive cooperative efforts at both the national level (through the Belgian Bankers' Association) and internationally. The banks also benefited from the experience acquired in connection with their preparations for implementation of the euro.

Bank branches and interbank settlement systems were closed on Friday, December 31, 1999. Branches were also closed on Monday, January 3, 2000, although the settlement systems were open. Cash dispensers and payment terminals continued to function properly throughout the changeover. Coordination during the actual transition period was facilitated through "command centers" established for this purpose.

Banks' Y2K efforts have yielded important benefits apart from successfully negotiating the transition to the new millenium. These include enhancement of IT capabilities, a better understanding of their systems and how they operate and improvement in business continuity contingency planning.

Developments Regarding Securities Products and Markets

The CBF for the first time has approved prospectus disclosure requirements for the issuance of warrants and reverse convertibles (bonds linked to put options).

Market Developments

During the period under review, the Belgian Government initiated the privatization of Crédit Professionnel. The Federal Participation Office, which held 74 percent of the shares of Crédit Professionnel, has sold 51.4 percent of these shares to the French Crédit Mutuel du Nord (CMN). The other shares of Crédit Professionnel held by the Federal Participation Office will be sold to CMN in January 2003. The remaining 26 percent of the shares of Crédit Professionnel are held by Crédit Professionnel's savings institutions.

In January 2000, Ippa Bank and Anhyp, which were jointly controlled by the AXA group, merged to create AXA Bank.

Establishment of Euronext

In March 2000, the Brussels Exchanges (BXS), which resulted from the merger of the Brussels Stock Exchange, the Belgian Options and Futures Exchange and the Belgian securities depository (CIK), announced its merger with the Paris and Amsterdam stock exchanges into a new exchange named "Euronext". It is anticipated that this merger will be take place by September 2000 and that the new exchange will be operations at the beginning of 2001. Consideration is being given to a public listing of the exchange.

Payment Systems Developments

The EU Directive on Cross-Border Money Transfers (97/5/EC) has been enacted into Belgian law by the Law of January 9, 2000.

Supervision of Non-Domestic Banking Organizations

Non-domestic banking organizations operating in Belgium are supervised on a global basis by their appropriate home country authorities, with the CBF monitoring them through receipt of their annual consolidated and non-consolidated financial statements and discussions with the home country.

Separately incorporated banks established in Belgium are subject to Belgian capital standards regardless of whether they are domestic or foreign-owned. With regard to banks headquartered outside the EU that operate branches in Belgium, these standards do not apply if their home country applies standards that are at least equivalent to Belgian standards and the bank's capital can be used without restriction in order to cover losses of the Belgian branch.

The branches of non-domestic banking organizations are not subject to any type of asset pledge requirement.

BERMUDA

Legislative Developments

The Bermuda Monetary Authority (BMA) Amendment Act 1999 received Royal Assent on December 22, 1999 with a commencement date of January 1, 2000. The Act amends a number of provisions of the Bermuda Monetary Authority Act 1969 with a view, in particular, to enhancing the effectiveness of the BMA's regulatory powers and strengthening its operational independence.

The Proceeds of Crime Amendment Act 1999 also received the Royal Assent on September 23, 1999. The changes reflected a need to follow international best practice by extending the scope of the legislation to cover the proceeds of all indictable offences including criminal tax evasion.

The Banks and Deposit Companies Act 1999 introduces a general prohibition on the carrying on of deposit-taking business in or from within Bermuda unless a person is licensed or exempt. The Act received Royal Assent on September 23, 1999 and came into operation on January 1, 2000. It seeks to give full effect to the Core Principles for Effective Banking Supervision issued by the Basle Committee on Banking Supervision; and repeals the Banks Act 1969 and Deposit Companies Act 1974. The Act charges the BMA with responsibility for licensing and supervising deposit-taking institutions. Under the provisions of the Act, a person carries on a deposit-taking business if:

(a) in the course of the business, the person lends money received by way of deposit to others; or
(b) the person finances any other activity of the business wholly or to any material extent, out of the capital of, or the interest on money received by way of deposit.

Only companies incorporated in Bermuda are eligible for a license under the Act. The licensing of branches of foreign banks is not permitted. The Act provides for the issue of two types of license: (a) a banking licence, and (b) a deposit company license. A <u>banking license</u> requires the institution to provide the following minimum services to the public in Bermuda –

(i) current accounts in Bermuda dollars on terms which require repayment on demand;
(ii) the payment and collection of checks, draft and orders;
(iii) savings, deposit or other similar accounts in Bermuda dollars;
(iv) overdraft and other loan facilities in Bermuda dollars;
(v) either directly or indirectly, loans in Bermuda dollars secured on the mortgage of real property in Bermuda;
(vi) foreign exchange services; and
(vii) either directly or indirectly, credit card or debit card facilities.

A <u>deposit company license</u> does not authorize the institution to accept deposits of money on current account or otherwise on terms which require repayment on demand but does require the institution to provide the following minimum services to the public in Bermuda:

(i) savings, deposit or similar other accounts in Bermuda dollars on terms which require repayment on notice; and
(ii) loans in Bermuda dollars secured on the mortgage of real property in Bermuda whereby not less than the prescribed minimum percentage of total assets (currently 60%) of the institution shall at all times be invested in loans secured to the full amount of the outstanding balance owed to the institution under such mortgages.

A bank must at the time of licensing have initial net assets amounting to not less than ten million Bermuda dollars (or an amount of equal value denominated wholly or partly in another unit of account). A deposit company must have initial net assets of not less than one million Bermuda dollars or the equivalent. The BMA may not grant a license unless it is satisfied that the minimum criteria in the Second Schedule of the Act are fulfilled and unless the Minister of Finance has advised the BMA that he is satisfied that the grant of a license is in accordance with the economic and financial policy of the government.

In connection with the Banks and Deposit Companies Act, the BMA has published a Statement of Principles and a number of policy and guidance papers setting out its regulatory requirements and approach, including:

- The Measurement of Capital;
- The BMA's Approach to Consolidated Supervision;
- The Measurement and Monitoring of Liquidity;
- Implementation of Provisions for the Reporting & Control of Large Exposures; and
- The BMA's Relationship with Auditors and Reporting Accountants of Banks and Deposit Companies (draft paper for consultation).

These papers may be accessed and downloaded from the BMA website (www.bma.bm).

The Investment Business Act 1998 and related Regulations and Orders came into effect on January 1, 2000. It provides that no person shall carry on, or purport to carry on, an investment business in or from within Bermuda unless that person holds a licence granted under the Act by the BMA or is exempted from holding a licence. Any person who contravenes this provision is guilty of an offence and is liable to a fine, to imprisonment, or to both. The BMA website (see above) gives details of the various exemptions and exclusions.

Applications for licenses must be made to the BMA. Persons conducting investment business prior to the commencement of the Act need to be licensed by June 30, 2000, or else notify the BMA that they are exempt. Persons who qualify for exemption must provide the BMA with a written declaration of the grounds under which they are exempt.

The definition of investment business in the Act is broad and includes dealing or arranging deals in securities, managing or offering securities belonging to another person and the giving or offering of investment advice on securities.

The Electronic Transactions Act 1999 received the Royal Assent on August 5, 1999. The Act creates a legal framework for e-commerce in Bermuda. It makes provision for legal recognition of electronic records and contracts and for the development of codes of conduct and appointment of standards relating to e-commerce.

Year 2000 Date Change

The BMA maintained under careful review the preparedness of local financial institutions for the millennium date change. It also liaised closely with central banks and regulatory authorities in other countries in order to ensure that adequate contingency plans were in place. In the event, the transition to the year 2000 went smoothly and no disruption occurred, reflecting the exhaustive preparations which had been made.

Regulation and Supervision of Non-Domestic Banking Organizations Operating in Bermuda

There is no provision for the licensing in Bermuda of branches of non-domestic banks. Only locally-incorporated entities are eligible for banking licenses.

The BMA always checks with a home supervisory authority before approving local non-banking subsidiaries in Bermuda in order to ensure that they have no difficulty with the proposal and are satisfied as to their ability to conduct consolidated banking supervision. The BMA would not, however, seek to apply capital adequacy monitoring to the home country parent organization in such cases.

BRAZIL

Rules for Classifying Credit Transactions.

Rules issued by the Central Bank of Brazil regarding risk classifications of credit transactions became effective in March 2000. The rules prescribe provisioning requirements for each of nine classification categories. The rules further provide that loans 60 days past due may no longer be held on an accrual basis. In addition, banks must factor into their provisioning policies their borrowers' credit history (i.e., performance on loans with other credit institutions and ability to service loans in the future).

Banks must specify the criteria they apply in making provisions, maintain records of their provisions and make such information available to the supervisory authority upon request.

The Central Bank has established a Risk Center to monitor the provisions made by banks. It is intended that banks' provisions will be assessed against borrowers' credit ratings and will be asked to explain any significant disparities found between their own and the market's assessment of a borrower's creditworthiness.

National Payments System

The Central Bank of Brazil has been involved in a project to identify the four major sources of movement in banks' Banking Reserve accounts – i.e., clearance and settlement of checks and other instruments, foreign exchange transactions, purchase and sale of government and private securities ("Cetip" and "Selic") and Stock Exchange trading. This project has resulted in the Brazilian Government's enactment of Provisional Measure 2008 of December 14, 1999, which establishes the legal framework for restructuring the Brazilian payments system.

Specifically, the Provisional Measure provides for the creation of clearing houses to function as intermediaries in the payments system and, through the application of operating limits and collateral deposits, take over from the Central Bank much of the default risk in the payments system. It is anticipated that this revised system will be operational by February 2001.

New "Lei das Sociedades Anônimas" (Law of Joint Stock Companies)

The Economics, Industry and Commerce Committee of the House of Representatives has started to evaluate the new *Lei das Sociedades Anônimas*, which has as one of its principal aims the development of conditions enabling the capital market to become one of the major tools for the funding of the country's economic development.

The project focuses in particular on controlling equity holders, minority holders and the role of the Comissão de Valores Mobiliários ("CVM", the Brazilian equivalent of the U.S. Securities and Exchange Commission). The key aspects of the program are as follows:

- Whenever the volume of outstanding shares of a company is less than 20 percent of its capital stock, the company would be required to conduct an offering to increase its public ownership or offer to reacquire its shares from the public. With respect to shares of common stock, minority shareholders would have to be offered treatment equal to that offered to a controlling shareholder, except in connection with the privatization of government-controlled companies.

- In connection with the sale of its interests in a company, a controlling shareholder would be required either to ensure payment of a fixed (4 percent) dividend to preferred shareholders, or, at the option of the controlling shareholder, extend the premium on the sale of the controlling equity to the preferred shareholders.

- Minority shareholders that control, individually or in the aggregate, at least 15 percent of a company's capital stock would be entitled to representation on the company's Board of Directors or Audit Committee.

- Minority shareholders would be given redemption rights permitting them to redeem their shares for a proportional amount of the company's net worth upon a major change in the structure of the company.

- The CVM would be restructured to give it more autonomy in the market.

Correspondents in the Country

Resolution 2707 issued by the Central Bank of Brazil on March 30, 2000, grants to multiple banks with commercial portfolios, to commercial banks and to the "Caixa Econômica Federal" (Federal Savings Bank) the right to contract with companies to perform the duties of correspondents in Brazil.

Year 2000 Date Change

Brazilian banks devoted considerable time and resources to prepare for the Year 2000 date change. Their focus during 1999 was the testing and validation of computer systems to confirm their Y2K readiness. These efforts proved successful as no significant problems were experienced in Brazil in connection with the Year 2000 date change.

CANADA

Recently, significant changes have been proposed in the financial system in Canada. Almost twelve months after the federal government released its "White Paper" on the future of the financial services industry, it tabled legislation (Bill C-38) to implement the proposals outlined in that White Paper. Previously, legislation had come into force that allows foreign banks to establish "full service" or "lending" branches in Canada. Furthermore, in late June 2000 legislation was passed to introduce additional anti-money laundering measures.

Financial Services Sector Reform

On June 13, 2000 the Canadian government introduced into parliament Bill C-38. The Bill, which is the culmination of a review process that began in 1996, is highly technical and more than 800 pages in length.

For the first time, the proposed legislation will permit financial institutions operating in Canada to establish non-operating "holding companies" that would face a reduced regulatory burden. Essentially, using a holding company structure, federally regulated financial institutions will be permitted to move certain activities that are currently conducted in-house or through a subsidiary, to a less regulated affiliate of the holding company. Some activities (e.g., retail deposit-taking) would still have to be offered through the regulated bank.

Bill C-38 will also make changes to the ownership structure, allow a greater range of investments for financial institutions, make changes to the ownership rules for banks, and introduce a number of consumer protection initiatives. Changes will also be made to the entry regime for foreign banks so that it is consistent with the domestic policy framework in areas such as permitted investments and business powers. The key principles underpinning the proposed foreign bank entry regime are to provide greater flexibility for foreign banks wishing to operate in Canada and streamline regulatory approvals.

Holding Companies

Bill C-38 will allow banks and the demutualized life insurance companies to re-organize themselves as subsidiaries of financial holding companies. The holding companies will be subject to the new "widely held rule" (see below), but will not carry on any active businesses themselves. Instead, they will raise capital, provide management and other services to their subsidiaries and other permitted investments, and generally manage the financial services group.

Ownership Structure

The new ownership proposals will permit all banks, with appropriate Ministerial approval, to have more concentrated ownership than is presently permitted. If Bill C-38 comes into force, there will be no restriction on the ownership of any bank, insurance or trust company which has equity of less than C$1 billion. Federal financial institutions which have equity of between C$1 billion and C$5 billion will be required to have at least 35 percent of their voting shares widely held and publicly traded. As a result, a commercial company that meets the "fit and proper" test would be able to wholly own a bank with less than C$1 billion in equity, or essentially control a bank with equity of less than C$5 billion.

Banks and demutualized life insurance companies with an equity in excess of C$5 billion will be required to be "widely held," but under a new definition of that term. Under Bill C-38, a single shareholder that was considered by the Finance Minister to be "fit and proper" will be permitted to hold up to 20 percent of any class of voting shares, and 30 percent of any class of non-voting shares. This person is described in the legislation as a "major shareholder."

Permitted Investments of Federal Financial Institutions

As a general rule, any activity carried out by a financial institution would be permitted by Bill C-38 to be carried out through a subsidiary of the financial institution, or a subsidiary or affiliate of its holding company. The intention is to provide federally regulated financial institutions with greater choice and flexibility in the way they structure their operations. In addition, amendments to the business power provisions of the existing federal financial institutions legislation will add to the range of powers that financial institutions may exercise by expanding their data processing and e-commerce businesses, both within and outside Canada.

Foreign Bank Entry

Bill C-38 revises the current *Bank Act* provisions relating to the entry into the Canadian marketplace of foreign banks. The new rules, while making few substantive changes to the existing structure, are very complex.

Generally, Bill C-38 distinguishes between "real" foreign banks and "near" foreign banks. This distinction recognizes, that due to the extremely broad definition of the term "foreign bank" in the *Bank Act* there are many foreign entities that while caught by the definition do not predominantly offer financial services, either in Canada or their home market. While these "near" foreign banks will continue to be defined as "foreign banks" in Bill C-38, provisions in the proposed legislation will essentially allow them to be unregulated unless they wish to establish a regulated financial institution such as a bank.

"Near" foreign banks will be permitted to carry on financial services activities in Canada through unregulated entities unless they decide to carry on an insurance business in Canada or core banking activities (effectively, deposit-taking business). A "real" foreign bank will be permitted to conduct financial services activities in Canada under a legislative regime that will mean that they are treated the same as the domestic banks. Any existing corporate structures of foreign banks in Canada that do not comply with the new rules under Bill C-38 will be grandfathered.

As a result of the changes proposed in Bill C-38, "real" foreign banks offering financial services in Canada will be given greater flexibility and will be able to offer those services through one or more Canadian subsidiary banks, branches of the parent bank, or financial services such as securities activities and trust business through separate affiliates.

Consumer Protection Measures

Bill C-38 contains a number of provisions that are intended to provide greater protection to consumers of financial services. Among these measures are the following:

Financial Consumer Agency of Canada

Bill C-38 will establish the Financial Consumer Agency of Canada (FCAC) to enforce the consumer oriented provisions in the various federal financial institutions statutes, monitor the financial industry's self-regulatory initiatives which are designed to protect the interests of consumers and small business, promote consumer awareness, and respond to general consumer inquiries.

Canadian Financial Services Ombudsman

A new Canadian Financial Services Ombudsman (CFSO) will be established to handle the complaints of consumers and small businesses with respect to their business relationship with financial institutions. The CFSO will operate independently of financial institutions and the federal government. Banks will be required to join the CFSO, while other federally incorporated financial institutions (e.g., insurance companies) will be required to be members of a third party dispute resolution system, but given an option as to whether to join the CFSO.

Low Cost Account

Bill C-38 will provide the federal government with the authority to pass regulations concerning a "low cost account." Initially, the banking industry will be given the opportunity to address the concerns about the availability of a low-cost account through a self-regulatory approach and, therefore, the federal government will negotiate "memoranda of understanding" with individual banks regarding the provision of a low-cost account.

Public Accountability Statement

Banks with equity of C$1 billion or more will be required to publish an annual statement describing the contributions of the bank to the Canadian economy and society.

Tied-Selling

Banks will come under stricter rules with respect to tied-selling. The *Bank Act* will be amended to make it an offense for a bank to put undue pressure on, or coerce, any person to purchase any product or service as a condition of obtaining any other product or service of the bank, rather than simply a loan, as is stated in the current *Bank Act.*

Foreign Bank Branching

Since the passage in June 1999 of legislation that allowed foreign banks to establish branches of the parent bank in Canada, the foreign bank community has been awaiting the release of the tax rules that will be applicable to such branches. It is understood that these tax rules will be released very shortly.

In the meantime, two foreign banks (Chase Manhattan Bank and Morgan Guaranty Trust) have received approval to establish branches in Canada and it is understood that approximately 10 more institutions are awaiting approval of their branch applications.

Anti-Money Laundering Initiatives

In February 2000, the federal government introduced Bill C-22, [the *Proceeds of Crime (Money Laundering) Act]*, and the Bill was passed by parliament in late June. The purpose of the legislation is to implement additional anti-money laundering measures, in addition to the existing Criminal Code provisions and record keeping requirements.

The most significant provisions in Bill C-22 are the ones that establish a mandatory suspicious transaction reporting system. In addition, Bill C-22 requires the reporting of any cross-border transfers of currency or monetary instruments above an amount that will be established by regulations. These regulations are currently being prepared.

While the cross-border reporting will be done to Customs Canada, the mandatory suspicious reports will be sent to a independent federal agency that is to be established under Bill C-22 called the Financial Transactions and Reports Analysis Centre of Canada (FTRACC). The mandate of the FTRACC will be to collect and analyze information to assist in combating money laundering and it will also have primary responsibility for monitoring compliance with the statutory requirements. The FTRACC will be given the authority to disclose information to various other agencies if FTRACC has reasonable grounds to suspect that the information will be relevant to investigating or prosecuting a money laundering offense. The other agencies to which FTRACC may release information include police forces, the Canada Customs and Revenue Agency, the Canadian Securities and Intelligence Service, and the Department of Citizenship and Immigration.

CAYMAN ISLANDS

Regulatory Developments

As the sixth largest international financial center in terms of external banking assets, which was US$669 billion in 1999 (1998: US$650 billion), the Cayman Islands is deeply committed to the promotion and preservation of safety and soundness in the financial system, both domestic and global. In late 1999, the Monetary Authority conducted a self-assessment against major international best practices including:

- the Basel Committee Core Principles for Effective Banking Supervision,
- the IOSCO Objectives and Principles of Securities Regulation and
- the IAIS Insurance Supervisory Principles

From this assessment it was concluded that the Cayman Islands was largely compliant with international best practices although some areas were identified for further improvement. The Government, through the Governor-in-Council (EXCO), has also given its commitment to the granting of greater regulatory autonomy to the Monetary Authority in order to be fully compliant with Core Principle 1.

Towards the end of summer 1999, the Monetary Authority achieved a significant milestone and in the process established a precedent for other financial centers to follow. The first cross-border on-site examination by an offshore center financial regulator was conducted outside of the Cayman Islands on a locally incorporated financial conglomerate with operations across several Latin American countries.

During the second half of 1999, the Monetary Authority conducted a comprehensive review of credit unions, money transfer businesses and building societies to get an understanding of the nature of such businesses. This effort was to determine the appropriate regulatory approach for those institutions as plans are in progress to formally include such entities in the regulatory framework.

Banking Sector Performance

The number of active bank and trust company licenses at the end of 1999 fell to 570 compared to 584 at the end of 1998. This decline was due largely to the global consolidation as merged institutions combined their Cayman's operations. Despite this, 43 of the top 50 banks in the world held active bank and trust company licenses in the Cayman Islands, a symbol of confidence accorded the jurisdiction as a premier international financial center. Active licensees represented sixty countries, with 27 percent from Europe and 24 percent from North America.

Insurance

At December 31, 1999, the total number of insurance licenses on record was 669. Cayman's captive insurance industry remains one of the fastest growing despite increased competition from other domiciles and the continuing soft insurance market. During 1999 the Cayman Islands maintained its position as the second largest captive insurance domicile in the world with 498 companies writing over US$3 billion in premiums and reporting total assets in excess of US$12 billion. These companies emanate mostly from the USA (83 percent), followed by the Caribbean and Latin America (6 percent) and Europe (5 percent).

Investment Services

In 1999, the Cayman Islands increased its dominance as the number two offshore mutual fund jurisdiction by eclipsing the vaunted 2,000 mark with assets of US$210 billion. At the end of 1999, there were 2,271 regulated funds, an increase of about 15 percent, which reflects the continued growth of the mutual funds industry in the Cayman Islands. In addition, the total number of mutual fund administrators licenses increased by fifteen, thirteen of these being Restricted Mutual Fund Administrators Licenses, bringing the total number of mutual fund administrators to 176. The advent of the Internet and the introduction of on-line brokerage services contributed to the continued phenomenal growth in the mutual funds industry globally.

Minor changes were made to the Mutual Funds Law as the enforcement powers were removed from the law and incorporated into the Monetary Authority Law. It is now more important than ever to consider both laws collectively to get a fair interpretation of the legislative framework governing the mutual fund industry in the Cayman Islands. In addition, the Companies Management Law (1998 Revision) was repealed and re-enacted as the Companies Management Law, 1999.

Regulation and Supervision of Non-Domestic Banking Organizations

The Cayman Islands subscribes to the Basel Core Principles for Banking Supervision. Licenses are issued only to branches and subsidiaries whose parents are licensed to conduct banking business in their home country. Furthermore there is a practice of not granting a banking licences to an applicant whose parent’s capital base is less than US$50 million. In the case of foreign banks establishing a branch or subsidiary, confirmation is sought from the home supervisor that there is no objection and that the applicant will be included in home country's consolidated supervision. In practice, the Monetary Authority takes into consideration whether or not the proposed legal and managerial structures of the bank will hinder effective supervision. Structures that are determined to be opaque are discouraged. The operational structure is required to reflect the scope and degree of sophistication of the proposed activities of the bank. The Cayman Islands follows the Basel Supervisory Committee’s risk-based capital standards and require banks, depending on their structure, to maintain a minimum capital equal to either 12 percent or 15 percent of their risk-adjusted assets. All banks licensed in the Cayman Islands are subject to on-going supervision. In the case of foreign branches, the Cayman Islands does not impose any type of asset pledge requirement.

CHILE

Management and Solvency Evaluation

In January 2000, as established by the General Banking Law, the normative about the rating of financial institutions, according to their management and financial solvency, was published. It establishes the process of classifying, when the assigned level for management, and when applicable the new level of solvency, will be notified. It also has a description of the focus of the evaluation of bank’s management, which will determine the classification the law establishes. The proposal is open to comments and suggestions by the industry for a one-year period.

The Year 2000 Date Change

No significant problems were experienced in Chile in connection with the Year 2000 date change, reflecting the intensive preparations by banks and other financial institutions. The Association of Chilean Banks and Financial Institutions was actively involved in coordinating these efforts.

Regulatory Developments

The Superintendent of Banks issued guidance regarding the Maximum Conventional Rate, setting the legal limit to the fixed or variable rate that national credit operations can be charged, and the banks' collection of consumption credit insurance.

In financial risk management, the normative related to asset/liability management in timing unhedged positions was modified, in agreement with the Central Bank**.** New margins, related to the maximum amount by which liabilities may exceed assets that have the same residual timing, considering the capital flows and interest, were established. Furthermore, with the Central Bank's agreement, it was established that beginning June 30, 2000, the unhedged interest rate exposure that financial institutions will have between assets and liabilities cannot surpass an amount equivalent to 8 percent of the basic capital.

The work developed with the Central Bank, through a technical committee created in 1998, allowed dollar interbank credits, the rise in the margin of time deposits that banks can hold overseas, the reduction of the foreign trade note and the increase in the limit of liquidity wedge, among others.

Regarding legal issues, during this period a normative was promulgated modifying the legal regime for securitization. The most outstanding was the rise in the percentage of the assets margin that can be securitized by banking entities from 15 percent to 35 percent.

At the end of 1999, the law that punishes the abuse in the process of extrajudicial collection came into effect.

Anti-Money Laundering Initiatives

The Association has been constantly worried about this issue, and therefore, the work of the Money Laundering Prevention Committee has continued. Furthermore, the Association has also participated as a guest in the Senate's specialized Commission that is studying possible modifications to the anti-money laundering laws.

Pending Issues

Among the challenges that the banking system faces is the improvement in the efficiency rates, that despite a 5-point rise in 1999, are still behind international standards. Also, restoring the profitability rates that were shown before the crisis, between 13 percent or 14 percent, as a result of the reduction in the expenses in reserves and write-offs.

The union field agenda for 2000 focuses on efforts to turn Santiago into an International Financial Center. The Association is convinced that, compared to other marketplaces in the region, Chile has a competitive advantage to fulfill this project. To do so, it is necessary to eliminate barriers that penalize the Chilean Capital Market, such as the reserve, the one-year minimum staying required, capital gain tax and the lack of double taxation agreement. Efforts are also underway to promote the export of financial services.

Another priority for the Association is to encourage revisions to existing law to improve the presence of national capital in medium-size banks. As the banking business requires huge amounts of capital, because of the existing technology and variety of products, it becomes necessary to strengthen the niche bank in a scenario where mega-banks are still in formation.

At the same time, the Association is seeking changes to improve the international presence of Chilean entities, having in mind that most of the regional economies should recuperate throughout 2000. We are aware that the internationalism established in the new Banking Law has not materialized at this moment, primarily due to a complex external environment, and to a very restrictive law. The Association favors relaxation of some of the normatives related to branch consolidation and country risk reserves.

Another issue on the Association's agenda deals with the information system re-engineering that Chilean banks and financial institutions have to give to the authorities. This has a lot to do with the industry's efficiency levels. It is intended to unify the information that flows from the different entities to the Superintendent, and also the information that goes overseas.

In regards to holdings, where the possibility that banks can own part of pension funds is still pending, the Association will follow closely the sending of the respective bill from the Executive to the Senate. It is contemplated that this initiative will allow banks to become part of the pension business through a specialist branch, with a clear normative that avoids conflicts of interest.

Another issue of continuing concern and that was informed to the authorities, deals with payments systems, especially the use of closed credit cards by big stores. The Association believes that the emission of credit cards should be related to banks and that the problem related to existing asymmetry in the markets should be solved by establishing equal rules for anyone that works with a given product.

The circular letter issued by the Value and Security Superintendency, which regulates the insurance housing market, attempted to accomplish what was just mentioned. It establishes similar conditions and transparency in the way it works, avoiding that some actors could offer incentives that were forbidden to mortgage brokers related to banks.

Financial risk evaluation has increased. With this tool, banks have materialized and optimized their risk procedures, establishing the maximum exposure to risk they can show without jeopardizing the normal and efficient operation and profits, due to variations in the exchange or interest rates, etc. In this way financial risk analysis has become a major issue in the Chilean finanical industry.

The Association is analyzing the "Distributed Processing" project that should enable the utilization of business opportunities in technology development, related to important changes due to market globalization in the new century. This would strengthen Chile as a financial center, able to satisfy big international holding needs. It is contemplated that new products and services would be created, which would be available to national enterprises and individuals.

CHINA

Organizational Changes in the Regulatory Structure

On March 21, 2000, China's State Council published a new set of regulations for the supervision of state-owned financial institutions. "The Interim Regulation Committees in State-Owned Key Financial Institutions" states that supervisory committees will oversee the financial and accounting activities of the institutions. The duties of the supervisory committees include:

- ensuring the implementation by the state-owned financial institutions (SOFI) of state laws concerning financial and business activities as well as other administrative rules and regulations;

- overseeing SOFI financial affairs, auditing accounting books and other records relating to SOFI business activities, and verifying the authenticity and legality of SOFI financial reports and capital activity records;

- inspecting SOFI's economic efficiency, profit distribution, retained and added value of state-owned assets, and capital management;

- examining and evaluating the work performance of SOFI chief executives, such as directors, governors, and managers; and

- submitting proposals for rewards and punishment and for appointments or removals.

Bank Regulatory Developments

At beginning of July 1999, Chinese authorities issued new rules aimed at reducing risk of losses from "special bank credits" extended to loss-making state-owned enterprises. According to this rule, only firms burdened with heavy debts and big losses but still having some products with promising market prospects are entitled to the special credit.

China plan to increase the provision for bad debts at domestic commercial banks in 2000 as banks finished reclassifying their loans under international accounting standards. Under existing rules, Chinese banks set aside 1 percent of their outstanding loans at the end of each year as provisions. It is contemplated that the Central Bank would tighten accounting rules for banks – interest on loans overdue for over six months could no longer be included in profits.

Regulation and Supervision of Securities Firms and Other Non-Bank Financial Institutions.

The People's Bank of China (PBOC) and the China Securities Regulatory Commission unveiled rules on allowing securities firms to seek loans from banks using their securities as collateral.

A new investment funds law has been drafted and was issued for review in September 1999.

In July 1999, China widened the investment options of its insurance companies by allowing them to hold investment grade corporate bonds. Insurance companies are limited to holding up to 10 percent of their total assets in corporate bonds with credit ratings above AA+.

In September 1999, seven brokerages and ten fund management companies were approved by the PBOC to borrow money on the inter-bank market.

In March 2000, the China Insurance Regulatory Commission lifted a restriction that limited the region in which insurance companies are allowed to operate.

Requirements for Listing on a Securities Exchange

In December 1999, the China Securities Regulatory Commission published new disclosure rules that require firms to inform shareholders if China's WTO entry will significantly affect company prospects. Companies must also provide more information on board decisions relating to dividends. Firms must provide more detailed explanations of large transactions.

In March 2000, the Commission eliminated quota assignments and administrative recommendations.

Regulation of Non-Domestic Financial Institutions

In November 1999, China allowed the first foreign bank (Japan's Sanwa Bank) to raise local currency through a rediscount transaction with the PBOC.

In January 2000, the China Insurance Regulatory Commission (CIRC) issued new guidelines allowing foreign investors hold as much as 25 percent of a local insurance company (the guidelines do not apply to insurance companies that are qualified and permitted for a listing).

Significant Market Developments

On March 20, 2000, China Min Sheng Bank, China's first privately owned joint-stock bank, commenced operations through its Nanjing branch.

In February 2000, the Chinese Securities Regulatory Commission authorized China Everbright Group to buy 18.67 percent of Shenyin Wanguo's shares, making the bank the brokerage firm's leading shareholder.

Future Developments

The PBOC is expected to strengthen its control over foreign banks in China with two or more branches and by requiring foreign banks to appoint one branch in China as the main reporting branch.

The PBOC also is expected to double the number of financial institutions allowed in the inter-bank market to over 600 by year-end 2000. This will increase trading volumes and allow the market to set interest rates. Finally, it is expected that all Chinese financial institutions will be allowed to participate in the inter-bank market.

COLOMBIA

Legislative and Regulatory Developments

During the period under review, there were significant changes in the financial sector regulation. Among them, the Congress passed Law 527 of 1999, which regulates the access and use of data messages, electronic commerce, and digital signatures.

At the end of 1999, Congress passed the House Financing Law, (Law 546), which establishes the regulatory framework for housing credit. This framework consists of a financing system based on real value units (UVR in Spanish) which maintains the purchasing power of money. Law 546 also ordered a reduction in the housing debts that would be financed with a mandatory investment made by the financial system and the conversion of the Saving and Housing Financial Entities into Commercial Banks. It also established a mortgage-backed securities system. The financial system is awaiting the decision of the Constitutional Court about the constitutionality of Law 546.

The Superintendency of Banks issued External Circulars 044 and 045 in July 1999 establishing a higher level of provisions for past due loans and for assets received as loan payments.

Year 2000 Date Change

Colombian financial institutions did not experience any serious problems in connection with the Year 2000 date change. The Y2K project not only successfully prevented any problems related to the data change, but also allowed the consolidation of the technological inventory in the financial system. Financial institutions modernized their technological platform, improved the development and maintenance of information systems, and increased their knowledge about enhancing their contingency plans.

Anti-Money Laundering Initiatives

Law 526 of August 1999 created the Unit of Information and Financial Analysis (UIAF in Spanish), whose objective is to facilitate governmental intervention in order to detect, prevent, and fight against assets laundering in all economics activities. This unit will centralize, systematize, and analyze the information collected from all economic sectors and share it with all prosecution authorities.

To accomplish its functions, the UIAF is authorized to ask any entity for relevant information even if this information is subject to bank secrecy or commercial secrecy. Once the UIAF has this information, its confidentially is established.

Supervision of Non-Domestic Banking Organizations

Non-domestic banking organizations are not allowed to establish branches in Colombia and instead must operate through separately chartered subsidiaries, which are regulated and supervised the same as domestic banks.

CZECH REPUBLIC

Only few modifications in the legal and regulatory framework of banking in the Czech Republic entered into force in the period from July 1, 1999 to June 30, 2000. Numerous substantial amendments, however, are in various stages of proceeding either in the government or in the parliament with an envisaged entry into force between July 1, 2000 and January 1, 2002 or - as the case may be - at the moment of the accession of the Czech Republic to the European Union. The "Harmonization Phase" of Czech legislation is at its peak period.

Law on Banks

The draft amendment to the Law No.21/1992 Coll. on Banks introduces the following principles of the EU banking legislation into the Czech law:

- single banking licence
- freedom of establishment
- freedom to provide services
- home country control.

The draft also redefines the rules of the deposit protection scheme. The scope of protected deposits is identical with that in the EU and the ceiling of the compensation is upgraded to an equivalent of 15,000 euro. The state is eliminated as a "lender of last resort" to the Deposit Insurance Fund. The deposits both in Czech and in foreign currencies are equally protected by the system.

The bill is going to be submitted to the Parliament before mid-year 2000. The entry into force of the amendment is envisaged for January 1, 2001, the enforcement of the single banking licence, freedom of establishment and freedom to provide services is postponed to the date of the accession of the Czech Republic to the European Union.

Law on Payment Transfer

An outline of a Law on Payment Transfer has been prepared by the Czech National Bank. It is a completely new law for the Czech Republic and is based on an implementation of the EU Directive 97/5/EC on cross-border credit transfers, Directive 98/26/EC on settlement finality in payment and securities settlement systems and the Recommendation 97/489/EC, concerning transactions by electronic payment instruments. The proposal is undergoing a debate in the banking and financial circles now and – if adopted – it should enter into force differently for various rules between January 1, 2002 and the date of the accession of the Czech Republic to the EU.

Law on the Czech National Bank

An "exclusively harmonization-aimed amendment" to the Law No.6/1993 Coll. on the Czech National Bank, as supplemented and amended, has been drafted by the Czech National Bank and is waiting for further proceedings in the government. The draft stipulates in a modified wording the main objective of the central bank (the price stability - not the monetary stability, as before), the independence of the central bank (stating, however, at the same time a commitment to support general economic policy of the government) and the inadmissibility of financing the public sector by the central bank. The draft also includes provisions which contemplate the restructuring of the Czech National Bank under the competence of the European Central Bank to be enacted at the date of the entry of the Czech Republic into the EMU. However, the draft would preserve the central bank's supervisory responsibility over credit co-operatives. The entry into force of the amendment is envisaged for January 1, 2002.

Law Concerning Some Measures Against Legalization of Proceeds of Criminal Activity (Money Laundering Prevention Law)

Law No.61/1996 Coll., concerning the prevention of money laundering, is also being amended to conform fully to the respective Directive 91/308/EC. The key alteration is in a termination of the possibility to maintain anonymous bank accounts, admissible so far in a form of the bearer savings books. The amendment is expected to be in force from July 1, 2000.

Some further developments in the legislation, affecting banks, took place in the period examined. Significant for banks has been an adoption of a Law on Public Auctions (No.26/2000 Coll.) and an amended Bankruptcy Law (No. 105/2000 Coll.), both in force from May 1, 2000. Credit institutions, on the one hand, expect more flexibility in the satisfaction of the secured claims through out-of-court seizures under the Law on Public Auctions. On the other hand, an introduction of a new class of claims (payments to employees) into the separate satisfaction scheme under the Bankruptcy Law Amendment would translate into tighter funds to be allocated for claims by banks related to unpaid credits.

Relevant for banks is also an amendment to the Securities Law, the draft of which is debated in the Parliament now. Banks as securities brokers would be affected by a proposed introduction of the Customer Property Insurance Scheme, which includes financing of a so-called Guarantee Fund. Another important development, introduced by the draft, is related to netting mechanism in the financial derivatives brokerage. Entry into force of the amendment is envisaged for January 1, 2001.

Regulatory Developments

The Czech National Bank's Provision No.3/1999 modified the capital adequacy rules for banks with regard to both credit and market risk. The new regulation was effective from April 1, 1999. Starting from July 19, 1999, bank supervision is conducted on a consolidated basis, with corresponding changes to the basis on which capital requirements, risk-weighted assets and credit exposure limits are calculated.

Market Developments

Two market developments in the period under review were especially significant. The process of privatization of the state's stakes in the banks continued by the sale of the state share in the Československá obchodní banka (Czechoslovak Trade Bank) and the Česká spořitelna (Czech Saving Bank). Of the former "big four" state-owned banks, the state retains a significant interest in only the Komerční banka. Even so, preparations are underway to arrange for participation by a private (foreign) partner.

The engagement of the state in the process of cleaning the credit portfolio of some of big banks prior to their sale continued, and the overall cumulative outlay from public sources reached, according to unofficial estimates, some 220 billion Czech korunas.

DENMARK

Nordic Integration

The integration of the Nordic financial markets continued in 1999/2000 with several cross-border transactions occurring. In 1999 Den Danske Bank acquired the Norwegian Fokus Bank. In March 2000, UniDanmark, the parent company to Unibank and Tryg-Baltica-insurance, merged with the Swedish-domiciled Nordic Baltic Holding, which is the parent company of the Finnish MeritaBank and the Swedish Nordbanken. The three banks continue their banking business in Denmark, Finland and Sweden respectively as subsidiaries of Nordic Baltic Holding.

A Nordic stock exchange alliance was created when the Copenhagen Stock Exchange and the Stockholm Stock Exchange established the stock exchange "NOREX" in January 1998. The aim is to create a common Nordic securities market, where stock exchanges and market participants are provided the best possible platform for offering their services. Norway and Iceland have recently joined NOREX. The first step in this joint effort has been the adoption of common rules and the development of a common trading system (SAXESS), which was introduced for Swedish shares in March 1999 and for Danish shares in June 1999, and is expected to be expanded to include Danish mortgage bonds and government bonds in October 2000.

The Committee on the Financial Sector after the Year 2000

In September 1999, the Committee on the Financial Sector after the Year 2000 submitted its report. The Committee was appointed in August 1997 by the Minister of Economic Affairs for the purpose of analyzing and evaluating the technological and market developments in the financial sector, including identifying areas where changes are needed. The Committee was also given the task of considering the need for legislative changes to address these developments and recommending legislative proposals, as it deemed appropriate.

The Committee report states that effective financial markets are essential for trade and industry, investors, households and the public sector. The report anticipates that the financial sector will be faced with growing competition and pressure for further structural adjustment in the new millenium owing to further advances in information technology (IT), the emergence of the Economic and Monetary Union and increased internationalization.

The Committee concludes that the general purpose of regulation must be to ensure well-functioning financial markets, a competitive framework for financial companies, and good customer relationships. The Committee states that considerable progress has been made toward these objectives, but that long-term action is required in some areas if the Danish financial sector is to be provided with the basis for doing well in the increasingly internationalized competitive markets.

Against this background, the report recommends that action be taken especially in the following three main areas:

- Enhanced financial supervision, including improved and more uniform supervision of financial groups.
- Removal of barriers to structural adjustment and effective capital markets.
- Ensuring that customers are able to make their sound and well-informed decisions.

The Danish Bankers Association, which was a member of the Committee, is generally satisfied with the findings of the Committee, but has not recommended that all of the proposals be implemented.

Supervision of Non-Domestic Banking Organizations

A Danish bank subsidiary of a non-domestic banking organization is subject to all the requirements of the Danish Banking Act, including its capital requirements. The Danish Financial Supervision Authority does not make an independent assessment of the capital adequacy of the non-domestic banking organization as a global entity.

Branches established in Denmark by non-domestic banks are not subject to any type of asset pledge requirement.

EGYPT

In connection with its economic reform program, the government continues to undertake efforts to promote development of the private sector, facilitate export growth and attract additional foreign investment for high priority projects.

At the beginning of July 2000, the Cairo Interbank Offered Rate (CIBOR) was introduced on a test basis to encourage transparency and disclosure by Egyptian banks. CIBOR is calculated on the basis of two-way quotations.

During the period under review, two public sector banks, the Arab Land Bank and the Egyptian Land Bank, merged, while other public sector banks issued shares in joint banks to promote private ownership in the banking sector.

Significant developments in banking include the following:

- the Ministry of the Economy proposed a new mortgage law, which remains under consideration;
- a new automated system for settlements in local currency among banks via SWIFT has been developed;
- automated check processing has been expanded; and
- actions have been taken to promote the use of credit cards and electronic banking, including home banking and ATMs.

The Federation of Egyptian Banks has established a Marketing Research Center to provide its members economic information and studies regarding banking products and services. The Federation is also involved with the Cairo Economic Center, which has been established with the aid of the International Monetary Fund.

Significant developments in the securities area include the following:

- securities dealers were exempted from capital gains tax on the trading of securities;
- arrangements were made with the Financial Times Association for publication of a new Egyptian stock index;
- arrangements were made for issuance of international identifying numbers for Egyptian securities;
- improvements were made in the means for clearance and settlements of securities transactions; and
- as increased activity is anticipated in the Egyptian bond market, preparations were completed for the introduction of an automated quotation system.

EUROPEAN UNION

The first eighteen months of the euro went smoothly without any technical difficulties emerging, though the euro itself suffered on the foreign exchange markets. In line with the European Commission's Action Plan for Financial Services, the development of the EU Single Market in financial services continued apace. In the banking sector continued consolidation was the order of the day.

ECONOMIC AND MONETARY AFFAIRS

With the successful introduction of the euro, the Federation identified the need to focus more resources on economic and monetary issues. At the end of 1999, it created the Economic and Monetary Affairs Committee (EMAC), and appointed Dr Martin Hüfner, Chief Economist of HypoVereinsbank AG, as its Chairman. The Committee is composed of senior economists from major banks and national banking associations from 16 countries. One of its main functions is to offer views and advice externally on issues that are important to the banking sector and to its interlocutors at the international level, in particular the European Central Bank (ECB) and the Commission.

For the year 2000, the Committee plans to focus on the economic and monetary situation in the EU; general monetary policy issues (such as asset price inflation); issues of communication; the mechanics of the single monetary policy; and the structure of the banking system.

The EMAC also issues regular "FBE Letters" on economic and monetary issues. It was responsible for the first and third FBE Letters on "Strategies for a stronger euro" and "Greek membership in the EMU" respectively.

THE EURO

The Federation has begun to conduct regular surveys on euro use in the EU banking system. These are intended to provide a picture of the spread of use of the euro over time, and to deepen understanding of the transition to the euro.

The results of the first survey, issued in May 2000, show that in most euro area countries, the demand for euro-denominated banking services is low. Most customers see no need to open bank accounts in euro as yet. This can be explained by the fact that, in these countries, the national legacy currency is in a legal sense already the euro. Moreover, there is perfect fungibility between the legacy currency and the euro: for example, if a French Franc account holder receives a payment in euro, this will be converted into French Francs at no cost to the account holder, and deposited on his/her account. Conversely, the account-holder can make a euro payment from a French Franc account at the same cost and with the same facility as a French Franc payment from the same account. The survey also shows that in most countries banks were able to make available the full range of retail payment services in euro as at January 1999. However, as in the case of euro accounts, the proportion of retail payment transactions taking place in euro was low.

The survey will be issued twice a year until January 1, 2002, when euro use becomes obligatory throughout the euro zone. Future results will show the migration from national legacy currencies to the euro, which is expected to intensify as January 2002 approaches.

EUROPEAN BANKING FEDERATION MASTER AGREEMENT FOR FINANCIAL TRANSACTIONS (European Master Agreement – EMA)

The European Banking Federation, in co-operation with the European Savings Banks Group, launched the European Master Agreement (EMA) on October 29, 1999. The EMA aims to consolidate into a single set of harmonized documents, various master agreements used within the euro zone and certain neighboring countries, particularly for repurchase transactions and securities lending. At the same time, parties to the EMA are able to choose the applicable law, jurisdiction and contractual language and can take into account various specific national legal requirements.

The EMA is primarily designed to replace master agreements existing under the laws of various continental European countries, which are used predominantly (though not exclusively) in a domestic context. It should also be suitable, however, for cross-border transactions. The EMA is innovative: it is a multi-jurisdictional and multi-product agreement.

Multi-jurisdictional: It is intended to be used in different jurisdictions under the laws of different jurisdictions in different languages, particularly within the EU.

Multi-product: It will enable market participants to document potentially all trading transactions under a single master agreement, including (in the current draft) repurchase transactions and securities loans. The structure of the agreement is open for new product annexes to be added in order to expand the scope of the agreement to include other financial transactions, such as FX, swaps and options.

The English version of the EMA, together with a detailed Explanatory Memorandum, is available on the EBF website (**www.fbe.be)**. Legal opinions are being sought in the various European jurisdictions, and versions in various languages are being prepared. Information concerning their finalization will also be published on this website.

EURIBOR AND EONIA

These new benchmarks were launched at the start of 1999 by the European Banking Federation and the ACI, the Financial Markets Association, in co-operation with the other European credit sector associations representing the savings banks and the co-operative banks. The rates are defined as follows:

Euribor	(Euro Interbank Offered Rate) is the rate at which euro interbank term deposits within the euro zone are offered by one prime bank to another prime bank.
Eonia	(Euro OverNight Index Average) is an effective overnight rate computed as a weighted average of all overnight unsecured lending transactions in the interbank market, initiated within the euro area by the contributing panel banks.

A panel of 57 banks was selected to contribute for both rates. As predicted, since the launch of the rates the number of banks on the panel has been decreasing due to mergers within the panel. The Euribor Steering Committee, consisting of independent money market experts, has overseen the management of the rates and the application of the Codes of Conduct.

In relation to Eonia, the European Banking Federation is working closely with the ECB, which calculates Eonia on behalf of FBE / ACI.

Within the first few weeks of European Monetary Union, Euribor and Eonia became established as the benchmarks in the euro market.

IMPROVING RETAIL PAYMENTS

The European Commission published a Communication on Retail Payments in the Internal Market largely concerned with small value credit transfers. The Commission calls for full implementation of the cross-border credit transfer Directive, and for banks to fully implement the IBAN and IPI standards by January 1, 2002. Furthermore, the Commission invites banks to put forward proposals for the establishment of efficient cross-border transfer linkages. On cash exchanges, the Commission asks for the review of bank charges for the exchange of small amounts while recognizing that charges have generally fallen to reflect the removal of the exchange rate risk.

The European Central Bank has published a report on the same issue as well. This Report sets out seven objectives which the industry should meet in the medium term to improve cross-border payments in euro. The ECB has set up several working groups to consolidate discussions with the banking industry on this.

ELECTRONIC MONEY INSTITUTIONS

A Directive authorizing nonbanks to issue electronic money throughout the EU was approved by the EU Council. The Directive subjects electronic money institutions to a set of banking supervision rules that are less strict than those applied to full credit institutions.

TAXATION OF SAVINGS INCOME

In 1997, the Council of Ministers for Finance (ECOFIN) had approved the basis for a proposal for a directive on taxation of savings, as one of the measures of a "tax package" to tackle harmful tax competition in the EU. This proposal was aimed at ensuring, for individuals, a minimum of effective taxation of savings income, in the form of interest payments, within the Community.

The European Council met in Santa Maria da Feira on June 19 and 20, 2000. They endorsed the report submitted by the ECOFIN Council and the statements attached to this report, the key elements of which are the following:

- The Council and the Commission commit themselves to seeking agreement on the substantial content of a Directive by the end of the year 2000.

- The Presidency and the Commission shall immediately enter into discussions with key third countries to promote the adoption of equivalent measures in those countries, while the Member States concerned commit themselves to promote the adoption of the same measures in all relevant dependent and associated territories. Once sufficient reassurances have been obtained, the Council will decide on the adoption and implementation of the Directive no later than December 31, 2002.

- During a transition period, Member States shall either exchange information with other Member States or operate a withholding tax and transfer an appropriate share of the revenue to the investor’s state of residence. The Commission shall report regularly on the application of these systems and on international developments.

- Exchange of information shall be the ultimate objective. Any Member State operating a withholding tax shall agree to implement exchange of information, as soon as conditions permit, and in any case, no later than seven years after the entry into force of the directive.

TOBIN TAX

On January 18, 2000, four motions of resolution relative to the "Tobin tax" were presented at the European Parliament. Three motions were tabled in favour of the introduction of such a tax, and the fourth one rejected it. The European Parliament rejected all four motions on January 20, 2000.

VAT AND ELECTRONIC COMMERCE

The European Commission presented in June 2000 a proposal for a Directive to modify the rules for applying VAT to certain services supplied by electronic means as well as subscription-based and pay-per-view radio and television broadcasting. The objective is to create a level playing field for the taxation of digital e-commerce in accordance with principles agreed at the 1998 OECD Ministerial Conference and to make compliance as easy and straightforward as possible.

NEW DIRECTIVE PROPOSAL AMENDING THE 1991 DIRECTIVE ON MONEY LAUNDERING

The proposal for a Directive on prevention of the use of the financial system to facilitate money laundering has been submitted to the European Parliament. The current report of the Parliament extends the obligations provided under the 1991 Directive to other professions such as tax consultants, accountants and members of legal professions. The definition of money laundering is limited to fraud and corruption that affects the financial interests of the European Union, and are covered by the Second Protocol of June 19, 1997 (which contains a rule stating that measures to combat money laundering in connection with fraud damaging to the financial interests of the EU should be taken only when serious offences have been committed).

At this stage, the Annex of the proposal, which specified appropriate methods for credit and financial institutions to identify customers when they are not face to face, has been deleted. Nevertheless, some provisions have been reintroduced in the proposal itself and the Banking Federation is still lobbying to avoid this.

FRAUD AND COUNTERFEITING OF NON-CASH MEANS OF PAYMENT

The European Commission has launched a major initiative against fraud and counterfeiting concerning payment cards, electronic money, checks, home banking and other non-cash means of payment. The key message is that problems concerning fraud and counterfeiting of non-cash means of payment must be tackled broadly by a comprehensive and consistent set of actions.

The new framework strategy, as outlined in the Commission Communication, has two components:

- joint action to ensure that fraud against all forms of non-cash means of payment is recognized as a criminal offense in all EU Member States;

- the outlining of a broad strategy to ensure safe non-cash transactions for consumers, companies and others in Europe. This strategy might include, in particular, non-cash means of payment issuers (i.e., banks, cards companies, etc.) being requested to notify, on a voluntary basis, the authorities of cases where there were reasonable grounds for considering that an offence might have been committed (i.e., to report suspicious transactions).

The Commission will be issuing a Communication on this project.

ELECTRONIC COMMERCE

The EU has adopted important legal provisions in this respect. The Directive of December 13, 1999 provides legal framework for electronic signatures. The Directive on certain legal aspects of Information Society Services, in particular electronic commerce was adopted in May 2000. Regarding the question of applicable law, the provision has established the "home country control principle" between businesses and between businesses and consumers. In the future, the on-line relationship will be governed by the law of the country of establishment of the service provider unless the parties have otherwise agreed. For contractual obligations involving consumers, the law of the country of residence of the consumer will apply when the conditions provided for in the Rome Convention are met (especially in case of advertising or prior solicitation).

The adoption of the Directive concerning the distance marketing of consumers' financial services is still in process.

The Regulation on jurisdiction and the recognition and enforcement of judgements in civil and commercial matters has formed the subject of a consultation procedure at European Parliament level. Concerning the e-commerce aspect, the current project draws on the U.S. case law to determinate jurisdiction in case of consumers' disputes. Industry is also incited to accept a system of out-of-court settlement of consumer disputes.

REVISION OF THE BASEL CAPITAL ACCORD

In June 1999, the Basel Committee issued its consultation document setting out proposals for a revised Accord. In response to the request to the banking industry to comment on the consultation document by March 2000, the EBF produced a paper setting out a framework for regulatory capital based on the use of internal credit ratings generated by the banks themselves. The EBF is firmly committed to the use of internal credit ratings by the majority of banks as the only practical means of delivering a new Accord which will ensure that the calculation of regulatory capital reflects closely the level of credit risk and thus the level of economic capital.

PROPOSAL FOR A DIRECTIVE TO ALLOW FAIR VALUE ACCOUNTING

The Commission has published a proposal for a Directive which would authorize Member States to permit companies to fair value financial instruments in their consolidated accounts. Banks would be kept outside the scope of this proposed Directive for the time being.

FINLAND

Bank Regulatory Developments

In 1999, the Basel Committee on Banking Supervision issued its proposed revisions to its risk-based capital adequacy regime. According to the proposal, the risk categories applied to credit institutions, public sector entities and corporate credits would be based on their external credit ratings. The risk-mitigating effect of mortgages, guarantees and netting would be taken into account on a larger scale than is currently permissible. Capital charges should also be assigned for interest rate risks in the banking book and for operational risks. Supervisory authorities would be granted more discretionary power so that they could impose a higher capital requirement on a bank on the basis of its risk profile. Public disclosure of information on the economic standing and capital adequacy of banks would be enhanced.

The Finnish Financial Supervision Authority revised its regulations on bookkeeping and financial statements of credit institutions. The amendments concerned the reporting of shares and real estate owned by a credit institution and other companies included in consolidated supervision and the reporting of own funds-required for covering market risk.

A working group to develop legislation governing credit institutions proposed that the election of a supervisory board for a credit institution should be voluntary. The proposal was approved by Parliament in Spring 2000. The working group also proposed that:

- statutory provisions concerning banks' merger, splitting and voluntary liquidation should be amended;

- legislation should be enacted providing for a bank's transfer of its business and voluntary surrender of its license; and

- the role and tasks of banks' administrative bodies should be reformed to correspond with the provisions in the Companies Act.

The proposals will be submitted to Parliament in Autumn 2000.

In late 1999, the Ministry of Finance appointed a committee to prepare questions in connection with the taking of deposits and other refundable assets from the public, the issuance of electronic money and the availability of payment services.

A new Act on Mortgage Banks was passed in autumn 1999. A mortgage bank grants loans from funds acquired by issuing secured bonds either against shares in a real estate or housing company or against real estate mortgages.

A revised Personal Data Act came into force in summer 1999. Thereafter, the Finnish Bankers' Association started to prepare rules for handling personal data in credit institutions. The new bank secrecy regulations were completed at the same time. Due to the amendments to the legislation, the authorities' right to obtain information has been increased in some respects. Measures to prevent money laundering have been improved, with a resulting increase in the number of banks' reports of suspicious cases to the police.

Payment Systems Developments

In autumn 1999, a new Giro Act came into force based on the EU Directive on harmonizing cross-border transfers. The Act also applies to domestic giros, thus increasing the importance of the account number in transferring the funds. The conditions for payment transfers were also revised and the customer information practices were accelerated.

Payments and cover transfers between the banks and the central bank have been transmitted in euros after its introduction. The same applies to securities trading and foreign payments. Card payments will be transmitted in euros from autumn 2000. The risk management procedures of payment systems required by the Bank of Finland were started along with the introduction of the euro. Preparations for the introduction of euro coins and notes have been going on intensively.

Year 2000 Date Change

The banks carried out their Year 2000 systems changes and testings independently, though in cooperation with their interest groups and the central bank. The banks encountered no problems in connection with the millenium date change. The decision of the European Central Bank to keep the TARGET system closed on December 31, 1999 called for an amendment to the Promissory Notes Act. In cases where banks' payment systems are closed because of the decision of the Bank of Finland or the European Central Bank, the due date of a debt will be shifted to the first banking day to follow.

Other Developments

In autumn 1999, the Government decided to privatize Leonia Bank, which was formed two years earlier by a merger between the state-owned companies Postipankki Ltd and Finnish Export Credit Ltd. The reorganization took place by a merger with the insurance group Sampo. The new group will start operations at the beginning of 2001. Within the group, banking operations will be conducted by Leonia Bank plc and Leonia Corporate Bank plc, with insurance operations undertaken by Sampo Group plc.

Pohjola Insurance Company is also reorganizing. Its major shareholder, Suomi Mutual Life Assurance Co., sold its ownership to a newly established consortium that includes the OKOBANK Group.

In spring 2000, the MeritaNordbanken Group and Unidanmark announced their merger. The MeritaNordbanken Group is still interested in buying from Norway the Christiania Bank. The group aims at expanding its operations to cover each of the Nordic countries and at becoming an institution of top importance within the whole Baltic area.

FRANCE

The French banking sector has been undergoing a process of restructuring during the past several years. A number of foreign banking organizations took advantage of the effort by Banque Nationale de Paris to acquire Société Générale and Paribas, as well as the privatization of Crédit Lyonnais, to strengthen their positions considerably. Thus, Spain's Banco Santander Central Hispano now owns 5.06 percent of Societe Generale, while Germany's Commerzbank and Spain's Banco Bilbao Vizcaya Argentaria acquired 4 percent and 3.75 percent, respectively, of Crédit Lyonnais.

Moreover, Act No. 99-532 of June 25, 1999 on savings and financial security reformed the statutes of the savings banks (Caisses d'épargne) buy, *inter alia*, defining rules governing ownership of their equity. As a result, these banks, which are now regarded legally as cooperative banks, have opened up their capital. The sale of their shares will conclude no later than 2003. The proceeds of such sales will be paid into the pension fund reserve.

On the occasion of the annual dinner of the Association Françaises des Banques (AFB), attended by the Minister for Finance and the Economy, which traditionally takes place in January, the President of the AFB announced the creation of the Fédération Bancaire Française. This new structure, which will operate as a type of "umbrella" organization for the banking industry, brings together banks that were formerly members of the AFB and mutual and cooperative banks, including the Caisses d'épargne.

Bank Regulatory Developments

Act of June 25, 1999 on Savings and Financial Security

This Act is of considerable importance to the banking industry. Among its more significant provisions are the following:

- Creation of a general deposit guarantee fund for the banking system

Funded by all lending institutions, except the financial services operations of the post office, the public treasury and the Bank of France, this guarantee fund is designed to cover various types of risks. Three distinct sections comprise the fund: guarantee of cash deposits, guarantee of security deposits and guarantee of bond sureties. The fund functions in both a preventive and remedial capacity, with its guarantee available to the Banking Commission to assist it in lending institution resolutions.

On July 21, 1999, a decree was passed approving the implementing regulations issued under the provisions of the Act regarding the guarantee of cash deposits. These regulations set forth rules relating to payment of claims (Regulation No. 99-05), resources and operation of the deposit guarantee fund (Regulation No. 99-06), conditions under which claims to the deposit guarantee fund can be made (Regulation No. 99-07) and determination of the aggregate amount of annual contributions to the fund.

- Reform of the Statutes of the Caisses d'épargne

Members of the AFB have for many years sought reform in the statutes of the savings banks, citing the competitive advantages the savings banks derive from, among other things, their lack of obligation to pay dividends and the favored status granted a number of the products they offer such as the state guarantee supporting the Livret A. The Act calls for gradual reform in the structure of the savings bank network and authorizes the savings banks to conduct all types of banking operations (hitherto they could perform such operations only with companies making a public call on savings). However the state guarantee of the Livret A has been retained.

- Strengthening financial security

Other provisions of the Act that are particularly relevant to lending institutions include the following:

Article 35, which broadens the powers of the central bodies of the different banking networks, notably with the prohibition on limiting the distribution of dividends;

Article 37, relating to the Banking Commission's power to issue recommendations;
Article 40, requiring lending institutions to establish internal audit systems;

Article 47, which defines the terms "financial group" and "mixed group";

Article 48, which permits the Comité des Establissements de Crédit et des Entreprises d'Investissement (CECEI) to withhold its approval upon its finding that effective supervision would be hindered by the existence of links of capital or control with a country that does not belong to the European Economic Area;

Article 50, which authorizes the Banking Commission to require designation of an additional external auditor; and

Articles 59 to 61, relating to the organization of cooperation for the audit authorities.

Other provisions of the Act relevant to the banking industry relate to cross-border transfers of money, early reimbursement compensation, renegotiation of building loans and information to guarantors.

Interest on Savings

Important changes were made by two decrees passed on July 23, 1999 in relation to housing savings rates and by Regulation No. 9913 issued on July 22, 1999 by the Comité de Réglementation Bancaire et Financiére (CRBF) in relation to interest paid on funds received by lending institutions.

For holders of Housing Savings Schemes (Plans d'Epargne Logement – PEL), the rate paid was lowered from 4 percent to 3.60 percent as from July 26, 1999, with 2.61% payable by the establishment.

For holders of house savings accounts (comptes d'épargne logement – CEL), the rate of interest paid from August 1, 1999, regardless of the date the account was opened, was lowered from 2 percent to 1.5 percent. The corresponding lending rates were lowered to 3 percent.

The following additional changes were effective August 1, 1999:

- The interest paid on the first Caisse d'épargne Livrets (passbook savings) such as Livrets bleus, Livrets d'épargne du travailleur manuel (manual workers' savings books) and the Codevi, was lowered from 3 percent to 2.25 percent.

- The rate of the Livret d'épargne populaire (popular savings book) was lowered from 2.25 percent to 1.5 percent.

Prudential Surveillance

Noteworthy regulations issued by the CRBF during the period under review include the following:

- Regulation No. 99-01 on prudential surveillance of market risks amends Regulation No. 95-02 of July 21, 1995 and clarifies certain of its provisions. In particular, it takes into account the latest recommendations formulated by international bodies. For example, it seeks to limit differences between the requirements of French law and the standards prescribed by the Basel Committee as to those financial institutions with a substantial international presence.

- Regulation No. 99-02 addresses three aspects of the risk-based capital standards applicable to French banks. It clarifies certain aspects of the risk weights assigned various classes of assets. Third, it requires that risks other than interest/exchange rate risks be taken into account with respect to a bank's trading of derivative instruments for its own account.

- Regulation No. 99-03 on the monitoring of major risks introduces an intermediary threshold for lending institutions with equity of between EUR 4.375 and 7 million. Until January 1, 2004, these institutions must limit their total risk-weighted exposure to any person to no more than EUR 1.75 million, which corresponds to between 25 percent and 40 percent of equity. For institutions with equity of less than EUR 4.375 million, such limit is set at 40 percent of equity.

In its Opinion No. 2000-1 (January 20, 2000) the Banque de France modified its Opinion no. 99-01 regarding maintenance of mandatory reserves. Commencing with the January 24, 2000 reserve period, the lump sum deduction for negotiable securities with an initial maturity equal to or less than two years is increased from 10 percent to 30 percent.

Experience with the Euro

The third phase of the Economic and Monetary Union commenced on January 1, 1999 with the changeover to the euro in eleven Member States and the irrevocable fixing of the parities of the participating national currencies. This transitional period will end on January 1, 2002 with the introduction of euro coins and banknotes. The "Euro 11" Council of November 8, 1999 limited the maximum duration of the concurrent circulation of euro and national currency notes and coins after January 1, 2002 to two months at the maximum.

Since January 1, 1999, the European Central Bank (ECB) has managed the monetary policy of the euro zone with the primary objective to maintain price stability. On several occasions, the European Parliament has criticized the ECB for lack of transparency in its actions. In a report adopted in October 1999, the Parliament invited the ECB to take a number of measures designed to heighten transparency.

Year 2000 Date Change

No significant problems were experienced in the French banking and financial system in connection with the Year 2000 date change. The successful transition was a tribute to the intensive preparations over a period of more than two years and the close cooperation between the industry and the supervisory authorities.

GERMANY

Germany's banks made a smooth transition to the year 2000 and are now busy preparing for the changeover from deutschmark to euro notes and coins at the beginning of 2002. The integration of national financial markets both within the European Monetary Union (EMU) and beyond made significant progress. In addition to a sweeping tax reform, further work was done on improving the general legal framework, also to promote electronic commerce, which German banks continue to push.

Smooth transition to the year 2000

Thanks to extensive preparations, the German financial industry negotiated the changeover to the new millennium without any trouble. National and international end-to-end tests in the payments sector in particular had already demonstrated in the third quarter of 1999 that Germany's banks would, as contemplated, be ready for the year 2000.

Preparations for the cash changeover from the deutschmark to the euro

Following the introduction of the euro for cashless payments in the EMU member countries on January 1, 1999, notes and coins denominated in euros will be introduced at the start of 2002. In Germany, the deutschmark will thus be replaced by the euro for good.

On December 16, 1999, the German parliament passed the *Act amending Monetary Provisions following the Introduction of Euro Notes and Coin (Third Euro Introduction Act)* . This Act, which enters into force on January 1, 2002, creates the legal framework for the introduction of euro notes and coins. It includes the following provisions:

- As of January 1, 2002, the euro will be the sole legal tender, which means the deutschmark will lose this status ("legal big bang"). From the beginning of 2002 onwards, the Bundesbank will exchange DM notes and coins for euros free of charge at the irrevocably fixed conversion rate.

- The use of notes and coins denominated in deutschmarks after January 1, 2002 is not regulated by law, but, in accordance with the "joint declaration" of the central associations of the banking industry, the vending machine industry, the retail trade and similar services, will be possible in practice until February 28, 2002.

- The Third Euro Introduction Act also extends the criminal and administrative sanctions against the counterfeiting of banknotes and coins to cover the deutschmarks which will still be in circulation during the changeover period.

Following the publication in mid-1999 of the Bundesbank's *Concept for the circulation of euro notes and coin in the Federal Republic of Germany*, a project coordinated by the Association of German Banks was carried out in the Greater Hamburg area to simulate the cash changeover under real conditions and so determine the conditions for ensuring that the changeover is carried out safely, efficiently and economically. This project showed that meticulous planning and preparation of transport and storage capacities in particular, but also of banks' counter facilities, are essential. The task of the German government will be to uphold law and order during this phase, which will see a dramatic increase in the volume of cash in circulation, and to ensure public confidence in the new currency.

Further integration of financial markets in the euro zone

Transactions between the central bank system and banks, on the money market, on the foreign exchange market and in other financial market segments have been conducted exclusively in euros since January 1, 1999.

An infrastructure comprising several payment systems is available for handling large-value payments resulting from money market and foreign exchange trading in euros. Besides TARGET, which links the national real-time gross settlement (RTGS) systems of the euro area's central banks, mention should be made, in particular, of Euro Access Frankfurt (EAF), a hybrid system combining gross and net settlement operated by the Bundesbank (Landeszentralbank in Hesse). On January 13, 2000, the Bundesbank's Governing Council decided to merge the German RTGS system ELS (Electronic Counter) with EAF. The resulting RTGS^{plus} system, due to replace ELS and EAF in 2001, will be a liquidity-saving gross system.

The net settlement system EURO1 operated by the Euro Banking Association (EBA), on the other hand, is designed to handle commercial payments and not large-value interbank payments. Despite this, large-value payments were often routed through this system, particularly during the early phase of monetary union, leading to liquidity management problems for banks. This is why, in September 1999, the European Banking Federation (EBF) extended the scope of its Guidelines on Liquidity Management, issued in December 1998 and originally geared solely to TARGET payments, to cover all euro payment systems. The guidelines recommend European banks to feed payments related to interbank transactions and commercial payments into the systems by certain times, with sufficient liquidity coverage, and to reserve the period after 5 p.m. for balancing their liquidity position.

In October 1999, the EBF, in collaboration with the European Savings Banks Group, issued the European Master Agreement (EMA). This was a major step towards standardizing existing national master agreements, in the area of securities lending and securities repurchase transactions to start with, and allowing, in the medium term, uniform documentation of financial derivatives transactions.

Integration and harmonization of stock exchanges

The German central securities depository Deutsche Börse Clearing AG and the international clearing organization Cedel International S.A. (Luxembourg) merged with effect from January 2000 to form a common European clearing house, called Clearstream International, based in Luxembourg with a German subsidiary in Frankfurt.

On June 1, 2000, Ascension Day, all German stock exchanges were open for trading on a national public holiday for the first time. From 2000 onwards, trading will in fact take place on four German public holidays: Ascension Day, Whit Monday, Corpus Christi and the Day of

German Unity (October 3). The reason for this is the need to be able to trade on days when TARGET is open for business.

With effect from June 2, 2000, the German stock exchange Deutsche Börse and Eurex, the futures and options exchange operated jointly by Germany and Switzerland, will extend the trading sessions for all stocks and warrants on the Frankfurt Stock Exchange and for all German stock derivatives and stock index derivatives on the Eurex until 8 p.m. This is intended to give private and institutional investors more chance to respond to market movements in the United States.

At the beginning of May 2000, Deutsche Börse and the London Stock Exchange announced that they had agreed to merge to create a new company, to be called iX (International Exchanges). iX signed a memorandum of understanding with NASDAQ in the United States on the creation of a joint, pan-European high-growth market. iX will offer trading and information products for equities, commodities and derivatives. It will also provide exchange systems and set up an Internet incubator. The new company will be Europe's largest stock market, with around 53 percent of traded volume and, through Eurex, the biggest derivatives market worldwide. iX will consist of all of Deutsche Börse's and the London Stock Exchange's businesses, except for Deutsche Börse's 50 percent stake in Clearstream International, which Deutsche Börse will continue to hold. Shares in iX will be split equally between Deutsche Börse and the London Stock Exchange. The electronic trading platform for stocks will be Deutsche Börse's Xetra system.

[Editor's note: On September 12, 2000, the London Stock Exchange announced its decision to withdraw its merger plan with Deutsche Börse in order to focus attention wholly on the hostile bid by OM Gruppen, which was made in late August.]

Decision by the European Commission against state aid provided by a German federal state to Westdeutsche Landesbank (WestLB) and distorting competition in the European Single Market

In July 1999, the European Commission announced its decision on the complaint submitted by the Association of German Banks against the Federal Republic of Germany in connection with the integration of the state housing agency WFA into the accounts of WestLB, Germany's biggest public-sector bank, by the state of North Rhine-Westphalia. The Commission's decision requires the Federal Republic of Germany to instruct the state of North Rhine-Westphalia to request WestLB to pay back the state aid which it provided by foregoing adequate compensation for the transfer of WFA's assets to WestLB. In May 2000, the European Commission filed a complaint at the European Court of Justice against the Federal Republic of Germany under Article 226 of the Treaty establishing the European Community (failure to comply with this treaty), since the Commission's decision had not yet been put into effect.

Improvement of the conditions for secure and convenient electronic commerce

Economical use of electronic networks requires fast and simple payment systems. The private banks in Germany have sponsored or themselves developed a number of projects dealing with Internet payment systems and new home banking modules for marketing banking products.

Mention should be made, in particular, of SET (Secure Electronic Transaction) in conjunction with a credit card and HBCI (Home Banking Computer Interface), a completely new development.

In electronic commerce, customers must be able to rely on their transactions not being blocked or manipulated. Digital signatures offer secure protection for confidential data. They allow verification of the sender's identity and of the authenticity of electronic documents by means of prior certification of the participants. Both SET and HBCI are based on user certification. In order to promote user-friendly and secure electronic commerce via the Internet, the four German big banks set up the service provider TC Trust Center as a common certification body for the private banks. TC Trust Center will offer the new security services to all interested banks, in close collaboration with Bank-Verlag, a subsidiary of the Association of German Banks.

New developments in the regulation of securities trading

The German Federal Securities Supervisory Office issued a general order on July 27, 1999 banning marketing by means of "cold calling". This order prohibits investment services firms from making telephone calls to customers with whom they have done no previous business with respect to investment services unless requested to do so by the contacted person in a manner satisfying the requirements laid down by the Supervisory Office.

In its announcement relating to the Prospectus Act and the Prospectus Ordinance, published in the Federal Gazette on September 21, 1999, the Supervisory Office interprets, among other things, the treatment of securities offered via the Internet. A public offer subject to the requirement to publish a prospectus is deemed to exist if German investors are directly addressed, it being of no relevance where the offeror is domiciled or where the server is located from which the data can be downloaded.

On November 4, 1999, the Federal Securities Supervisory Office published a new *Guideline on the organizational duties of investment services enterprises* (Compliance Guideline). The guideline sets out statutory organizational duties in detail. According to this guideline, an investment services enterprise must be organized in such a way as to ensure that the interests of its customers are always safeguarded. The new regulation replaces a guideline with the same content of December 2, 1998, which applied only to banks, and merely extends the scope of the guideline to cover financial services institutions.

On July 15, 2000, the Federal Banking Supervisory Office (FBSO) and the Federal Securities Supervisory Office published their joint announcement on staff transactions. The announcement defines the responsibility of the credit institutions and financial services institutions to safeguard their solvency and protect investors by ensuring that transactions in securities and derivatives carried out by members of their staff are not contrary to the interests of the institution or its customers. The new guidelines replace an announcement published by the FBSO in 1993 and are a major element of the German compliance framework.

New bank regulatory developments

The new liquidity standard announced by the FBSO on November 25, 1998, which is better geared to banks' liquidity management, replaced the existing standards on an optional basis on January 1, 1999 and will do so on a mandatory basis with effect from July 1, 2000.

Accounting and reporting

The *Act relating to the Publication of the Annual Accounts of Certain Trading Partnerships*, which entered into force on March 9, 2000, gives all enterprises which make use of an organized market the chance – previously restricted to exchange-listed companies – to draw up consolidated annual accounts in accordance with international accounting standards, thereby exempting them from national rules. It also allows branches of foreign banks to present the annual accounts of their bank in the home-country language, provided that they also publish a German translation of the attestation issued by the home-country registrar. Finally, the Act raises the disclosure threshold for banks from DM 300 million to € 200 million.

The German Accounting Standards Committee issued special standards for flow-of-funds analysis and segment performance reporting by banks. Standards for banks' risk reporting and corporate takeover accounting are in the pipeline.

The FBSO arranged for the joint survey by the Basel Committee on Banking Supervision and the International Organization of Securities Commissions (IOSCO) on the public disclosure of trading and derivatives activities to be circulated to German banks. The disclosure requirements it contains are already largely accommodated by way of recommendations made by the Association of German Banks' Accounts Committee. The risk disclosure standard for banks laid down by the German Accounting Standards Committee will further improve transparency.

Auditing

In January 2000, the FBSO issued comprehensive minimum requirements for banks' internal auditing to replace rules in force since 1976.

The German government introduced in February 2000 a bill amending rules governing the activity of auditors. This bill's main aim is to introduce external auditing quality controls (including, inter alia, a so-called peer review). It is expected to be passed in the course of the year.

New developments in company law

In May 2000, the Federal Government introduced a bill dealing with registered shares and easier exercise of voting rights. The bill is designed, first and foremost, to update registered share law and thus facilitate the increasing transition from bearer to registered shares. It also aims to create the conditions for opening company law to communication by electronic media.

At the end of June 2000, the Federal Ministry of Finance introduced a bill on takeovers, based on the anticipated EU Directive on takeover bids, which is intended to ensure that corporate takeovers take place in conditions which are fair and transparent while paying due regard to the legitimate interests of minority shareholders and employees. Along with provisions regulating voluntary bids, the bill envisages that a company will have to make a mandatory bid once it has acquired a stake of 30 percent in the target company. Instead of a cash offer, the bidder may, as a rule, offer liquid voting shares in exchange for shares in the target company. The board of directors and the supervisory board of the target company must, in principle, maintain a neutral position, although certain measures are permissible. These include seeking a white knight, issuing new shares on the basis of an approved capital increase in compliance with the subscription rights of existing shareholders and taking defensive action approved by a general meeting of shareholders.

Also in the context of corporate takeover legislation, an amendment to the German Share Companies Act is envisaged which would permit majority shareholders who have acquired a stake of at least 95 percent to carry out squeeze-out transactions. The takeover law is expected to come into effect in the first quarter of 2001.

The fight against money laundering

From a legal point of view, the European Commission's proposal for an amendment of Money Laundering Directive 91/308/EEC dominates the discussion in Germany at present on further measures to combat money laundering. To support the practical measures taken by banks to prevent money laundering, the central associations of the German banking industry, working together within the *Zentraler Kreditausschuss (ZKA),* are revising their *Guidelines for combating money laundering*, which are designed, above all, to help money laundering compliance officers carry out their duties. New measures to reliably identify customers in electronic banking are also being discussed.

Tax developments

In July 2000, a sweeping income and corporation tax reform (*Tax Reduction Act*) was passed, providing for a cut in tax rates and the reform of business taxation. The bill abandons, with effect from 2002, the existing imputation system of corporation tax on joint stock corporations and their shareholders in favor of a definitive 25 percent flat-rate corporation tax on retained and distributed profits in conjunction with income tax payable on 50 percent of shareholders' dividends. Capital gains from the sale of shares in corporations will be tax exempt for corporations, while for individuals only 50 percent of the capital gain will be subject to tax. Another key feature of the reform is a phased reduction in the top rate of income tax from 50 percent to 42 percent.

Regulation and supervision of non-domestic banking organizations

Under German banking law, the term "banking" covers both commercial and investment banking services. The commencement or expansion of business which is not banking business in this sense by a bank domiciled abroad is not subject to any separate supervisory examination either at individual bank level or at global entity level. The commencement of non-banking business must be notified to the authorities if the anticipated annual turnover from such business exceeds DM 500,000.

If a bank that is domiciled abroad operates a branch in Germany which conducts banking business, the branch is deemed to be a bank. The minimum capital endowment requirement of € 5 million for banks applies accordingly. There are no further requirements in the form of an asset pledge.

Where branches of banks from other European Economic Area countries are concerned, home-country licensing is recognized.

HONG KONG

Legislative Reform of the Securities and Futures Market

The Securities and Futures Bill (the "composite Bill") was published as a draft Bill on April 7, 2000. Major proposals to be introduced in the Composite Bill were the subject of consultation in July 1999. Following the publication of the Bill, a further period of consultation took place from April to June 2000. It is anticipated that the Composite Bill will be introduced into the Legislative Council in Hong Kong before the end of 2000 and be enacted by April 2001.

The Composite Bill will bring together statutory provisions governing the securities and futures industry currently scattered over ten different Ordinances. In addition to consolidating existing legislation, the Composite Bill introduces a number of important provisions to bring the legislative framework up to date and on par with international standards, including:

(a) a change from a multi-registration regime for intermediaries to a requirement for a single license to engage in activities regulated by the Securities and Futures Commission;

(b) a fuller range of disciplinary sanctions for improper conduct by intermediaries;

(c) tightening of the disclosure threshold and time limits for disclosure of interests in securities;

(d) the introduction of s statutory private right of action against market misconduct and the provision of false information;

(e) the introduction of a Market Misconduct Tribunal to handle insider dealing and other specified market misconduct;

(f) adequate tools for inquiries into the management of a listed company;

(g) immunity for auditors who choose to report suspected fraud;

(h) a flexible and pragmatic approach to regulation of automated trading services;

(i) provisions to enhance transparency in the professional investor markets, including large position reporting requirements in the futures and options markets;

(j) allowing the Securities and Futures Commission to join in litigation between third parties; and

(k) the introduction of a new investor compensation scheme.

The Composite Bill will seek to minimize regulatory overlap for authorized institutions, which are subject to prudential regulation by the Hong Kong Monetary Authority and the Securities and Futures Commission. The Composite bill provides for exemptions from the need to be licensed and introduces a new provision allowing the Securities and Futures Commission to rely upon the Hong Kong Monetary Authority to supervise and regulate certain exempt authorized financial institutions.

Prior to the introduction of the Composite Bill, legislation amending securities margin financing, short selling and provision of false information has been enacted in 2000.

Interbank Clearing Arrangements

Two important changes are being made to the system for clearing and settlement of interbank payments:

(a) A clearing system is to be established in Hong Kong for the clearing and settlement of payments in U.S. dollars. The new clearing system, which will be launched in August 2000, largely replicates the existing system with the clearing being handled by the existing clearing organization, Hong Kong Interbank Clearing Limited. However, an important difference will be that settlement will be effected across the books of The Hongkong and Shanghai Banking Corporation Limited. The existing settlement arrangements for the Hong Kong dollar clearing involves settlement across the books of the Hong Kong Monetary Authority.

(b) The existing real time gross settlement system for Hong Kong dollar interbank payments is now open to restricted license banks.

Merger of the Exchanges and Clearing Houses

On March 6, 2000, the five exchanges and clearing houses were brought together under common ownership by a single operator with the formal establishment of the Hong Kong Exchanges and Clearing Limited, a public company that plans to list on the Hong Kong Stock Exchange later. The Exchanges and Clearing Houses (Merger) Ordinance, effective from March 6, 2000, provides a new regulatory framework for the operation of the Hong Kong Exchanges and Clearing Limited to ensure an appropriate balance between its commercial objectives and public functions.

Virtual Banks

The Hong Kong Monetary Authority has issued a Guideline regarding the establishment and authorization in Hong Kong of virtual banks (a "virtual bank" is one that delivers banking services primarily through the Internet).

The Guideline provides that, for virtual banks to be authorized to conduct banking business in Hong Kong, they must:

(a) satisfy the same prudential criteria which apply to normal banks;

(b) maintain a physical presence in Hong Kong;

(c) maintain a level of security which is appropriate to the type of business which they intend to conduct;

(d) put in place policies and procedures to deal with risks to which they are subject;

(e) present a business plan which strikes an appropriate balance between the desire to build market share and the need to earn a reasonable return on assets and equity;

(f) set out in their terms and conditions for service what the rights and obligations of customers are; and

(g) in respect of outsourcing their data processing operations, observe the guidelines of the Hong Kong Monetary Authority on outsourcing.

Locally incorporated virtual banks must be existing locally incorporated banks and should be at least 50 percent owned by a well established bank or other supervised financial institution.

Overseas incorporated virtual banks must be from countries with a regulatory framework for electronic banking, must have total assets of more than US$16 billion, must comply with the three-building condition (which limits their physical – but not electronic – presence in Hong Kong to three branches), and must maintain books and records in Hong Kong.

Corporate Governance of Locally Incorporated Financial Institutions

The Hong Kong Monetary Authority has issued a detailed Guideline on corporate governance of locally incorporated authorized institutions. This Guideline provides a detailed set of rules regarding the responsibility of the board of an authorized institution, responsibility of individual directors, the use of internal and external auditors, establishment of procedures to manage risks, policies towards connected lending, control over the influence of controlling shareholders, attendance at board meetings and establishment of board committees.

Year 2000 Date Change

Hong Kong financial markets entered into the new millenium smoothly. No major disruptions were encountered by the financial institutions in Hong Kong. The successful entry into 2000 was the result of months of extensive preparations and close cooperation between the regulators and the market participants.

Relaxation of the One-Branch Policy for Foreign Banks

The one-branch policy applicable to foreign banks authorized after 1978 was relaxed in September 1999. Foreign banks subject to this policy are now allowed to operate three branches rather than one. This measure has provided these banks with greater flexibility in doing business. The Hong Kong Monetary Authority will consider further relaxation of this policy upon a review in early 2001.

The Insurance Companies (Amendment) Bill 2000

Notice of the Amendment Bill was published on January 14, 2000. It is proposed:

(a) to allow the Insurance Authority to disclose financial and statistical information of individual insurers and Lloyd's if, in its opinion, it is in the public interest to do so; and

(b) to require appointed actuaries or insurers to comply with the prescribed or other compatible standards.

Insurance Intermediaries Quality Assurance Scheme

The Insurance Intermediaries Quality Assurance Scheme has been implemented with effect from January 1, 2000 to enhance the professional standard of insurance intermediaries by requiring them to pass a qualifying examination, unless otherwise exempted, before they can be registered or authorized as such. Thereafter, they need to attend continuing professional development programs as a condition for renewal of their registration or authorization.

Supervision of Non-Domestic Banking Organizations

In the case of an institution incorporated outside Hong Kong, the primary responsibility for supervising capital adequacy rests with the home country supervisor. In arriving at an assessment of an institution's financial strength, the Hong Kong Monetary Authority will take the views of the home country supervisor into account but may also wish to make an independent assessment. The Hong Kong Monetary Authority will generally require an overseas bank which wishes to set up a branch in Hong Kong to have a total risk-based capital ratio of at least 8 percent measured in a manner consistent with the Basel Capital Accord.

Generally, the Hong Kong Monetary Authority accepts the calculations of the capital adequacy ratio based on the methodology of the home supervisor, provided that this is consistent with the various national variations allowed under the Basel Capital Accord. However, the Hong Kong Monetary Authority reserves the right to require the ratio to be recalculated on the basis of the methodology used in Hong Kong to ensure that it is not overstated.

While the Hong Kong Monetary Authority regulates the liquidity, large exposures, provisions and other matters relating to the Hong Kong branches of non-domestic banking organizations, it does not impose on them any type of asset pledge requirement.

INDIA

Regulation of the Financial Sector

Establishment of an Insurance Regulatory Authority

In India, all commercial banks and non-bank finance companies are regulated by the Reserve Bank of India (RBI). Capital markets activities are supervised by the Securities Exchange Board of India (SEBI). Pursuant to legislation enacted in January 2000, a new agency – the Insurance Regulatory and Development Authority (IRDA) – has been established to regulate the insurance sector and promote and ensure its orderly growth. This legislation also seeks to open up the insurance sector to foreign and private investors.

Bank Regulatory Developments

In October 1999, the RBI reduced the Cash Reserve Ratio (CRR) from 10 percent to 9 percent. In April 2000, the RBI instituted a number of other measures to give more flexibility to commercial banks:

- the CRR was further reduced to 8 percent;
- the bank rate, which is the benchmark for various refinance facilities was reduced from 8 percent to 7 percent;
- the repo rate was reduced from 6 percent to 5 percent; and
- the savings deposit rate, which is the only rate still regulated by the RBI, was reduced from 4.5 percent to 4 percent.

With a view to tightening liquidity and ensuring stability in the value of the rupee, the RBI subsequently announced the following measures:

- a two-step increase in the CRR from 8 percent to 8.5 (the rate increased to 8.25 percent effective July 29, and to 8.5 percent effective August 12);
- an increase in the bank rate from 7 percent to 8 percent effective July 21; and
- a temporary reduction in all refinance facilities available to banks by 50 percent of eligible limits.

The RBI has introduced various measures to develop the money market. Rupee derivative products have been introduced, and permission for non-bank entities to operate in the call/notice money market through primary dealers was extended to June 30, 2000. Authorization has been given for the establishment of money market mutual funds (MMMFs) so long as they are organized only as trusts. To provide more information on the volume of transactions, the RBI proposes to develop, in consultation with market participants, modalities of releasing on a daily basis, data on the volume and rates in the call money market as well as some other relevant data.

In April 1999, the RBI established a Regulation Review Authority (RRA) to determine which (if any) of the RBI's regulations and procedures are considered unnecessary or overly burdensome by banks, market participants, foreign investors, non-resident Indians (NRIs), Indian citizens and experts.

Effective March 31, 2000, the minimum risk-based capital adequacy ratio increased from 8 percent to 9 percent. The RBI has established an internal committee to assess the impact of the Basel Committee's proposed "New Capital Adequacy Framework" and consider its applicability in the Indian situation.

A plan for revival of weak banks on the basis of revival plans prepared by each bank is in progress.

With regard to supervisory matters, recent years have witnessed a gradual shift towards deregulation, reinforced by the introduction of prudential norms and the adoption of international supervisory best practices as articulated by the Basel Committee. Considering the complexities in the banking business as well as the emergence of new products, there is a growing acceptance that a risk-based supervisory approach would be more efficient than the traditional transaction-based approach. The RBI is planning to adopt a risk-based supervisory approach in due course after observing the experience of other countries which have already adopted this method of supervision.

The RBI has issued comprehensive guidelines to enable banks to put in place appropriate risk management systems for credit risk, market risk and operational risk. Under these guidelines, a bank's board of directors should include in the bank's loan policy prudential limits regarding, among other things, the bank's exposure to a single borrower, a group of borrowers, particular industries and sensitive sectors of the economy.

The high level of bad loans is one of the major problems faced by the public sector banks. To address this situation, the Government has set up Debt Recovery Tribunals (DRTs) to adjudicate loan disputes and Settlement Advisory Committees (SACs) to facilitate compromise in the settlement of chronic non-performing assets, particularly in the small enterprise sector. In addition, the powers of the chairman and managing director of public sector banks to waive/write-off bad loans has been raised from Rs.1 million to Rs. 5 million.

Year 2000 Date Change

As a result of its intensive preparations, the Indian banking and financial sector did not encounter any significant problems in connection with the Year 2000 date change (banks were closed to the public on January 1).

Regulation of Non-Bank Financial Companies (NBFCs)

In January 2000, the RBI amended and clarified certain directives relating to the regulation of NBFCs. Some of the important regulatory amendments include the following:

- Mutual benefit companies (MBCs) in existence as of January 9,1997 and having net own funds (NOF) of Rs.1 million would be exempted from both the requirements to register, maintain liquid assets and create a reserve fund and the provisions of NBFC directives regarding the acceptance of public deposits and application of prudential norms which do not apply to notified nidhi companies.

- Of the 15 percent of public deposits required to be invested in liquid assets, NBFCs are permitted to maintain up to 5 percent in term deposits with scheduled commercial banks.

- To ensure the continuity of their certificates of registration, all NBFCs are required to furnish to the appropriate Regional Office of the RBI the details of the permanent account [taxpayer identification] number issued by the Income Tax Authorities to each of their directors. However, commencing with the quarter ended December 1999, an NBFC not holding public deposits need not furnish to the RBI a statement of business activities and the prudential norms it observes.

In the case of insurance companies, several initiatives are in progress, including the establishment of the IRDA (see above), measures to promote efficiency in the conduct of the insurance business, efforts to promote and regulate professional organizations connected with the insurance and reinsurance business, and revisions to rate regulation.

Developments in the Capital Markets

In August 1999, the Securities and Exchange Board of India (SEBI) relaxed the listing norms for Information Technology (IT) companies by reducing the minimum requirement for a public offering from 25 percent to 10 percent of an IT company's shares. In addition, IT companies are required to issue at least Rs.2 million (20 lakh) of securities to the public (excluding reservations, firm allotments and promoters' contributions). The size of the net offer to the public (i.e., the offer price multiplied by the number of securities offered) should be at least Rs.500 million (50 crore).

In December 1999, SEBI introduced rolling settlement on certain securities – specifically, uncertificated securities that have a daily turnover of at least Rs.1 crore. There will be no new margin requirements, exposure limits or price bands for trading in these securities.

The Government has liberalized the norms for overseas acquisitions by domestic software companies by providing for automatic approval for acquisitions up to $100 million by Indian companies listed abroad. In addition the limit on funding of such overseas acquisitions from the proceeds of either GDRs or ADRs has been increased from 50 percent to 100 percent.

SEBI has banned the disclosure of financial results of companies during market hours and has directed stock exchanges to immediately put any information from a company received under the listing agreement on the Internet. The information provided in balance sheets should include more details on expenditure incurred.

Market Developments

Two new private sector banks – HDFC Bank Ltd and Times Bank Ltd – merged in February 2000.

Payment Systems Developments

Efforts are continuing to introduce RTGS (Real Time Gross Settlement) in India.

Effective July 1, 2000, SWADHAN, the Shared Payment Network System, operates throughout India, having previously been limited to Mumbai.

Over the past years, the RBI has developed two electronic payment systems: Electronic Fund Transfer (EFT) and Electronic Clearing Services (ECS). EFT permits banks to offer their customers money transfer service across their own branches as well as with branches of other participating banks. The EFT system presently covers all the branches of the 27 public sector banks and 8 scheduled commercial banks at the four metropolitan centers (Calcutta, Chennai, Mumbai and New Delhi). Funds transfer is possible from any branch of a participating bank to any other branch both within and between these cities.

ECS-Credit Clearing is a mode of payment whereby an institution having to pay interest, dividend, salary, pension to a large number of investors/shareholders/employees/ex-employees can make the payments electronically instead of issuing paper warrants. This scheme is operational in 46 cities in India.

ECS- Debit Clearing permits customers to authorize utilities, insurance companies, credit card companies and finance companies to debit their accounts on the due date in the amount owed on telephone/ electricity bills, insurance premiums or periodic installments. This scheme is available through the RBI at 15 centers.

To facilitate banks' efforts to introduce appropriate schemes in issuing electronic cards as a means to ease pressure on the demand for cash, the RBI published Guidelines regarding the issuance of debit cards and smart cards.

Regulation of Non-Domestic Banking Organizations

All banks in India, whether domestic or non-domestic in their origin, must maintain reserves with the RBI in accordance with the Cash Reserve Ratio and the Statutory Liquidity Ratio. To open a branch in India, a non-domestic banking organization must commit the following minimum amounts from their own resources: $10 million to open each of the first two branches and $5 million to open a third branch. However, non-domestic banking organizations that maintain branches in India are not subject to any type of asset pledge requirement.

Non-domestic banking organizations may commence nonbanking activities in India either directly or in partnership with an Indian company. The prior approval of the Foreign

Investment Promotion Board (FIPB) is required in either case. Once the approval of the FIPB is obtained, the local operation is regulated by the appropriate authority with jurisdiction over its activities (e.g., the RBI, SEBI or IRDA).

INDONESIA

The Central Bank/Bank Indonesia

Under the new central bank law, Bank Indonesia (BI) is given an independent status, free from government intervention. With its main objective achieving and maintaining the stability of the rupiah, BI is responsible for formulating and implementing monetary policy, regulating and safeguarding the operation of the payments system as well as regulating and supervising banks. In fulfilling its role, the central bank's activities include issuing currency, management of foreign exchange reserves, maintaining domestic liquidity and ensuring the integrity of the banking system.

As to monetary policy, BI is authorized to establish monetary targets and control the money supply. The instruments used for this purpose include open market operations and the setting of the discount rate and minimum reserve requirements.

The central bank law limits BI's role as lender of last resort. BI may lend only short-term (maximum maturity of 90 days) credit that is covered by high-quality collateral. Such credit will be made available only to banks that face genuine liquidity problems. The law prevents the central bank from providing credit to the government in order to prevent financing budget deficits through the printing of money.

In regulating and supervising banks, BI has the power to grant and revoke bank licenses, approve bank ownership and management and determine the scope of an individual bank's permissible business activities. The central bank's supervisory function is to be transferred to a new independent supervisory board that is intended to in operation no later than December 2002. Ultimately, this new "super regulator" will be responsible for supervision of all financial entities, including banks, insurance companies, pension funds, securities firms, venture capital and other investment funds, and asset management firms.

The central bank is headed by a board of governors, composed of a Governor, Senior Deputy Governor and a minimum of four and a maximum of seven Deputy Governors. The Governor and the Senior Deputy Governor are nominated and appointed by the President, subject to approval by the House of Representatives. The Deputy Governors are nominated by the Governor and then appointed by the President, again subject to approval by the House of Representatives. All board members can be discharged only upon their resignation or conviction of a crime.

Indonesian Bank Restructuring Agency (IBRA)

Established in 1998, IBRA has been involved in several projects aimed to restructure the Indonesian banking sector. It is responsible for implementation of the bank recapitalization program. Under this program, all of the state banks and several privately held commercial banks are being recapitalized through the injection of government funds in order to restore their capital adequacy ratios to a 4 percent minimum. For listed banks, the recapitalization had to be done through rights issues, with the former shareholders injecting a minimum 20 percent of the total recapitalization amount. So far, 66 banks have been liquidated, 13 banks have been taken over and 8 private banks have been recapitalized.

As part of the recapitalization agreement, banks have to transfer their bad assets to IBRA's Asset Management Unit (AMU), which is responsible for maximizing recoveries from these assets. The loans are bundled into pools and then sold to investor groups. Some non-core assets controlled by AMU have already been auctioned.

Year 2000 Date Change

Reflecting extensive preparatory efforts throughout the financial sector, no significant problems were experienced in connection with the Year 2000 date change.

Market Developments

Following a favorable determination by IBRA as to its condition, Bank Central Asia, the largest private commercial bank nationalized by the government in May 1998, listed its shares on the Jakarta Stock Exchange in May 2000.

In August 1999, Bank Mandiri, a state bank, was created from the merger of Bank EXIM, Bank Bumi Daya, Bank Dagang Negara and BAPINDO. As a result of the merger, Bank Mandiri has become the largest bank in Indonesia in terms of assets.

It is anticipated that sometime in the middle of 2000 several private commercial banks taken over by IBRA will be merged into Bank Danamon. The merged banks are: Bank Tiara Asia, Bank Duta, Bank Jaya International, Bank Nusa Nasional, Bank Pos Nusantara, Bank Rama, Bank Risjad Salim International and Bank Tamara.

Branches of Non-Domestic Banking Organizations

Non-domestic banking organizations are permitted to open branches in Indonesia if:

- they are among the 200 largest banks in the world, as measured by total assets;

- they are found to have a good reputation and hold at least an "A" rating from a reputable international rating agency; and

- they maintain branch capital of at least Rp 3 trillion.

IRELAND

Supervision of Financial Institutions

Introduction

The Central Bank of Ireland supervises a wide range of financial institutions. Responsibility for the authorization and ongoing prudential supervision of credit institutions is discharged by the Banking Supervision Department. The supervision of entities other than credit institutions, including the Irish Stock Exchange, stockbrokers, moneybrokers, investment intermediaries, various entities in the International Financial Services Center, futures exchanges and collective investment schemes, is carried out by the Securities and Exchanges Supervision Department and the IFSC and Funds Supervision Department.

Banking Supervision

The Central Bank of Ireland is the licensing authority for all credit institutions incorporated in the State and for branches of credit institutions from outside the European Economic Area. The Bank derives its supervisory powers from the Central Bank Act, 1971, 1989, 1997 and 1998; the Building Societies Act, 1989; the Trustee Savings Bank Act, 1989; the ACC Bank Act, 1992; the ICC Bank Act, 1992; and, to an increasing extent, from various EU Banking Directives.

In addition, the Bank has formulated non-statutory Licensing and Supervision Requirements and Standards for Credit Institutions, which it applies to all license holders.

Developments Regarding the Regulation and Supervision of Credit Institutions

In accordance with the EU Directive on Deposit Guarantee Schemes (94/19/EC), the maximum level of cover available to a depositor under the Irish deposit protection scheme, in the event of a bank being unable to repay deposits, was increased from Euro 15,000 to Euro 20,000 with effect from December 31, 1999.

The Directives amending the Capital Adequacy Directive (CAD I), the Solvency Ratio Directive and the First Banking Directive, which were published by the EU Commission in July 1998, will be implemented for credit institutions during 2000. Banks are not permitted at this time to use internal models in the calculation of capital requirements for market risks, other than in the form of pre-processing models permitted under CAD I. It is proposed to permit the use of these models in Ireland during 2000 following the implementation of CAD II.

The Bank coordinated the Irish response to the EU Consultation Paper on a Review of Regulatory Capital requirements for EU Credit Institutions and Investment Firms.

Developments in the Banking Sector

One banking license (Sachsen LB Europe plc) was approved and issued during the period under review. Three licenses were revoked at the request of the license holders: Caterpillar

International Bank plc in August 1999; GE Capital Woodchester Bank Limited in April 2000, following transfer of its business to the Irish branch of Investec Bank (UK) Limited; and Eurohypo European Mortgage Bank plc, following transfer of its business to the Irish branch of Europaische Hypothekenbank S.A.

The Department continued to monitor the growth in private sector credit and requested credit institutions to carry out sensitivity analyses on their financial position assuming various hypothetical scenarios depicting a severe economic downturn and tight liquidity conditions. The results of the surveys showed that all institutions could sustain the impact of the adverse economic conditions outlined in the hypothetical scenarios and that institutions were aware of the potential difficulties which could arise in the event of an economic downturn.

All institutions were advised in September 1999 that they should have, within their internal control systems and strategic planning process, the facility to carry out sensitivity analyses on their financial position.

Securities and Exchange Supervision; IFSC and Funds Supervision

Apart from credit institutions, the Central Bank of Ireland is also responsible for the supervision of a wide range of non-bank financial institutions. Up to the end of 1999, the Securities and Exchanges Supervision Department carried out this responsibility. In response to the significant increase in the number of non-bank financial institutions supervised by the Bank, a new supervision department has been established within the Bank.

The Central Bank's responsibility for the supervision of non-bank financial institutions is derived from various pieces of legislation:

- The Investment Intermediaries Act, 1995 (as amended by the Central Bank Act, 1997 and the Investor Compensation Act, 1998), provides for the authorization and supervision of investment firms; the Stock Exchange Act, 1995, provides for the approval of stock exchanges and the authorization of their member firms and the ongoing supervision of such exchanges and member firms. (The Bank does not have a role in relation to listing requirements or insider dealing requirements for members of the Irish Stock Exchange; the Exchange itself undertakes these functions.) Both these pieces of legislation transpose the obligations of the EU Investment Services Directive, the key element of which is that once an investment firm has been authorized to undertake investment business by the competent authority in the Member State in which it has its head office, that firm can carry on the business covered by their authorization throughout the EU (either directly or through branches) without seeking further authorization in that other Member State. In such circumstances, the firm is required to comply with the conduct of business rules and advertising requirements applying in the host country.

- Under the Central Bank Act, 1989 (as amended by the Central Bank Act, 1997), the Bank supervises certain institutions operating in the International Financial Services Center (IFSC). However, many of these IFSC firms are now regulated under the Investment Intermediaries Act, 1995, as investment firms and the remaining firms regulated under the

1989 Act comprise mainly of futures brokers. Two Futures Exchanges operating in the IFSC are regulated under a separate section of the Central Bank Act.

- The Bank is also responsible for the authorization and supervision of collective investment schemes established under the European Communities (Undertakings for Collective Investments in Transferable Securities) Regulations, 1989 (UCITS Regulations), the Unit Trust Act, 1990, Part XIII of the Companies Act, 1990, and the Investment Limited Partnerships Act, 1994.

In addition to the legal requirements imposed under the various pieces of legislation, the scope of the detailed supervisory requirements imposed on individual firms depends on the Bank's assessment of, among other things, the prudential risk involved, the nature of the activities of the firm, the status of the owners and the experience and expertise of the management. The typical supervisory framework includes the submission to the Bank of financial and other information on a regular basis, together with on-site inspections and meetings to review firms' operations and their compliance with the Bank's requirements. Such requirements include:

- general requirements which apply to all firms;
- capital requirements;
- advertising requirements;
- conduct of business rules;
- client asset requirements; and
- anti-money laundering guidance notes.

In particular, the advertising requirements and the conduct of business rules require regulated firms to disclose all relevant information to their clients. These rules seek to ensure that clients are dealt with in a just and equitable manner according to the standards set down in these rules.

Securities Regulation Developments

The Insurance Bill 1999, which proposes to transfer responsibility for the authorization and regulation of Insurance Intermediaries to the Central Bank, was published in December 1999. It is now at an advanced stage in the legislative process and is expected to pass all stages before the summer 2000 recess.

Developments Affecting Financial Institutions Supervised by the Central Bank

Year 2000 Date Change

As part of its ongoing process of monitoring the Year 2000 preparedness of regulated entities, the Bank issued and assessed a number of questionnaires to regulated entities over the past two years. These questionnaires focused on areas such as identifying systems requiring changes, testing timetables and contingency planning measures. Year 2000 issues formed part of the subject matter of all review meetings with senior management of credit institutions and the Bank also conducted focused Year 2000 preparation inspections on a sample basis.

The Bank established a Central Communication Point, which operated over the millenium changeover, monitoring the financial sector and liaised with government and international bodies.

Regulated entities were asked to submit a status report in January 2000 confirming that no problems had been encountered with the century changeover. These status reports indicated that the changeover went smoothly and problem free.

Anti-Money Laundering Developments

The Anti-Money Laundering Guidance Notes, issued with the approval of the Money Laundering Steering Committee of the Department of Finance in April 1995, are under review and proposed amendments will be brought before the Steering Committee for approval during 2000.

At the EU level, discussions are continuing regarding revisions to the EU Directive on the prevention of the use of the financial system for the purpose of money laundering which will, *inter alia*, extend the scope of the Directive to other persons such as solicitors, accountants and real estate agents.

Developments Affecting the Supervisory Function of the Central Bank of Ireland

Three separate reviews of supervision have taken place in recent times. First, the Financial Action Task Force undertook a mutual evaluation of Ireland in April 1998 to assess the effectiveness of legislation and systems in place in Ireland to combat money laundering. Their report was issued in July 1999. It concluded that Ireland has put in place a comprehensive and very solid legislative scheme for combating money laundering and that the Bank has taken an active approach regarding the institutions it supervises.

Secondly, on February 2, 2000, the Comptroller and Auditor General published a report on the Bank's role in relation to financial regulation following an examination which took place during 1999. This report is entitled "Report on Evaluation and Effectiveness: Central Bank Financial Regulation".

Finally, the International Monetary Fund carried out a large-scale assessment of the Bank's performance as a supervisor. This assessment was part of a pilot exercise relating to financial stability. The objective was to identify strengths and weaknesses in the financial system.

Payment Systems Developments

Under the Central Bank Act, 1997, the Bank was given a statutory role in relation to the regulation of payment systems. The provisions of this Act require all payment systems to be approved, and have their rules vetted, by the Bank. The Bank may impose conditions on approval, revoke approval and issue directions to the system or its members. Specifically, in approving rules, the Bank must have regard to the equity and openness of the system.

The definition of a system in the Act encompasses the "clearance and settlement of any means of payment or of any securities." The regulatory role extends, therefore, to securities settlement systems. The Act states that actions by the Bank relating to conditions/requirements imposed on a system shall be "as the Bank sees fit in the interest of the proper and orderly regulation of the payment system concerned and of competition between payment systems." Moreover, in relation to the possible exemption of payment systems, it is stated, more generally, that any such exemption from some or all of the requirements may be made where the Bank is "of the opinion that it is not necessary in the interest of the proper and orderly regulation of financial transactions in the State."

The general objective of the regulatory regime reflects, therefore, the Bank's concern to ensure that such systems in the State are effective, efficient and open and that the systems themselves do not add to, or cause, instability in the operation of financial markets.

In 1998 an amendment to the 1997 Act was implemented to ensure that the Bank's ESCB-related involvement in payment systems would not be prejudiced by the Bank having to have the consent of the Minister of Finance prior to its refusal to approve the rules of a payment system or subsequently revoke such approval (this provision is contained in Section 28 of the Economic and Monetary Union Act, 1998).

Within this regulatory framework, the payments system has the following operational characteristics:

- Large-scale interbank payments are made on a real time gross settlement (RTGS) basis since March 1997. All lending (e.g., overdrafts/provision of liquidity) to participants in this system is fully collateralized. The RTGS system in Ireland (IRIS) is fully integrated into the TARGET system, which facilitates cross-border payments in euro on an RTGS basis.

- There is no large-value netting system in Ireland.

- A reform of the retail clearing mechanisms is underway which will include legal agreements specifying obligations and responsibilities. It is anticipated that this reform will be completed during 2000.

- The legal underpinning for the current settlement system for gilts is based on assured payment agreements and a system of "settlement banks". The system is run by the Central Bank. However, it is scheduled to move to Euroclear in mid-2000.

- Settlement for Irish equities in euro is effected via the CREST mechanism (a UK-based system).

ISRAEL

Developments Regarding the Regulation and Supervision of Banks

Virtually all Israeli banks have weathered well the economic slowdown of the years 1997-1999. Their profitability has improved in most cases, and the provisions for doubtful debts have not increased. However, banks' risk exposures have grown as a result of the liberalzation in the control of the foreign exchange market, the expanding use of derivative financial instruments and the volatility of the international financial markets.

These developments have led the Supervisor of Banks to tighten the regulations relating to capital adequacy and risk management. Following the raising of the minimum risk-adjusted capital ratio from 8 to 9 percent in March 1999, the Supervisor has issued several amendments to existing directives and a major new directive relating to the allocation of capital to cover specific market risks. The amended directives:

- limit the volume of credit granted to finance the acquisition of controlling interests in other banking corporations to a ceiling of 5 percent of the capital of the acquired bank or of the financing bank, whichever is less; and

- require an additional provision for doubtful debts in cases of excessive concentration of credit risks in certain industries or categories of borrowers.

Issued in April 1999, these amendments gave banks that were in breach of the new rules an adjustment period until 2005.

Additional new directives issued in December 1999 introduced a third layer of capital – Tier 3 capital – that may be used to supplement Tier 1 and Tier 2 capital in case of shortage created by the new requirements to allocate capital to cover specific market risks. Tier 3 capital consists of subordinated capital notes of a minimum average duration of two years, the repayment of which is subject to the condition that such repayment will not lower the bank's capital ratio below the required minimum.

The new capital allocation directive includes very detailed specifications of methods to estimate risk exposures to changes in interest rates and stock prices of the bank's securities portfolio as well as risk exposures to changes in the rate of exchange and in the general price level.

The directive covers the proper treatment of options held by the bank and the use of internal models for estimating the exposure to market risks. It also specifies the required allocations of capital to cover each of the foregoing exposures.

Banks will have to devote substantial management resources in order to prepare the risk management tools and the control systems that will be needed to ensure compliance with the directives related to management of risks. It is also possible that additional capital resources will be required to satisfy the minimum capital ratio following the additional, risk-related allocations.

Year 2000 Date Change

There were no disruptions in the systems and activities of Israeli financial institutions as a result of the Year 2000 date change. Substantial resources were invested in preparing the systems, and the results justified the efforts.

The Regulation of Insurance and of Retirement Funds

The Treasury's plan to change the existing arrangements for the insurance of victims of motor vehicle accidents that was scheduled to take place on January 1, 2000 was postponed until at least January 1, 2001. The exact model of "regulated competition" has not been elaborated yet and there are doubts whether it will reduce the overall cost of this category of insurance.

After withdrawing the bill relating to the regulation of provident funds (retirement funds) in early 1999, the Government nominated a committee headed by the Director General of the Ministry of Finance to re-examine the issue of the banks' role in the management of pr ovident funds. (The three large banks and their subsidiaries manage more than two thirds of the money invested in these funds.) The committee recommended limiting the market share of each banking group to no more than 10 percent. The implementation of this recommendation seems quite problematic and it may further delay legislation aimed at regulation of an important segment of the retirement funds market.

The Scope of Permissible Affiliations of Banks and Other Financial Firms

There were no important developments in this area during the period covered by this report, but the recommendation mentioned above to limit the share of the large banking groups in the management of retirement funds reflects the opinion of the regulatory authorities (the Bank of Israel and the Ministry of Finance) that the degree of concentration of the Israeli banking system is too high and that the large banking groups are too powerful. It is too early to predict whether this view will prevail and how it will translate into actual legislation.

Electronic Banking and the Internet

Israeli banks in recent years have invested very substantial resources in developing and upgrading their computer systems and communication capabilities, including Internet sites, and are now gradually expanding the online facilities made available to their customers. Besides supplying both account and general financial information electronically, the banks enable customers to execute various types of transactions, such as buying and selling securities. The scope of services that the banks are allowed to offer (e.g., the transfer of funds from one account to another) is determined by the Supervisor of Banks on a case-by-case basis.

Anti-Money Laundering Initiatives

The "Prohibition of Money Laundering Law" is expected to go through the third and final reading in the Knesset during the first week of August 2000. The law defines money laundering itself (namely, the performance of transactions with property which originates from a list of specified offenses, in order to conceal or disguise its origin) as a criminal offense. A person who has committed this offense is liable to ten years imprisonment. The law also prohibits transactions with property connected to an offense, and a person who has knowingly performed a transaction with such property will be liable to seven years imprisonment or to a fine.

Providers of financial services will have to report on transactions performed by their customers. The reporting requirements will be specified in an order to be issued by the Governor of the Bank of Israel after consultation with the Ministers of Finance, Justice and Internal Security.

On June 22, 2000, the Financial Action Task Force on Money Laundering (FATF) issued a reporting naming Israel as one of 15 jurisdictions that FATF has determined have not taken adequate measures to combat international money laundering. It is anticipated in Israel that passage of the anti-money laundering legislation described above will lead to Israel's removal from the FATF list.

Supervision of Non-Domestic Banking Organizations

Israeli legislation does not discriminate against non-domestic financial institutions, and the attitude of the regulatory authorities toward these institutions is quite hospitable. The number of non-domestic firms present in the Israeli market has thus far been limited, but it is growing. In what may become a breakthrough, Citigroup and, more recently, HSBC decided to open full-fledged branches in Israel, and it is expected that other banks, securities firms and insurance companies will follow suit, especially in the wake of the liberalization of Israel's foreign exchange regime.

Significant Developments in the Financial Markets

In early May 2000, an experts committee, headed by the Director General of the Ministry of Finance, submitted to the Government a report on income tax reform. A major recommendation of the report is to tax both current income and capital gains from many financial assets that have been exempt from tax until now. The implementation of this reform, which must still clear some substantial political obstacles, will modify the relative attractiveness of some important instruments – for example, reducing the net return on time deposits with banks and equalizing the burden of taxation on domestic and foreign securities (the former being exempt until now from capital gains tax). It is too early to predict the exact impact of such a reform on the future development of thc Israeli capital market, but it will certainly be significant.

Finally, it is worthwhile to mention that the Government is considering changes in the method of bank privatization that has been pursued until now. The sale of a controlling interest to an identified investor, or group of investors, is encountering difficulties in the cases of Bank Leumi and Discount Bank, two of the three largest Israeli banks. Completing the privatization of thc banks acquired by the Government following the bank shares crisis of 1983 may require more reliance on sales of smaller blocks of shares in the market, both in Israel and abroad.

ITALY

Bank Regulatory Developments

During the period under review, the Bank of Italy released the revised version of its supervisory instructions, incorporating the capital adequacy rules laid down by the Basel Committee and the European Commission (Directives 98/31/EC and 98/32/EC). Specific changes were:

1. extension of the 50 percent risk weighting category to include mortgage loans on non-residential properties, real property leases intended for business purposes and other financial instruments secured by mortgages (effective March 1999);

2. permission for banks to use internal models for calculating capital ratios vis-à-vis market risk (effective March 2000);

3. eligibility of preference shares for inclusion in banks' capital base (effective July 1998);

4. revision of the standardized methodology for calculating capital requirements to take into account commodities position risk and the introduction of new methodologies for treating options;

5. lowering to 20 percent the risk weighting for exposures to real estate investment firms;

6. requiring use of the current value method in calculating the "credit equivalent" for currency and interest rate derivatives.

The changes cited under points 4, 5 and 6 go into effect on December 31, 2000.

As to accounting rules for banks, measures were introduced governing changes in accounting practices and deferred taxation, on the basis of the provisions of international accounting standards IAS 8 and IAS 12.

Law 526/1999 delegates power to the Government to transpose the EU Directive on settlement finality into Italian law by the end of 2001.

Year 2000 Date Change

Thorough and intensive preparations were undertaken in Italy in connection with the Year 2000 date change, particularly with regard to the banking and financial system. Listed in their order of succession, these preparations included verification of the following : the regular completion of end-year data processing; the normal operation of ATM, POS and credit card circuits; the reactivation of the central bank's information system with the January 1, 2000 date and confirmation of EDP links; the regular functioning of the national interbank network, the Bancomat ATM system and of banking and financial intermediaries; the correct resumption of computer connections with international payment systems and the settlement of interbank payments with an accounting date of January 3, 2000; the full operation of the branches of the Bank of Italy, of all the financial markets (stock exchange, screen-based government securities, interbank deposit, futures, financial futures, and options markets), of the entire real-time interbank wholesale payment cycle with final settlement on central bank accounts (BI-REL) and of gross settlement between central banks (TARGET); the correct settlement of securities transactions in central depositories; correct settlement in clearing systems for retail payments (clearing of local items) and of securities transactions; the normal resumption of operations by insurance companies; the regular operation of financial markets together with absence of strains on short-term interest rates; the regular resumption of activities of Bancoposta (postal current accounts, savings books and savings certifications, money orders, postal credit card and Eurogiro).

In the end, no significant problems were experienced in connection with the Year 2000 date change. The successful transition resulted from the considerable resources dedicated by the Italian Government to this strategic problem – including its efforts to identify and publicize the problem, its establishment of a specific and highly detailed strategy to address the problem, its ability to bring all the members of the national community together in the national interest, and the availability of an effective operational apparatus under the Ministry of the Interior for the practical application of government measures and recommendations – in combination with the full cooperation of business enterprises and utilities.

Securities Regulation Developments

Law 139/1999 on loan securitization was passed authorizing for the first time in Italy the use of "special purpose vehicles" (SPVs) in connection therewith, as is the case in the United States and Britain.

The Treasury Ministry issued Decree 228/1999 implementing the Consolidated Law on Financial Intermediation. This liberalizes the creation and operation of hedge funds and broadens the objectives of investment funds to include "all goods susceptible to certain valuation at least once every six months".

On May 15, 2000 trading after hours — when fully phased in, from 17.50 to 22.00, CET — began on the Borsa Italiana S.p.A., the regulated stock exchange for corporate shares.

During 1999, changes were made in the structure of the enterprises that manage the Italian financial markets. Borsa Italiana absorbed the government securities futures exchange (MIF), which it already fully controlled, and took a majority stake in Cassa di Compensazione e Garanzia (the Italian Clearing House). It also established *Nuovo Mercato* (for shares with high growth potential and firms in the "new economy") and the Euro MOT (for eurobonds and asset-backed securities).

Internationally, Borsa Italiana signed a protocol with seven other European bourses (London, Frankfurt, Paris, Brussels, Amsterdam, Madrid and Zurich) for the establishment of a circuit for trading in the blue chips listed in the participating exchanges.

The other Italian market, MTS S.p.A. (the screen-based market in government securities), formed single markets in other countries for trading such countries' domestic government securities, all using the technological platform provided by SIA S.p.A (the Interbank Company for Automation). These markets, at present, are:

- MTS Amsterdam;
- MTS France (operational from April 2000);
- MTS Belgium (operational from May 2000); and
- MTS Japan (established April 2000, operational from 2001).

These markets ultimately will be linked to the platform of Euro MTS (a British company in which MTS Italia has a 75 percent stake), which already allows trading of benchmark government securities of the main European countries (Italy, Germany, France, the Netherlands, Portugal, Finland, and others).

Finally, e-MID S.p.A. was constituted, with the conversion of the former Management Committee into the Board of Directors for the screen-based interbank deposit market, founded in 1989. The company's main task is computerized trading of money market deposits with maturities ranging from overnight to 6 months; it also provides for remote access, which involves the participation of foreign intermediaries in the market from their own country through electronic links to the Italian market.

Anti-Money Laundering Initiatives

Legislative Decree 374 of September 25, 1999 extended the application of current anti-money laundering provisions (Law 197/1991 with its amendments and additions) to other categories of institutions in lines of business that are especially vulnerable to exploitation for purposes of money laundering. These activities comprise credit recovery, custody and transport of cash, securities and valuables with armed guards, commerce in antiquities, auction houses and art galleries, and gambling and gaming houses.

On January 31, 2000, the Italian Foreign Exchange Office (UIC – the authority responsible in this sphere) issued an opinion regarding the identification of customers in distance transactions for the purposes of the formalities that intermediaries must carry out to comply with Law 197/1991 and subsequent amendments. As defined in the opinion, a "distance transaction" is a transaction carried out by means that do not involve the simultaneous physical presence of the customer and the intermediary or its agent, such as a financial salesman. This definition is contained in the same form not only in a number of Italian laws (Article 32 of the Consolidated Law on Financial Intermediation, and Article 1(a) and 1(d) of Legislative Decree 185/1999), but also in Community legislation (Article 2(1) and 2(4) of Directive 97/7/EC of May 20, 1997, and Article 2(a) and 2(c) of the proposed directive concerning the distance marketing of consumer financial services (COM (1999(385)).

In the opinion, the UIC sets forth two methods by which the intermediary can provide a "suitable attestation" that customer identity has been ascertained, both of which are sufficient for the distance identification of persons who carry out transactions involving amounts of more than 20 million lire or who wish to establish a continuing relationship with the intermediary.

Under the first method, the attestation of identity is provided implicitly through the effectuation of a credit transfer by the bank at which the customer has already been identified to the intermediary, which must make the "distance" identification, on the condition that:

- the funds used for the credit transfer are drawn on an account in the customer's name for which the customer has already been identified;

- the intermediary, which must make the distance identification and receive identifying details from the customer, has assigned an identification code to the customer, which the latter must transmit to the bank where the account is held. In turn, the bank must indicate the identification code on the credit transfer to the intermediary; and

- all subsequent transactions are effected through the original account.

The second method provides for the completion of a form, duly signed and sealed by the intermediary providing the attestation, in which the identifying particulars of the customers are given together with those of the identity document used for the identification. This method is considered equally valid by the UIC for the purposes of compliance with anti-money laundering regulations.

The certification by means of the form mentioned above may also be provided by potential customers themselves, which enables them to use means of payment other than credit transfers.

These procedures apply in Italian territory and, as regards cross-border relations, to:

- banks with their legal and administrative head office in FATF member countries (FATF banks), or the branches in these countries of Italian and other FATF banks; and

- Italian and other FATF bank branches located in non-FATF countries, provided that the parent bank states that as far as the business done by these branches is concerned it will abide by the principles of the FATF recommendations.

Developments in Electronic Commerce

As to electronic commerce and digital signatures, AIPA (the Information Technology Authority for the Public Administration) issued a circular dated July 26, 1999 (published in *Gazzetta Ufficiale* 179, August 2, 1999) which completes the regulatory framework requested by Parliament to begin the process of authenticating digital signatures on computer messages. The first authentication agency authorized by AIPA is Società Interbancaria per l'Automazione (SIA), a banking industry company.

At the EU level, Directive 1999/93 on electronic signatures was issued on December 13. It lays down common principles for use and authentication of electronic signatures. As regards developments in Community regulation of electronic commerce, Directive 2000/31/EC was issued on June 8, 2000 and published in the Official Journal of the European Union on July 17 (L 178/1). The Directive, which is designed to create a uniform regulatory framework for “Information Society services”, came into force upon its publication and must be transposed into national legislation by the Member States no later than January 17, 2002.

Italian banks have been actively engaged in preparing the functional and technical specifications for migration from magnetic band to chip cards. Generally, the use of payment cards and direct debits increased significantly. There was a substantial increase (44.5 percent) in the number POS debit card transactions and a considerable decrease (16.7 percent) in the number of banker’s drafts. The greater use of innovative payment channels (POS) underscores the continuing transformation in consumers’ habits as they learn to exploit the potential of the new payment instruments that banks offer.

By value, there was growth of more than 35 percent during the year in POS debit card sales, 20 percent in direct debits, and 14.5 percent in banker’s drafts.

The average size of transactions using traditional instruments (personal checks and banker’s drafts) increased, while that of POS debit transactions decreased. This is explained by the more frequent use of debit cards by consumers, even for small purchases.

Supervision of Non-Domestic Banking Organizations

The branches of EU banks are subject to mutual recognition and home country control pursuant to the Second Banking Directive. This means that EU banks are regulated and supervised by the authorities of their country of origin. For branches of non-EU banks, the same rules apply as to Italian banks, taking into account the adequacy of supervisory systems in the home country, reciprocity and any limitations on the branch’s business imposed at its own discretion by the parent bank. For example, in securities trading non-EU branches must comply with the regulation on market risk, which is in line with the Basel Accord’s standards.

Non-EU bank branches are not required to have any specific reserves over and above the usual compulsory reserves, proportional to their deposit liabilities, which are required of all banks operating in Italy. Branches of non-domestic banking organizations operating in Italy are not subject to any type of asset pledge requirement.

JAPAN

Commercial Code Amended to Introduce Share Swap System

On October 1, 1999, the Commercial Code was amended to introduce a new share swap system and share transfer system. Japan has allowed holding companies to be established since December 1997, and bank holding companies since March 1998. The share swap system and share transfer system facilitate the establishment of holding companies (full parent companies) by enabling the parent company to hold all shares issued by the subsidiaries. Japan's first bank holding company (the "Mizuho Financial Group," see below) is scheduled to be established in the Fall of 2000 using this system.

In May 2000, a new "Bill to Amend a Part of the Commercial Code" passed the Diet. The law will create a "corporate separation system" that will make it easier for joint-stock companies to reorganize. Specifically, it will set up procedures to split companies and transfer part of their business to another company. The corporate separation system will make it possible for financial groups to consolidate the functions of their member institutions.

Large Financial Institutions Continue to Consolidate

Dai-Ichi Kangyo Bank, Fuji Bank, and Industrial Bank of Japan agreed on August 20, 1999 to a full integration of their operations into a new financial services group. At the end of March 1999, the three banks had combined assets of ¥141.0 trillion, making them the largest financial group in the world. In the Fall of 2000, the three will become subsidiaries of a holding company that they will jointly establish. By the Spring of 2002, they will unbundle their functions and reorganize themselves into a retail bank, a wholesale bank and an investment bank. The new group to emerge out of this consolidation will be called the "Mizuho Financial Group."

Sakura Bank and Sumitomo Bank reached a basic agreement to merge on October 14, 1999. The banks had combined assets of ¥98.7 trillion as at the end of March 1999. The merger is scheduled to take place in April 2001. The new bank will be called the "Sumitomo Mitsui Banking Corporation."

On July 5, 2000, Sanwa Bank, Tokai Bank and Toyo Trust and Banking announced an agreement to integrate their operations under a holding company organization. Their goal for establishment of the holding company is April 2001, with the subsequent merger of Sanwa and Tokai by April 2002. The three banks had combined assets of ¥82.6 trillion as at the end of March 2000.

On April 19, 2000, four institutions, the Bank of Tokyo-Mitsubishi, Mitsubishi Trust and Banking, Nippon Trust Bank (a trust banking subsidiary of Bank of Tokyo-Mitsubishi), and Tokyo Trust and Banking (also a trust bank subsidiary of Bank of Tokyo-Mitsubishi) agreed to establish a joint holding company under which their operations will be integrated. The joint holding company will be established by the banks in April 2001, with the three trust banks merging by that October. The name of the new holding company will be "Mitsubishi Tokyo Financial Group, Inc." The four banks had combined assets of ¥90.1 trillion as at the end of March 1999.

As a result of these mergers and consolidations, Japan's city banks and other large financial institutions will reorganize into four main financial groups.

In addition, on April 1, 2000 Mitsui Trust and Banking and Chuo Trust and Banking merged to form Chuo Mitsui Trust and Banking. That same day, Bank of Kinki and Bank of Osaka, both regional banks, merged to form Kinki Osaka Bank.

Capital Injections under the Early Strengthening Law

The Financial Reconstruction Commission invoked the "Law Concerning Emergency Measures for Early Strengthening of the Function of the Financial System" on September 13 and December 9, 1999 and again on March 14, 2000 to approve applications for the issue of shares and subordinated debt to be underwritten with public funds. The first round of underwriting was for regional banks Ashikaga Bank, Hokuriku Bank, and Bank of Ryukus, and for the member banks of the Second Association of Regional Banks (Hiroshima-Sogo Bank and Kumamoto Family Bank); the second round for the Long-Term Credit Bank of Japan, Limited (LTCB) and Hokkaido Bank. On September 29, 1999, it injected ¥260 billion in public funds into four banks; in March 31, ¥315 billion into three banks. These injections of capital were in addition to the ¥7,459 billion that had already been paid into fifteen large banks at the end of March 1999.

Long-Term Credit Bank of Japan, Nippon Credit Bank Sold

On September 28, 1999, the Financial Reconstruction Commission named "New LTCB Partners" (NLP), an investment consortium led by the Ripplewood Holding Company (New York, USA), its highest priority in negotiating the full transfer of LTCB, which had earlier been placed under special public management. On March 1, 2000, the Deposit Insurance Corporation sold all of the ordinary shares of the bank to NLP, ending the special public management of the LTCB. LTCB began business under new management on March 2, 2000, and on June 5, 2000 changed its name to the "Shinsei Bank." LTCB had been placed under special public management in October 1998 under the provisions of the "Financial Reconstruction Law." The Deposit Insurance Corporation acquired all shares in the bank at that time.

On June 6, 2000, the Deposit Insurance Corporation, the Softbank Group, an investment group comprising Softbank (an Internet related company), Orix (a leasing company), Tokyo Marine and Fire Insurance and Nippon Credit Bank, which was placed under special public management in December 1998, reached a basic agreement to sell all the shares of Nippon Credit Bank held by the Deposit Insurance Corporation to the Softbank Group.

Deregulation

On October 1, 1999, Japan lifted the long-standing ban on straight bond issues by ordinary banks. Sumitomo Bank became the first ordinary bank to issue straight bonds. Several other banks have also made straight bond issues. There were no written regulations against straight bond issues by ordinary banks in the past, but they had not been permitted under "administrative guidance."

On October 1, 1999, all limitations were eliminated on the scope of business open to banking, securities, and trust subsidiaries. In 1993, Financial System Reform Law permitted institutions to participate in each other's industries by establishing banking, securities, and trust subsidiaries, but the scope of business open to them had been limited in order to avoid rapid changes.

Also on October 1, 1999, stock trading fees were fully liberalized.

Amendments to the Deposit Insurance Law

The Deposit Insurance Law was amended on May 24, 2000.

The amendments establish the framework for the deposit insurance system and the resolution of financial institution bankruptcies after April 2001. The principal provisions of the law are as follows:

- The financial reorganization administrator system and bridge bank system provisionally established (until the end of March 2001) under the Financial Reconstruction Law have been made a permanent part of the deposit insurance system.

- A wider range of cases is open to financial support by the Deposit Insurance Corporation (DIC). Financial support will now be available for partial transfers of business (purchase and assumption of insured deposits) and after-the-fact financial support by the DIC will be available to receiving financial institutions (loss-sharing rule between the DIC and receiving institutions).

- Exceptional provisions have been added for emergency situations in which occurrence of systemic risk is expected to be unavoidable.

- Insurance has been extended to bank debentures held by individuals, deposits by local governments, and interest on deposits.

- Special provisions for financial support in excess of deposit payoff costs have been extended for one year to the end of March 2002.

- Full protection for current accounts, ordinary deposits and other demand deposits has been extended until the end of March 2003.

Ordinance Passed on New Size-Based Corporate Tax on Banks Levied by Tokyo Metropolitan Government

The Tokyo Metropolitan Government announced on February 7, 2000 that it would impose a new size-based corporate tax (local business tax on corporations) specifically on large banks and other financial institutions. The new tax uses a loophole to calculate business taxes based on core operating profits rather than income, which is the ordinary standard. It applies only to banks with deposits in excess of ¥5 trillion, and will expire in five years time. According to the announcement by the metropolitan government, the tax will raise approximately ¥110.0 billion from banks, most of which will come from about thirty large institutions.

The Japanese Bankers Association (JBA) immediately lobbied against the new tax, and the central government expressed misgivings over it in an oral statement issued by the Cabinet. The ordinance nonetheless passed the metropolitan legislature on March 30, 2000 and took effect on April 1, 2000. The JBA has announced it is now planning to challenge the legitimacy of new tax in the courts.

NASDAQ Japan, "Mothers"

On May 8, 2000, "NASDAQ Japan Market" was established within the Osaka Securities Exchange, and started trading on June 19. The establishment of "NASDAQ Japan" is based on a June 1999 agreement between Softbank and the National Association of Securities Dealers (USA) to create a new over-the-counter securities market in Japan. Seven companies had listed by June 2000.

In September 1999 the Tokyo Stock Exchange established "Mothers" as a new market for start-up companies. Trading began on December 22nd. Ten companies had listed by June 2000.

Law for Punishment of Organized Crimes Takes Effect (New Financial Intelligence Unit Established)

The Law for Punishment of Organized Crimes took effect on February 1, 2000, bringing into force new punitive measures for crimes committed by organizations and stronger measures against money laundering.

The law expands the crimes contributing to money laundering from drug-related activities to a wider range of serious criminal activities. It also establishes a Financial Intelligence Unit (FIU) within the government to receive, analyze, and provide information on money laundering. The FIU is under the Financial Supervisory Agency (now the Financial Services Agency).

J-Debit

On March 6, 2000, a new on-line debit card system, "J-Debit" began nationwide operations. Under the system, ATM cards issued by 617 financial institutions (approximately 300 million cards) gained debit card function and can be used at debit card terminals installed at approximately 100,000 locations around the country.

Japan has experimented with debit card systems for several years, but this is the first to provide nationwide services.

Year 2000 Date Change

All financial institutions in Japan had their major computer systems Y2K compliant by the end of November 1999, at which time outside connection tests were performed for the payment systems. Banks in Japan had holidays from December 31, 1999 to January 3, 2000, so internal tests and outside connection tests were run for financial institutions and the payment systems during the January 1-3 period.

When banks opened their doors for business on January 4, 2000, there were slight problems at some institutions, but no major Y2K-related troubles.

Commercial Firms to Enter Banking

In November 1999, Ito-Yokado, a nationwide supermarket chain, revealed plans to establish a bank specialized in payment services. The new bank will install ATMs in supermarkets and convenience stores of Ito-Yokado to process payments. The bank will not make loans to companies, but will invest exclusively in government bonds and similar instruments.

On March 30, 2000, Sony announced plans to establish an internet bank. The new bank will also have investments from Sakura Bank and JP Morgan.

There is no prohibition in Japanese banking law against commercial firms owning banks, but there has been no new entry from commercial firms into banking to date. In May 2000, the Financial Reconstruction Commission, which has licensing authority for banks, requested comment on new guidelines for licensing and supervision of new-type entrants into banking.

Three Laws Improving Financial Infrastructure Passed

On May 23, 2000, the "Financial Products Sales Law," "Law Amending the Special Purpose Company Law" and "Law Amending the Securities and Exchange Law" were enacted.

The Financial Products Sales Law and the amendments to the Special Purpose Company Law were drafted as part of the Japanese version of the "Financial Services Act." The Financial Products Sales Law defines rules for the sale and solicitation of financial products. For example, it obligates sellers to provide explanations to customers who lack expert knowledge when selling financial products that do not guarantee principal and making the seller liable to compensate for loss of principal in the event that explanations were not made and the customer incurs losses. The law takes effect in April 2001.

The Law Amending the Special Purpose Company Law has two principal aspects:

- It amends the Special Purpose Company Law to expand the assets eligible for securitization using special purpose companies to claims on assets in general, and it permits the use of trusts in securitization.

- It amends the Securities Investment Trust Law to expand the categories of assets eligible for investment trusts from securities to real estate and a wide variety of other assets.

The Law Amending the Securities and Exchange Law likewise has two principal aspects:

- to provide for electronic, on-line submissions and receipts of securities reports and other disclosure documents; and

- to permit stock exchanges and financial futures exchanges to convert from membership organizations to joint stock companies.

The first aspect will become mandatory in principle beginning June 2004; the second will take effect in December 2000.

Establishment of Financial Services Agency

On July 1, 2000, the Financial Supervisory Agency and the Financial Planning Bureau of the Ministry of Finance were absorbed into a new body, the Financial Services Agency (FSA). In addition, the FSA will take over the function of the Financial Reconstruction Commission when the latter is abolished in January 2001 in connection with the ministerial reorganization.

KOREA

Regulatory Developments

Introduction of Forward-Looking Criteria

Effective December 31, 1999, the Financial Supervisory Service (FSS) revised the asset classification standards for domestic banks to incorporate "forward looking criteria" into the evaluation of a borrower's ability to repay a loan. Under the revised standards, decisions to extend credit to large corporations will no longer be based solely on collateral coverage and the borrower's financial condition, but also on the borrower's competitiveness and future earnings prospects.

The revised standards are intended to serve as base guidelines for assessing the adequacy and feasibility of banks' internal asset classification standards. Where necessary, the FSS will require a bank to revise its standards to meet the minimum requirements of the revised standards. The FSS will also determine whether banks have properly classified their assets and made adequate provisions in accordance with the revised standards and require prompt remedial action to correct any deficiencies.

Early Write-Off of Bad Assets Permitted

The FSS has revised its regulations to allow financial institutions to write off non-performing assets more easily. This change was made in conjunction with the introduction of forward-looking criteria and addresses the potential for the application of such criteria to increase substantially domestic financial institutions' non-performing loans and thereby adversely affect their credit rating.

As revised, the regulations permit financial institutions to write off estimated losses from their non-performing assets even before their liquidation upon the determination, based on the assessment of the obligor's financial condition and ability to repay, that recovery will be impossible. In addition, the FSS has relaxed the restrictions on writing off non-performing assets that are subject to a court receivership or are in composition (i.e., the obligor on the loan is undergoing reorganization through a formal bankruptcy proceeding). Whereas formerly such write-offs were permitted only if the obligor has been in the red for two consecutive years and the obligation to pay is more than two years overdue, new rules allow even such assets to be written off under the same conditions applied to other non-performing assets that are neither subject to a court receivership nor in composition.

Enhancement of Internal Controls

Increased attention has been given to enhancing financial institutions' internal control functions as a means to address growing concerns regarding transparency and customer protection. Effective January 2000, banks, securities firms, insurance companies and investment trust corporations (ITCs) are required to replace their standing auditors with an audit committee. Under revisions to the Banking Act enacted in 1999, a bank's audit committee must be composed of at least three individuals, and two-thirds of a committee's members must be outside directors.

Financial Holding Companies To Be Introduced

The government is preparing a bill to encourage the establishment of financial holding companies. It is contemplated that there would be two types of financial holding companies. A "bank financial holding company" would be any financial holding company that includes a bank within the group, while a "nonbank financial holding company" would be one that does not have any banks within the group. Under this arrangement, industrial enterprises would be permitted to participate in nonbank financial holding companies but not in bank financial holding companies. The FSS is working to establish guidelines and regulations for financial holding companies by the second half of 2000.

Establishment of the Third Stock Market

Korea's third stock market was established in March 2000. This new market is designed for trading stocks that either have not been listed on the Korea Stock Exchange (KSE) or the Korea Securities Dealers Automated Quotation System (KOSDAQ) or have been delisted from such exchanges. Whereas investors previously have traded unlisted shares through unregistered trading facilities, the introduction of the third market will increase liquidity in such shares and reduce settlement risk. In addition, the availability of the third market will provide expanded funding sources for unlisted companies.

Unlike trades on the KSE or through KOSDAQ, capital gains from trades in the third market will be subject to capital gains taxes. A 20 percent tax will be levied on capital gains from shares of large firms, with a 10 percent tax levied on those from small and medium-size firms.

Implementation of an Electronic Disclosure System

In connection with its continuing efforts to improve the financial disclosure system and enhance overall business transparency, the FSS on April 1, 2000 introduced an electronic disclosure system which will create a virtual "one stop filing system" for all listed companies. In addition to expediting the disclosure process, the new system allows firms to submit their required disclosure documents only to the FSS and thus eliminates the need for companies to submit separate disclosure reports and data to the KSE or KOSDAQ (these entities will receive the documents electronically directly from the FSS). It is estimated that the shift to electronic disclosure will reduce by 25 percent the amount of paperwork generated by disclosure requirements.

To implement this new system, the FSS has established the Data Analysis Retrieval and Transfer (DART) system, which is capable of simultaneously sending multiple data files to multiple recipients. In addition, disclosed information will be made available to both domestic and foreign investors via the Internet.

"Best Practices" Introduced for Derivatives Transactions

The FSS has introduced a set of "best practices" to enhance domestic financial institutions' ability to manage the risks associated with derivatives transactions. Among these best practices are the following:

- The effectiveness of a financial institution's internal controls and risk management practices should be evaluated on the basis of the complexity and risk exposures of the derivative instruments it trades. In this regard, a clear division between operational and risk management departments should be maintained.

- To enhance the role of market discipline, financial institutions should disclose the following information about their derivatives transactions: accounting methodology; risks; risk management practices; and creditworthiness of counterparties.

- Prior to entering into a derivatives transaction with an investor, a financial institutions should provide the investor an in-depth explanation of the transaction geared to the level of the investors' sophistication.

- To prevent unfair transactions, the best practices prohibit concealment of losses through over/under valuation of prices. Transferring a loss on one instrument to another instrument is also prohibited.

Establishment of a New Warrant Market

In June 2000, the KSE commenced the trading of warrants separate from the "bonds with warrants" (BWs) to which they are attached. Such trading is limited to warrants linked to BWs that are issued through public offerings by listed companies and that have a remaining exercise period of greater than one year.

Anti-Money Laundering Initiatives

The National Assembly adjourned in May 2000 without acting on an anti-money laundering bill, which had been deadlocked for three years. A new bill is expected to be presented in the new session convened in July 2000.

LATVIA

Development of a Consolidated Supervisory System

In June 2000, the Parliament has passed a law which calls for the establishment of a consolidated financial supervisory system under the auspices of a new "Financial and Capital Market Committee" starting July 1, 2001. The Committee will be formed through the consolidation of existing supervisory authorities such as the Supervision Department of the Bank of Latvia, the Securities Market Commission and the Insurance Supervision Inspectorate. It will be an independent state institution that will be responsible directly to the Parliament.

Bank Regulatory Developments

Within the framework of the continued harmonization of Latvian laws and regulations with relevant EC directives, the Bank of Latvia's Board of Governors approved amendments to the "Regulation for Annual Financial Statements of Credit Institutions" effective May 1, 1999. The amendments relate to the disclosure of additional information in the notes to annual financial statements regarding the average number of a credit institution`s employees, the salaries of its board and executive board members and the total amounts of their advances, loans, guarantees and other transactions with the institution. In addition, the amendments call for inclusion in the balance sheet of information about subordinated claims, liabilities and claims on associated and related companies.

The Bank of Latvia issued its "Regulation for Compiling the 'Report on Country Risk'" (effective October 1, 1999) calling for the periodic provision of information that will enable it to evaluate country risk inherent in credit institutions' operations.

When preparing annual financial statements for 1999 and subsequent years, credit institutions will have to comply with the "Regulation for Consolidated Financial Statements of Banks". This regulation requires that consolidated financial statements disclose information about the financial standing and results of operations of any group consisting of a bank (a parent undertaking) and its subsidiaries to any person or investor wishing to obtain such information.

Promulgation of the "Regulation for Assessing Assets and Off-Balance-Sheet Liabilities" (effective January 1, 2000) addressed the considerable qualitative changes that have occurred in recent years in the lending and credit risk management practices of Latvian banks. The regulation replaced the "Provisions for Evaluating Credits and Off-Balance-Sheet Items" approved by the Board of Governors on January 17, 1996 and is based on the principles articulated in the Basel Committee's consultative paper on "Sound Practices for Loan Accounting and Disclosure". The regulation provides guidelines for evaluating the quality of assets and off-balance-sheet liabilities, classification of them in accordance with the determined degree of credit risk, and disclosure of changes in their quality in financial statements.

In March 2000, the Bank of Latvia`s Board of Governors approved new regulations "On Capital Adequacy Ratio Calculation". This regulation adds to the existing capital charges for credit risk (solvency ratio) capital charges for market risks in the trading book that are in accordance with the respective EU legislation.

Year 2000 Date Change

At the instruction of the Governor of the Bank of Latvia, a working group within the Bank was established in October 1998 to coordinate solutions to the Year 2000 problem and to assure that the Bank`s information and other systems would operate smoothly throughout the Year 2000 rollover period. The Bank of Latvia carefully monitored the banking sector to see whether measures taken to address the potential Year 2000 problem were adequate and whether banks complied with the requirements set forth by the “Regulation for Year 2000 Compliance”. As part of these efforts, the Bank established a Common Coordination Center for Solving the Year 2000 Problem in Latvia to gather information on the readiness of all Latvian financial institutions for the Year 2000 date change and any deficiencies detected. The Bank also collaborated with banks and other Latvian and foreign financial institutions and participated in similar working groups formed by the Government.

As a result of these efforts, Latvian financial institutions experienced no significant problems in connection with the Year 2000 date change.

Developments in the Securities Markets

On May 2, 2000, a Protocol of Intent was signed by the three Baltic stock exchanges. The Riga Stock Exchange has also been involved in discussions regarding its joining the alliance of exchanges of the Northern European countries (NOREX), which would allow the integration of the Latvian securities market with European financial markets.

The laws "On Securities" and "On Joint-Stock Companies" have been amended to clarify the standards applicable to participants in the securities markets and their liability for failing to meet these standards. These amendments also modified the requirements applicable to the conduct of tender offers and enhanced the protections accorded minority shareholders.

The Council of the Securities Market Commission took a number of actions to improve information-reporting standards, regulate the conduct of securities intermediaries and promote further harmonization with EU directives. These included issuance of the following regulations:

- Regulations on Stock Exchange Licensing (July 12, 1999)
- Regulations on Tender Offer (September 16, 1999)
- Regulations on Reporting of Securities Transactions (November 10, 1999)
- Regulations on Reporting of Over-the-Counter Market Transactions (December 24, 1999)
- Regulations on Transfer of the Securities Accounts (March 8, 2000)
- Regulations on Registration of Foreign Investment firms with the Securities Market Commission (May 5, 2000)

Developments Regarding Insurance

Financial reporting requirements have been amended to conform to the measures prescribed by EU directives. Amendments to the law on “Insurance Companies and their Supervision” clarify the investment authority of insurance companies and liberalize their ability to invest abroad.

The Insurance Supervision Inspectorate has issued additional guidance regarding credit insurance, surety bonds, travel insurance and insurance coverage of legal expenses.

At the end of 1999, the Inspectorate became a member of the International Association of Insurance Supervisors (IAIS).

Supervision of Non-Domestic Banking Organizations

According to the Law on Foreign Investment in the Republic of Latvia, foreign investors are guaranteed the same rights and obligations as domestic investors. A non-domestic banking organization may conduct banking operations in Latvia through either a branch or a subsidiary that is registered as a Latvian bank with foreign share capital.

In order to establish a subsidiary or set up a branch in Latvia, a foreign banking organization must provide satisfactory evidence that such action is taken with the approval of its home country supervisory authority. In addition, it must submit a confirmed statement from such authority that (i) it supervises credit institutions organized under home country laws on the basis of globally consolidated financial statements, (ii) the supervisory authority is authorized under applicable home country law to receive from and provide to foreign supervisory bodies supervisory information regarding credit institutions and (iii) home country prohibits the unauthorized use of such information.

The Bank of Latvia independently assesses on the basis of its own standards the capital adequacy of credit institutions, including those that are subsidiaries of non-domestic banking organizations. A Latvian bank subsidiary of a non-domestic banking organization may expand its nonbanking activities in Latvia through acquisitions, provided that it does not invest more than 15 percent of its capital in a single entity or more than 60 percent of its capital in the aggregate. However, these limitations do not apply to the non-domestic banking organization itself.

Non-domestic banks that operate in Latvia through branches are not required to maintain on deposit with custodian banks in Latvia a specific amount or type of collateral. However, a non-domestic bank that has established a branch in Latvia is required to invest in assets in Latvia of not less than one million euro during the year after the receipt of the license and must maintain this level of investment throughout the period of its operation.

LUXEMBOURG

Law of June 8, 1999 establishing private pension fund vehicles in the form of open-ended private pension fund companies (SEPCAVs) and private pension funds (ASSEPs)

A new legal regime for pension funds has been developed by the Law of June 8, 1999, which enables the creation of national and international pension vehicles. These are designed to carry supplementary pension obligations undertaken on a voluntary basis by employers in the form of Luxembourg-based, foreign-based or multinational undertakings in favor of their employees.

As discussed below, the framework of the new regime is characterized by flexibility, security and fiscal neutrality.

1.1. Flexibility and security

The Law of June 8 permits promoters of pension vehicles to adopt limitations to protect the interests of employees, but does not itself mandate any such limitations. This reflects the intention to ensure flexibility at every level:

1) at the level of the promoters

A pension fund may be limited to a single company or extended to a group of companies. It may be open to personal contributions by the beneficiaries, but also may be used by a professional body (like lawyers or architects) to create their own pension vehicle in which they will be the only contributors and beneficiaries.

2) at the level of the benefits to be provided

The fund must be capable of serving as a support for all kinds of retirement benefits. Payments can take the form of either a lump sum distribution or a life annuity. Pension vehicles may be organized to finance defined benefits schemes or defined contribution schemes.

Defined contribution schemes typically provide a lump sum capital payment at a specified age. The reimbursement of capital plus earnings to the beneficiary could also take the form of installment payments over a period of time to be chosen by the employee.

The pension fund likewise may provide payment of a life annuity during the years of retirement.

3) at the level of investment policy

Like the existing law on investment funds, the only constraint imposed by the law on pension funds will be the principle of diversification of risks and the detailed definition of an investment policy in a regulation between the parties concerned. Beyond this, no limit is defined in advance. The investment policy has to be approved by the supervisory authority, which has to take into account the maturities of the pension liabilities (for defined benefits schemes).

4) at the level of the employer's responsibilities

If the defined benefit consists of the payment of a life annuity, detailed financing plans, which are subject to external regulations, have to be elaborated. The form of the regulation has not been defined in order to maintain the flexibility of the structure. The law leaves the application of the legal requirements within the competence of the prudential supervisory authorities so as not to deprive the promoters of the essential flexibility when the fund is set up.

5) at the level of relations between the social partners

Each fund is able to function according to its own specific rules. Those rules may vary widely depending on the origin or the wishes of the fund promoters. Foreign companies which create pension funds in Luxembourg and wish to respect the statutory requirements of their own country are able to do so; no constraint in that regard has been imposed on them by Luxembourg law.

6) at the level of the management of a pension fund

The management of a fund can be determined individually by each fund. It may also be open to personal contributions by the beneficiaries; management of assets and liabilities can both be delegated to other professionals.

7) transferability of acquired rights

Inherent to the nature of the fund, the beneficiary has the opportunity to transfer his acquired rights in case of changing his employer.

1.2. Legal structures

Following the law of June 8, 1999, two scheme structures may be distinguished as follows:

the SEPCAV (société d'épargne-pension à capital variable)

is a corporate-type structure whose members and beneficiaries are its shareholders, entitled to withdraw their equity capital in a single lump sum on retirement.

the ASSEP (association d'épargne-pension à capital variable)

is a mutual-type structure whereby the rights of members and of beneficiaries are represented by a liability, to be discharged on retirement either as a lump-sum distribution of capital or as a regular income (annuity) payment.

1.3. Third parties

The supervisory authority

All pension schemes must obtain authorization from the CSSF (Commission for the Supervision of the Financial Sector) before commencing activities. CSSF authorization shall comprise the approval of the scheme's organizational documents, including the scheme particulars, together with the approval of the proposed custodian bank and any proposed investment and/or actuarial advisers.

The depository bank

The assets of both SEPCAVs and ASSEPs must be segregated in a depository bank (subject to the law of April 5, 1993 on the financial sector) which has its head office in Luxembourg or which is an EU or EFA credit institution established in Luxembourg. The depository bank is required to carry out the day-to-day administration of the assets. Similar to the investment fund and insurance laws, the depository may appoint sub-custodians but remains responsible to the shareholders of a SEPCAV and to an ASSEP for the proper performance of its duties.

The external auditor

Private pension funds have to assign an external auditor agreed in Luxembourg in order to audit annual accounts.

The asset and liability manager

Pension funds (SEPCAV and ASSEP) can either manage their assets themselves or delegate the management to one or more asset managers. Within Luxembourg, asset managers must be authorized under the applicable provisions of the law of April 5, 1993. Foreign professionals not subject to the above law but specifically agreed by the CSSF may also be responsible for the management of assets.

Liability management is only an obligation for ASSEPs. They can either carry out this function themselves or delegate the management to liability managers having the qualification of an actuary.

Taxation

Both pension fund structures are taxable entities subject to corporate tax. However the two structures have been designed to be "tax neutral" as much as possible. Consequently besides income tax the two are subject to a small capital duty. The SEPCAV is exempt from wealth tax whereas the ASSEP is not. The SEPCAV is exempted by the provisions of the law to taxation from securities income, whereas the ASSEP is required to establish provisions equal to the assets attributable to the members, thus ensuring that tax will either be non-existent or minimal.

The new law enables the facilitation of tax co-operation with foreign tax authorities in order to enable SEPCAV members to maximize their tax benefits in their country of residence. The law currently contains no similar provisions for ASSEP members.

Both vehicles should benefit from double taxation treaties and the new law exempts asset management fees from VAT.

Grand-ducal decree of December 23, 1999 determining the nature of financial assets and the modalities of reporting and conservation of declarations

The EEC directive of May 10, 1993 on investment services has been implemented in Luxembourg through two different laws:

- law of March 12, 1998 amending the law of April 5, 1993 on the financial sector and Art. 113 of the Commercial Code; and

- law of December 23, 1998 on the supervision of financial assets markets.

As to the supervision of financial assets markets, other legislative developments have been introduced by the aforementioned grand-ducal decree and a circular of the CSSF in order to give the necessary interpretations regarding the nature of financial assets and the modalities of reporting and conservation of declarations.

Modification of the legislation on capital requirements

Pursuant to article 56 of the law of April 5, 1993 on the financial sector, the CSSF is the competent authority for determining the capital ratios which are imposed by the different European directives.

In Luxembourg, these directives are implemented through circulars issued by the CSSF. On March 17, 2000, the CSSF published two further circulars in order to implement the following directives into Luxembourg legislation:

- directive 98/31/EEC of June 22, 1998, modifying directive 93/6/EEC on capital adequacy of banks and investment firms;

- directive 98/32/EEC, modifying directive 89/647/EEC on a solvency ratio in the context of mortgage backed securities; and

- directive 98/33/EEC modifying different annexes of the capital adequacy and the solvency ratio directives.

The recent modifications complete the requirements for solvency and large exposures without affecting the main principles. They introduce a new capital requirement for risks due to the change of prices in raw materials.

Furthermore, the use of internal models is authorized for calculating capital requirements for coverage of exchange risk, the risks due to the change of prices in raw materials, and other market risks. However use of internal models is subject to prior CSSF approval as to certain qualitative and quantitative criteria and must be used as a substitute for or a complement to the standardized approach.

Finally, the new regulation introduces a more favorable weighting for commercial mortgage-backed securities.

Supervision of Non-Domestic Banking Organizations

Non-domestic banking organizations may operate in Luxembourg through separately-incorporated bank subsidiaries or branches.

Separately-incorporated subsidiaries are legal entities established under Luxembourg law and as such are subject to the supervision of the CSSF. As a majority of Luxembourg banks are owned by foreign shareholders, they also are subject to supervision on a consolidated basis by the appropriate home country authority in accordance with EEC or BIS rules.

Branches of banks organized in another Member State of the EU may be operated in Luxembourg on the basis of the principle of free establishment and are subject to the supervision of the appropriate home country authority.

Banks organized outside the EU may operate branches in Luxembourg with the consent of the CSSF and subject to its supervision. Such banks must respect the same conditions as those applied to banks established under Luxembourg law, including in particular the provisions concerning the allocation of endowment capital to the operations of the branch.

THE NETHERLANDS

Organization of the Supervisory Authorities

The Dutch Minister of Finance announced in 1999 plans to strengthen the cooperation of the three financial supervisors in The Netherlands: the central bank, the securities and exchange commission and the supervisor of insurance firms. It is contemplated that cooperative efforts among the three authorities will focus on supervision of financial conglomerates and the integrity and transparency of financial products, without requiring the establishment of an additional supervisory body. The contours of these cooperative supervisory arrangements remain under discussion.

Proposals have been put forward concerning the incorporation of supervisory guidelines into enforceable law with regard to, for example, capital adequacy, administrative organization, internal organization, permissible mergers and acquisitions. The Dutch banks are trying to focus the discussion on issues like duplicative supervision and improved coordination among supervisors. Since the existing regulation has proven its effectiveness, the Dutch banks and insurance companies do not see a justification for new legislation. An in-depth study is underway by the financial conglomerates themselves on the impact these proposals may have on their respective supervisors, the enforceability of these proposals and the proposals' implications for internal requirements and measures.

Banking Supervision

Integrity Audits

The Dutch central bank has developed the "integrity audit" to measure the way in which banks manage integrity risks within their organization systematically. The audit will be applied by internal audit personnel and checked by the individual supervisor of the banks. It does not require an adjustment of the legal framework, but is simply means to address potential problems.

Liquidity supervision

A new liquidity directive that covers both the domestic position and the foreign position of bank holdings is being prepared. The directive calls for an explicit description of all kinds of crisis scenarios, a "cocktail" approach of the sum of necessary liquidity in the various scenarios, an exemption for holdings comprised of large, independent foreign banks, and special treatment of the liquidity effects of derivatives positions. Implementation is expected sometime in 2001.

Country risk supervision

A new country risk policy has been adopted to allow ba nks, even before any modification to the Basel Capital Accord, to allocate capital to country portfolios according to internal models (i.e., minimum add ons have to be calculated for certain types of cross-border and foreign assets). Existing country provisions are retained only for high-risk countries (currently, Russia and Indonesia). Implementation is expected by year-end 2000.

Capital Adequacy

During the period under review, the Dutch central bank accepted as Tier 1 capital the new forms of risk-sharing capital announced by the Basel Committee in October 1998 and subsequently accepted by banking authorities in Japan, the United States and the United Kingdom.

Basel Accord Review

Consultations with the Dutch central bank regarding the review of the Basel Capital Accord have been very constructive. The Dutch position paper on the proposed revisions to the Accord focused in particular on:

- the importance of convergence of regulatory capital and economic capital;
- avoiding competitive distortions (i.e., preservation of a level playing field);
- a flexible transition between various approaches to credit risk;
- use of internal ratings for credit risk;
- providing for interest rate risk in the first pillar; and
- conditionally providing for operational risk in the first pillar.

Disclosure

The Dutch banks initiated a directive on banks' disclosure. The new directive integrates traditional Dutch and European values with the new IASC standards. While disclosure regulation was fragmented before, the new directive is uniform and transparent.

Year 2000 Date Change

The Dutch banks did not experience any problems in connection with the Year 2000 date change. The Bankers' Association had created a platform for interbank communication and preparation projects in 1997. These projects involved:

- checklists for adjustments;
- external communication efforts and an enforceable Code of Conduct;
- cooperation with accountants' organizations;
- interbank alignment of contingency measures; and
- emergency scenarios stemming from uncertainties around utility and telecom facilities.

In addition, the Dutch banks participated in the Global 2000 Coordinating Group, which measured international readiness and developed test models for international networks, disclosure of the Y2K information and risk analysis and contingency planing.

This cooperation in preparing for the Year 2000 date change has resulted in improved business continuity plans (an extremely experience with international projects of this size), international cooperation and new methods, techniques and systems that might be applicable to other areas as well.

Regulation of Non-Bank Financial Companies: Electronic Money Institutions

On November 29, 1999, the Council of Ministers decided on a common position on two draft directives that aim to set the conditions under which nonbanks are allowed to issue electronic money. These so-called ELMIs (electronic money institutions) will be subject to supervisory rules and capital requirements that are less restrictive than those applicable to banks and investment institutions. To limit the risk exposure of ELMI customers, investments made by these institutions are restricted.

ELMIs operating in line with the directive are granted a European passport and allowed to operate throughout the Community. Member states still have the prerogative of imposing less restrictive requirements on small ELMIs, but these would then be unable to benefit from the free movement of capital and services. Within the framework of the second reading, the Commission for Economic and Monetary Affairs recently organized a hearing with the European Central Bank and the Banking Federation of the European Union at which the banks pressed for specification of a maximum amount that may be deposited in an ELMIs electronic purse and for limiting the exemptions member states are allowed to grant small ELMIs.

Anti-Money Laundering Initiatives

Dutch money laundering laws are based on reporting unusual transactions on the basis of objective and subjective criteria. Approximately 25 percent of the reports are sent to the police for further investigation. The number of convictions and seizures that result from these investigations is not disclosed. As a result of new mandatory notifications of money transfers, the total number of notifications increased from 25,000 in 1998 to more than 45,000 in 1999, of which the banks reported more than 12,000 transactions and the bureau de change and the money transmitting companies more than 30,000. Other reports came from casinos and credit card issuers.

The European money laundering directive of June 10, 1991 will be updated. The main proposed amendments relate to extending the definition of criminal activity from "drugs related" to "all forms of serious organized crime". Mandatory disclosure is also extended to notaries, legal advisers, estate agents, accountants, dealers in gems or precious metals, money transporters and casinos.

The Dutch banks have welcomes the proposals. Attention has been drawn to the need for alterations and clarifications regarding feedback, host country control and customer identification procedures.

Electronic Commerce

In March 1998, the Dutch Ministry of Economic Affairs launched an action plan on electronic commerce with the ambitious aim to make the Netherlands one of the leading countries in this field. One of the principal objectives of the plan is enhancing confidence on business and consumers in doing transactions by electronic means. In the legal field, the starting point has been that no special legislation should be necessary – what goes for off-line transactions likewise go for online transactions. The Ministry of Justice made an inquiry on existing legislation that could hamper smooth development of e-commerce and came to the conclusion that, generally speaking, the existing legal framework can be applied to electronic commerce without difficulty.

The Dutch government has adopted a policy to enhance self-regulation by parties involved to enable them to react quickly and flexibly to new developments without being hampered by rigid legislation. Several self-regulatory initiatives have been taken to promote e-commerce in The Netherlands and to enhance cooperation in this field (e.g., the development of a code of best practice by ECP.NL, an independent body founded by, among others, the Ministry of Economic Affairs and the Dutch central employers organization (VNO/NCW)).

The European Parliament and the European council recently adopted a new EU Directive on the legal aspects of e-commerce. In view of the speed at which the "new economy" is developing, the Dutch Bankers' Association welcomes this development and hopes that the same energetic approach will be adopted in respect of other proposals relating to e-commerce. Of particular importance in this regard are: a directive on distance-selling of financial services; modernization of the Conventions of Brussels and Rome; identifying at the national and

European levels potentially obstructive consumer legislation; and developing mechanisms for facilitating dispute resolutions in the Internet environment.

Supervision of Non-Domestic Banking Organizations

In accordance with the Second Banking Directive, banks from member states of the European Union that operate in The Netherlands are supervised by the appropriate home country supervisor, although the liquidity of their Dutch operations and the impact of such operations on the country's monetary stability is monitored by the Dutch central bank.

The Dutch operations of banks from outside the European Union are subject to the Dutch central bank's supervision, although a distinction is made between branches and separately-incorporated local subsidiaries. This supervision includes monitoring the adequacy of their capital under the standards of the Basel Accord.

Branches of non-domestic banking organization operating in The Netherlands are not subject to any asset pledge requirement.

NIGERIA

Background Information

The second half of 1999 represented a period of transformation for the Nigerian political economy. The new civilian administration was sworn-in in May 1999, bringing to an end 15 years of military rule in Nigeria. That brought about rejuvenated confidence in the Nigerian economic and financial system.

The new administration has been working towards putting the economy in proper order. Indeed, the major gain that accrued to the economy by the end of 1999 was the achievement of a single-digit inflation rate, which declined from 14 percent in May to 8.20 percent in October 1999 and further to 6.6 percent in December 1999.

Under the new democratic administration, the Central Bank of Nigeria (CBN) has enjoyed greater autonomy and has been able to take steps to mop-up excess liquidity in the system thereby putting in place a measure of economic stability.

The Government has reopened licensing of new banks with a new policy on bank ownership structure, and new banks are now entering the financial system. Under the new policy, an individual or institution with proven financial resources and relevant competence can acquire a controlling interest in a bank.

The Government is also tackling the issue of privatization and a number of parastatals have either already been privatized or are scheduled to be privatized. The Bureau for Public Enterprises set up for that purpose is to co-ordinate all privatization affairs, while the National Council on Privatization (NCP) is the ultimate approving authority.

The new Anti-Graft Bill recently passed into law by the National Assembly is expected to help in restoring the confidence of foreign governments, multilateral institutions and investors in the Nigerian economy.

Regulatory Developments

Organization of Financial Supervisory Authorities

The Central Bank of Nigeria enjoys instrument autonomy and, together with the Nigeria Deposit Insurance Corporation (NDIC), is responsible for the regulation and supervision of banks. The Securities and Exchange Commission (SEC) regulates and supervises securities firms, while the National Insurance Commission (NAICOM) regulates and supervises insurance firms. The Central Bank, SEC and NAICOM are members of the Financial Services Regulation Coordinating Committee (FSRCC), which coordinates the supervision of the respective financial institutions in the country. The Governor of the Central Bank of Nigeria is the Chairman of the FSRCC.

Universal Banking

The Central Bank of Nigeria in its Monetary, Credit, Foreign Trade and Exchange Policy Guidelines for fiscal year 2000 granted approval in principle for the introduction of universal banking in the Nigerian banking system. This will enable each bank to engage in a wide range of financial and fee-based activities, including underwriting of new debt and equity issues, insurance brokerage, discount house services, trusteeship and administration of estates. The present dichotomy between merchant and commercial banks will also be removed. Implementation of a universal banking system awaits implementing legislation.

Discontinuance of Special Treasury Bills

In April, 1999, the CBN introduced the mandatory sale of Special Treasury Bills (STBs) to banks in order to address the problem of liquidity overhang in the system which was a consequence of the excess funds injected into the system by the last Military Administration. The strategy quite succeeded in its intended purpose and, having outlived that purpose, the CBN in the last quarter of 1999 discontinued its use. The discontinuation is expected to remain in effect in fiscal year 2000.

Capital Adequacy Requirements for New Banks

In January 1997, the minimum paid-up capital requirement for both commercial and merchant banks operating in Nigeria was raised to N500 million with a target compliance date of not later than December 31, 1998. The deadline was later extended to March 31, 1999.

However, effective January 1, 2000, modifications were introduced to synchronize with the trend of the economy. While the minimum paid-up capital requirement for existing banks remains N500 million, that for new banks coming on stream has been raised to N1.0 billion. The few distressed banks taken over by the CBN were given up to June 30, 2000 for possible buyers to acquire and revive.

Deregulation of Banks' Commercial Advertisements and New Products Introduction

Pursuant to guidelines release on April 3, 2000, banks no longer have to seek prior approval of CBN before introducing new financial products or advertising their services.

Developments in Foreign Exchange and Trade

Effective from October 25, 1999, foreign investors in the country, especially oil and gas service companies operating in Nigeria, have been allowed to sell foreign exchange brought into the country to meet their local running expenses to any authorized foreign exchange dealer of their choice (including the Central Bank of Nigeria). This follows the replacement of the erstwhile Autonomous Foreign Exchange Market (AFEM) with the Inter-Bank Foreign Exchange Market (IFEM). The bid-and-offer rate approach to management of foreign exchange is now adopted. The Central Bank of Nigeria under the bid-and-offer rate approach can sell or buy foreign exchange towards ensuring a more realistic exchange rate.

With guided deregulation still in place, foreign exchange transactions are now moving towards minimum documentation requirements largely for statistical and recordkeeping purposes.

In response to observed lapses in the operation of the Destination Inspection Scheme adopted in April 1, 1999 to replace the Pre-shipment Inspection Scheme, the Pre-Shipment Inspection Scheme was reinstated with effect from September 1, 1999.

Other Developments in the Financial Sector

Financing Small-Scale Industries

Based on the agreement by banks in Nigeria, the CBN has requested that commencing in 2000 banks are to set aside 10 percent of their profit before tax for financing and promoting small-scale industries. The banks' assistance in this regard will take the form of equity participation or long-term loans to nurture specific industries of their choice to maturity.

Year 2000 Date Change

Financial institutions in Nigeria did not experience any serious disruption in their business in connection with the Year 2000 date change.

NORWAY

Regulatory Developments

Implementation of a new Accounting Act in 1999 resulted in banks having to report their trading portfolios at market prices. In addition, the Act and its implementing regulations have enhanced banks' disclosure of their financial derivatives exposures, financial risks, liquidity, interest rate, currency and credit risks, and loan losses.

Insurance and securities firms are regulated very much the same way as banks, and are supervised by the same body, the Banking, Insurance and Securities Commission. Banks' risk-weighted credit risk solvency requirements apply also to insurance companies. Because commodity derivatives are not defined as financial instruments under applicable law, the Commission does not supervise commodities firms. However, under a proposed amendment to the Securities Trading Act, commodities would be defined as financial instruments, with the result that commodities firms and commodities exchanges would then be treated and supervised the same as securities firms and securities exchanges, respectively. It is anticipated that this amendment will be enacted by June 2001.

Year 2000 Date Change

No significant problems were experienced in Norway in connection with the Year 2000 date change.

Affiliations with Industrial and Commercial Firms

Financial conglomerates comprising banks, securities firms and insurance companies are permitted and common. As a general rule, affiliations between banks and insurance companies, on the one hand, with commercial and industrial firms, on the other hand, are not permitted. Thus, a commercial or industrial firm may hold a maximum of 10 percent in a bank, an insurance company or a financial holding company. A bank may own a minority stake (not to exceed 49 percent) in a commercial or industrial firm, but it may not permanently hold a majority stake. An insurance company may permanently hold a maximum stake of 15 percent in such a firm.

Anti-Money Laundering Initiatives

In June 1999, the Banking, Insurance and Securities Commission issued Anti-Money Laundering Guidelines, which complete with details the laws and regulations already in place since 1994. The Guidelines clarify a number of practical aspects of the application of the money laundering regulations.

Payment Systems Developments

A new Payment Systems Act has been enacted implementing the EU Directive on settlement. In addition, a new Financial Agreement Act has been enacted to provide enhanced consumer protection in connection with payment transactions. In a final development, the banking community has introduced a common electronic customer identity. This so-called "Bank ID" is an electronic certificate and signature that a bank customer (the signature holder) may use in order to protect electronic messages between the bank and the customer by assuring authenticity, integrity, non-refusal and encryption.

Market Developments

In 1999, two of the largest Norwegian banks, Den norske Bank and Postbanken, merged, with the government retaining a 60 percent stake in the resulting Den norske Bank. However, it has declared its intention to sell down this stake to about 34 percent, thus maintaining a controlling minority position.

Also in 1999, Fokus Bank (the third largest commercial bank in Norway) was acquired by Den Danske Bank (Denmark), and Bergensbanken (a smaller commercial bank) was acquired by Svenska Handelsbanken (Sweden). A bid for Christiania Bank (the second largest commercial bank in Norway) from Nordic Baltic Holding (Sweden/Finland/Denmark) was still pending as of June 30, 2000. The government holds a controlling 34 percent interest in Christiana Bank, but has declared its intention to sell at an appropriate price. The bank therefore most certainly will be sold to a non-domestic owner. Earlier in the year, Nordic Baltic Holding acquired the third largest non-life insurance company, Vesta, thereby becoming a major player in all parts of the Norwegian market.

In 1999, Storebrand, the largest insurance group in Norway, bought a smaller bank, Finansbanken. In 2000, Storebrand sold its non-life business to a new Nordic group called "if…" in which Storebrand, together with the Swedish group Skandia, maintains an important ownership interest.

Union Bank of Norway (the country's largest savings bank) joined forces with the mutual insurer Gjensidige (the country's second largest non-life and life insurer) in 1999. The joined group recently has declared its intention to demutualize, but this requires government approval and amendments to the Savings Bank Act. The prospects of obtaining the required approval and amendments are positive, although not certain.

Supervision of Non-Domestic Financial Institutions

Branch offices of financial institutions having their head offices in the European Economic Area (i.e., the 15 EU countries and Norway, Iceland and Liechtenstein) are regulated according to the rules of the Single European Market since 1994. This means that a financial institution having its head office within one of those countries is free to set up a branch office in another country under its home country rules and have the branch supervised by the home country supervisor. Branch offices of banks from other countries that apply comparable supervisory standards to those applied within the EEA (i.e., Australia, Canada, Japan and the United States) are treated in the same way.

A non-domestic financial institution may establish branches in Norway and own a bank and an insurance company in Norway. Subsidiaries owned by non-domestic institutions in Norway are supervised on a solo basis. The Norwegian authorities supervise the Norwegian financial markets as well as the conduct of non-domestic participants in those markets, but do not interfere with the home country supervision of a non-domestic financial institution as a global entity. The Banking, Insurance and Securities Commission requires that a non-domestic institution that operates in Norway through a branch or a subsidiary obtain the necessary licenses and be supervised by its appropriate home country supervisor. The solvency of the global entity may well be different from what the Norwegian authorities require for domestic entities.

There are no asset pledge, capital equivalency deposit, or similar requirements applicable to branches of non-domestic banks in Norway. Whereas the Norwegian authorities apply liquidity requirements to domestic banks, these requirements are not applied to branches of non-domestic banks. However, non-domestic banks that wish to borrow from the central bank (Norges Bank) are subject to the same collateral requirements as domestic banks.

PAKISTAN

Financial Sector Reforms

Financial sector reforms initiated in the early 1990s have made positive headway. Public sector financial institutions have implemented the restructuring plans for downsizing of staff and closure of loss-making branches. Two of the large banks, Habib Bank Limited and United Bank Limited, have been recapitalized. Restructuring of state-owned development financial institutions is underway to make them operationally efficient and financially viable. Banks have begun to seek recovery on problem loans pursuant to the law enacted on this subject in May 1997.

In order to upgrade and enhance its bank supervisory capabilities, the State Bank of Pakistan (SBP) retained the services of the international consulting firm Arthur Andersen to provide on-the-job training to its banking supervision staff.

During the period under review, no public sector financial institution has been privatized, owing to the continuing problems in the economy. A privatization ordinance is being drafted to strengthen the privatization process and provide a legal basis for privatization transactions.

Open Market Operations

During the period under review, the SBP has conducted its open market operations to keep the flow of monetary aggregates within targets, induce the commercial banks to extend credit to the private sector, and keep short-term interest rates at desired levels. Open market operations are conducted regularly and transparently on alternate Thursdays with settlement on the same day. Open Market Operations Notices and Results are released regularly through Reuters as well as through the press.

The SBP continues to act as lender of last resort in providing financial accommodation to banks.

Since July 1997, the SBP adopted a weekly averaging procedure to facilitate management of banks' cash reserve requirements. This procedure gives banks more flexibility in managing their reserves and helps to avoid unintended short-term swings in money market interest rates. Banks are required to maintain average cash reserves of 5 percent on a weekly basis, with a minimum daily balance of 4 percent.

To reduce lending rates charged by banks, the SBP has gradually reduced its 3-day repo rate (discount rate) to 11 percent. Restrictions on banks' maximum lending rates, except those charged in connection with concessionary finance schemes, were removed in 1995, and minimum lending rates were abolished in July 1997. In June 1998, the SBP allowed banks and other financial institutions to determine their deposit rates subject to principles of Islamic banking. Presently, banks and other financial institutions are able to determine their deposit and lending rates independently.

Treasury Bill Auctions

A fixed schedule of auctions was introduced in September 1999 to ensure regularity and transparency for investors. Auctions of Treasury Bills are now conducted on alternate Wednesdays with settlement on the next business day. To remove the mismatch between settlement and maturity dates, the maturity period for 3-month bills is 84 days, for 6-month bills 182 days and for one-year bills 364 days. Tender notices containing necessary information and results of the auctions are posted on Reuters. Information is also published in the leading daily newspapers

Capital Adequacy Requirements

Risk-based capital standards based on the Basel Accord were first applied to banks effective December 31, 1997. All banks operating in Pakistan are required to maintain a minimum 8 percent ratio of total capital to risk-adjusted assets. In addition, banks maintain a minimum paid up capital of Rs.500 million. It is contemplated that these capital adequacy guidelines will be applied in due course to nonbank financial institutions such as development finance institutions, investment banks, house finance companies, discount housing companies and venture capital companies.

PANAMA

Bank Regulatory Developments

The Superintendency of Banks has adopted several regulations implementing provisions of the new banking law relating to the following matters (among others):

- loan limits to (i) a single non-related party, (ii) a single related party, and (iii) two or more persons or companies that constitute a "single economic group" (related and non-related to the bank);
- management and reporting of interest rate risk;
- liquidity requirements and reporting;
- a provision that requires banks in Panama to apply either International Accounting Standards (IAS) or US Generally Accepted Accounting Principles (USGAAP); and

- procedures for non-domestic banks that have branches and subsidiaries with an International License and that consolidate at head office to demonstrate the adequacy of their capital. Such banks are required to meet the minimum capital standards prescribed by their home country supervisor. To demonstrate their compliance with this requirement, such banks must submit to the Superintendency every six months a certification by the external auditor of the head office to the effect that the bank complies on a consolidated basis, including its operations in Panama, with the applicable home country standard.

On June 28, 2000, the Superintendency issued a regulation on "Classification of the Loan Portfolio and the Establishment of Loan Loss Provisions." This regulation distinguishes between corporate loans and personal loans (which include residential mortgage loans). The requirements of the regulation are in line with those of IAS and USGAAP, one of which a bank must adopt (see above).

On Juy 19, 2000, the Superintendency issued Agreement No. 7-2000 containing the regulations for the classification of investments other than loans. These regulations specify that such investments must be classified in accordance with IAS or USGAAP, whichever a bank has adopted.

Anti-Money Laundering Initiatives

The Superintendency of Banks has been actively pursuing the strict compliance by all domestic and foreign institutions with Panamanian laws requiring banks to have and apply "know your customer" (KYC) policies and procedures, as well as reinforcing the system for reporting suspicious operations to the Financial Analysis Unit (FAU), carefully taking all necessary steps, within Panamanian laws and the Constitution, to comply with the recommendations of the Financial Action Task Force on Money Laundering (FATF).

Under current law, the crime of money laundering can arise only in connection with drug trafficking. The government has completed preparation of draft legislation to add a new Chapter to the Penal Code to expand the list of predicate crimes for money laundering to include illegal arms trafficking, kidnapping, extortion, fraud, embezzlement of public funds, corruption of public officials, robbery and smuggling of automobiles and acts of terrorism. The legislation will be presented to the Legislative Assembly when it returns in September from its current recess, and it is expected to be enacted before the end of that month.

Other actions taken by the Government include the reorganization of the FAU, which serves a function similar to the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) and other countries' Financial Intelligence Units, in order to authorize it to transmit directly to the Attorney General's Office any case that arises from its analysis of a reported suspcious activity it determines should be investigated. The modifications also will allow FAU to solicit whatever informaton it needs in connection with a report received in order to complete its analysis and authorize it to enter into mutual agreements for the mutual exchange of informaton with its counterparts in other countries. The Superintendency has been coordinating with the Panama Banking Association to expand obligatory KYC rules and regulations to ratify and confirm that banks cannot open an account for a coproration unless it has full access to the indentity of the beneficial owner(s).

It is intended that the foregoing actions will facilitate Panama’s removal from the list of jurisdictions deemed not to have taken adequate measures to combat money laundering published by FATF on June 22, 2000.

New Securities Legislation

On July 8, 1999, the government adopted Decree-Law No. 1, a new comprehensive law containing 285 articles that creates the new National Securities Commission (NSC) and regulates all activities and instruments in the securities and capital markets. The NSC is governed by three full time Commissioners, each appointed by the President of the Republic for a five-year term. The law provides that a Commissioner, once appointed, can be removed only through a judicial process.

Among other things, the new law regulates the authorization of stock brokers and financial advisors, as well as the authorization and operation of all stock markets. The law regulates for the first time public offerings of securities and also establishes the basic provisions for the regulation of stock registration and reports by issuers. Other provisions of the new law address issues related to custody, compensation and liquidation of securities. The law also specifies prohibited activities and prescribes civil penalties. In addition, it establishes a comprehensive scheme for intervention and liquidation or reorganization of stock brokerage companies, and provides for a system of examinations and confidentiality of information.

The law addresses as well a variety of fiscal matters. For example it provides tax exemptions for profits from the sale of securities issued or guaranteed by the State. It also exempts profits from the sale of securities registered with the NSC that are made through an organized stock exchange or market, that result from a public purchase offer or that is the result of a merger or corporate reorganization in which the shareholder receives stock of the continuing corporation. Interest paid on securities registered with the NSC will be subject only to a 5 percent income tax, but such income will not be included in the total taxable income of the taxpayer.

The new law establishes provisions for the supervision of all securities firms and transactions in derivatives and all securities products, and includes detailed disclosure requirements, margin requirements and requirements for registration and listing on the Panama Stock Exchange.

Market Developments

Several mergers involving banks with operations in Panama occurred during the period under review. Spain´s Banco Central Hispanoamericano purchased Banco Santa Cruz de la Sierra, and then Spain’s Banco Santander merged with Central Hispano, to form the new Banco Santander Central Hispano. Banco Bilbao Vizcaya, also from Spain, bought Colombia´s Banco Ganadero, and more recently merged with the Spanish Banco Exterior Argentaria to form the new Banco Bilbao Vizcaya Argentaria. Banco General, Panama´s largest private bank bought Banco Comercial de Panama, Panama´s fifth largest bank. This was followed by Panama´s Banco del Istmo purchasing Primer Banco de Ahorros to become the largest private bank in both

Panama and Central America. In another transaction, HSBC bought Chase Manhattan´s operations in Panama.

Electronic Banking

Although somewhat slowly, banks in Panama are steadily introducing electronic banking, with some institutions already quite advanced. Twenty nine banks with a General License, three with an International License and two with a Representative License have active websites. Almost all offer for now limited facilities, but one Panamanian bank in particular has already started to offer a wide variety of domestic and international facilities, as it presently owns a bank in a Central American country.

Supervision of Non-Domestic Banking Organizations

As provided for in the banking law on the consolidated supervision of establishments of foreign (non-domestic) banks, the Superintendency of Banks has negotiated information-sharing agreements with the Superintendents of Peru and Costa Rica. Other agreements will follow, as experience with the administration of these two is gathered. The purpose of these agreements is to permit the exchange of information that will facilitate each party's consolidated supervision of banks under its home country jurisdiction. The agreements are for an initial term of three years, which may be extended upon the agreement of the parties. The agreements embody the following principles:

- *reciprocity* – each party will be permitted to participate in on-site examinations of banks from their country in the host country (all examinations in Panama by a foreign supervisor will be cordinated with the Superintendency and with the presence of Panamanian examiners, and copes of the foreign supervisor's examination report will be provided to the Superintendency);

- *pertinency* – the information obtained can be used only for purposes of bank supervision and not for any other purposes such as investigative, fiscal, penal, administrative and political;

- *national treatment* – the scope of the foreign supervisor's examination cannot exceed that of the Superintendency; and

- *confidentiality* – the examination of documents by a foreign supervisor in Panama must be conducted so as not to disclose the identity of depositors, and information obtained by a foreign supervisor may not be transmitted to any other person or authority.

The Banking Law specifically provides that branches and subsidiaries of non-domestic banks with an International License (i.e., that can only conduct foreign operations) are generally subject to the supervision of the Superintendency and to the requirements of the Banking Law. However, for such banks that are subject to consolidated supervision in their home country and operate branches in Panama, the applicable home country requirements will control with regard to their liquidty, capital adequacy and other technical conditions.

Non-domestic banks with a General License (i.e., that can conduct domestic and foreign operations from Panama), will be supervised on a consolidated basis by the appropriate home country supervisor. The local operations of these banks nevertheless remain subject to the requirements of the Banking Law.

Non-domestic banking organizations are subject to the same conditions that the banking law establishes for domestic banks with respect to investments in other non-banking financial businesses. The banking law provides that all banks are limited to invest no more than 25 percent of their capital funds in another non-banking institution, except in connection with securities market activities, among others.

The is no asset pledge requirement for branches of non-domestic banks operating in Panama.

PHILIPPINES

Legislative Developments

The General Banking Law was signed into law by the President of the Philippines last May 23, 2000. The bill amending the Central Bank Act is still pending in Congress and is expected to be enacted before the end of the year.

Bank Regulatory Developments

Restructured Loans

In November 1999, the Bangko Sentral ng Pilipinas (BSP) modified the regulation requiring an independent appraisal company in connection with restructured loans. Under the modified regulation, independent appraisals are required for restructured loans whose outstanding principal exceeds the following thresholds: P5 million, P1 million and P500 thousand for commercial banks, thrift banks and rural banks, respectively.

On June 1, 2000, the BSP issued Circular No. 246 to amend the regulations governing restructured loans to provide that all loans shall be considered non-performing on the date of a restructuring, except loans restructured with updated principal and interest payments.

Capital Adequacy Requirements

On December 24, 1999, the BSP extended the deadline of the second phase (first phase for thrift banks outside Metro Manila and rural banks) of the capital build-up programs of banks from December 31, 1999 to January 31, 2000.

Reporting and Disclosure Requirements

On August 17, 1999, the BSP issued a regulation directing banks to disclose the following information in the quarterly published Consolidated Statement of Condition:

- non-performing loans and their ratio to the total loan portfolio;
- classified loans and other risk assets;
- general loan loss reserve;
- specific loan loss reserve;
- return on equity;
- loans/advances to directors, officers, stockholders and their related interests (DOSRI) and the ratio of DOSRI loans to the total loan portfolio; and
- past due DOSRI loans/advances and their ratio to the total loan portfolio.

On October 20, 1999, the BSP issued a regulation requiring banks and non-bank financial intermediaries with quasi-banking functions (NBQBs) to disclose additional information in the notes to their Audited Financial Statements and Annual Report.

On March 15, 2000, the BSP issued a regulation requiring that a transaction by a bank with its and/or its employees involving chattel shall be reported to the BSP. The bank shall also certify that said transaction was entered into in the best interest of the bank. In a related development, the BSP on March 23, 2000 required that DOSRI rules be applied to credit card operations of banks and quasi-banks in transactions where DOSRI are concerned.

On April 19, 2000, the Monetary Board approved the issuance of a circular requiring the disclosure of the ultimate beneficial owner of shares of stock of banks under the name of the Philippine Central Depository, Inc. in the quarterly report on Consolidated List of Stockholders and Their Stockholdings.

Other Issuances/Developments

- On July 20, 1999, the BSP issued policy guidelines on the election/appointment of directors/officers of commercial and thrift banks in line with efforts to upgrade the quality of corporate governance in the banking sector.

- On September 9, 1999, the BSP issued an amendment of the guidelines on the classification of loans and advances to include *miscellaneous exceptions – loans and advances* which cover loans and advances with technical defects, deficiencies in documentation/collaterals and without up-to-date credit information/audited financial statements which are subject for corrective action during examination.

- In November 1999, the BSP lifted the limitation of an expanded commercial bank's equity investments in an insurance company, allowing up to 100% ownership therein.

- On December 7, 1999, the BSP issued guidelines on the reporting of FCDU liquid cover and on the imposition of a monetary penalty on banks for willful violation of the FCDU cover and other reporting requirements to ensure accurate reporting and to promote banks' foreign exchange liquidity.

- On December 24, 1999, the BSP established a requirement that peso deposits should be funded from inward foreign exchange remittance and prohibiting banks from extending peso loans to non-residents to prevent undue speculation.

- On April 27, 2000, the BSP amended its regulation on the issuance of redeemable shares (Circular No. 241). Under the revised rules, banks may issue redeemable shares subject to additional conditions that the applicant bank has met the prescribed net worth to risk assets ratio during the sixty (60) days immediately preceding the date of application and its accounting records, systems, procedures and internal control systems are satisfactorily maintained.

- On May 5, 2000, the BSP issued guidelines that a bank should seek prior BSP approval before it can provide electronic banking services to ensure that banks have in place a risk management process that is adequate to assess, control and monitor any risk arising from the proposed electronic banking activities (Circular No. 240).

- On May 19, 2000, the BSP issued rules and regulation to govern the accreditation, appointment and reporting requirements for external auditors of universal banks and commercial banks (Circular No. 245).

- On June 2, 2000, the BSP amended its guidelines on the classification of loans, and the provisioning requirements for classified loans.

Regulation of Non-Bank Financial Institutions

As mandated by Republic Act No. 7653 (The New Central Bank Act) the BSP turned over to the Securities Exchange Commission (SEC) its regulatory powers over certain non-bank financial institutions (NBFIs), namely: lending investors (LIs), investment houses (IHs), financing companies (FCs), investment companies (ICs) and securities dealers/brokers (SDBs). However, if the NBFIs are (1) authorized to engage in quasi-banking functions, (2) subsidiaries or affiliates of banks, (3) authorized to engage in trust and investment management operations, and (4) required by law to be under the supervision of the BSP (such as pawnshops, building and loan associations), then they shall continue to be regulated and supervised by the BSP.

Year 2000 Date Change

No significant problems arose in the Philippines financial system in connection with the Year 2000 date change, reflecting the substantial preparations made by financial institutions and the BSP. Some banks opened during the holidays, and all ATMs were made operational to service the banking needs of the public during the critical crossover period.

To cope with the abnormal demand for liquidity arising from apprehensions about the Year 2000, the Monetary Board approved the following liquidity schemes:

- special repurchase facility;
- emergency year 2000 loan facility;

- extension of the compliance period for the reserve position of banks from one week to three weeks; and
- zero reserve requirement on interbank loans.

In addition to these liquidity assistance measures, the BSP also increased its cash inventories through accelerated production of coins and bills.

Anti-Money Laundering Initiatives

On June 22, 2000, the Financial Action Task Force on Money Laundering (FATF) issued a report naming the Philippines as one of 15 jurisdictions that FATF has determined have not taken adequate measures to combat international money laundering. Subsequent to this report, the BSP on July 7, 2000 issued rules and regulations for banks and NBFIs to combat laundering (Circular No. 251). The regulation requires banks and NBFIs to:

- Take reasonable measures to establish the true identity of their clients based on official records or other reliable documents or records when establishing business relations or conducting transactions.

- Prohibit anonymous accounts or accounts under fictitious names.

- Renew/update at least every other year the identity of existing clients or beneficial owners of deposits and other funds held or being managed by the bank.

- Maintain necessary records on transactions, both domestic and international, for at least five (5) years even after the account is closed.

- Give special attention to complex, unusual large transactions and all unusual patterns of transactions which have no apparent or visible lawful purpose.

- Report to competent authorities other suspicious transactions not involving deposits.

- Avoid transacting business with criminals.

- Develop a program against money laundering.

To reinforce these measures, the BSP issued Circular No. 253 on July 31, 2000 to require banks and NBFIs to report certain information (at a minimum, the names of the parties involved, a brief description of the transaction and amounts involved) about the following types of transactions:

- outward remittances without visible lawful purpose;

- inward remittances without visible lawful purpose or without underlying trade transactions;

- unusual purchases of foreign exchange without visible lawful purpose;

- unusual sales of foreign exchange whose sources are not satisfactorily established;

- complex, unusual large transactions, and all unusual patterns of transactions, which have no apparent or visible lawful purpose;

- funds being managed or held as deposit substitutes if thee is reasonable ground to believe that the same are proceeds of criminal and other illegal activities; and

- all other suspicious transactions/activities which can be reported without violating any law.

Developments in the Regulation of Securities Firms and Markets

On September 2, 1999, the Securities and Exchange Commission (SEC) issued Memorandum Circular No. 04 requiring securities representatives/salesmen who failed to renew their licenses for a continuous period of at lease five (5) years to retake and pass the written examination conducted by the SEC or any SEC-authorized institute. Attendance at a securities training course/seminar, however, is not required. The re-qualification requirement has been instituted to ensure that individuals whose licenses have lapsed are familiar with any substantial changes in the securities statutes, regulations and industry practices that may have taken place during the period of the lapse.

The status of the Philippine Stock Exchange (PSE) as a “self-regulatory organization” was suspended on March 7, 2000. Henceforth, the SEC will have direct supervision over broker/dealer firms which are members of the PSE and will conduct routine examinations of broker/dealer firms.

In order to forestall trading by unlicensed individuals, the SEC issued Memorandum Circular No. 10 of 2000 listing guidelines with respect to hands-on or on-the-job training. Under the guidelines, on-the-job training shall be for a period of two (2) months and shall be undertaken only after an individual has passed the Certified Securities Representative Examination. The trainee shall be under the strict supervision of a licensed individual who shall ensure that he applies the knowledge acquired from the training and examination phases in a professional manner. Further, all recommendations made by the trainee-salesman to an investor shall be concurred with by his appointed Supervisor and all orders entered by a trainee-salesman on behalf of an investor must be co-signed by the Supervisor.

House Bill 8015, otherwise known as Securities Act 2000, amending the Revised Securities Act, was approved by the House of Representatives on second and third reading on April 12, 2000. Among the more significant provisions, the amendments:

- Require that stock exchanges be organized in the form of stock corporations.

- Increase penalties (administrative, civil and criminal).

- Codify the “full disclosure” approach to the regulation of companies which publicly offer their securities, are publicly held and/or publicly traded and provide for a more transparent market.

- Increase capitalization requirements of brokerage firms to insure against defaults and protection against market risks.

- Prohibit brokers from acting as dealers, except in certain instances.

- Clarify how self-regulatory organizations (SROs) will be regulated and the SEC's supervisory powers over SROs.

- Require that SEC's regulatory, administrative and quasi-judicial decisions be appealable only to the courts.

- Expand the definition of insider and clarify prohibited market practices such as insider trading in line with international best practices.

With the passage of the Securities Act, the SEC is expected to review all existing rules, make the necessary amendments and promulgate new rules, as appropriate. This process will occur after June 2000.

Regulation of Financing Companies

Significant changes have occurred in the regulation of financing companies as a result of the Republic Act No. 8556, the Financing Company Act of 1998 (Republic Act No. 8556), which amended the Financing Company Act (Republic Act No., 5980). Rules and regulations implementing these changes were adopted during the period under review. They provide as follows:

- A financing company must be organized in the form of a stock corporation in accordance with the provisions of the Corporation Code, subject to the following:

  - At least 40 percent of the voting stock of the corporation shall be owned by citizens of the Philippines.

  - The company must have a minimum paid-up capital of:

    - P10,000,000.00 if it is located in Metro Manila and other First Class Cities;
    - P 5,000,000.00 if it is in other classes of Cities; and
    - P 2,500,000.00 if it is located in a Municipality.

- Financing companies have the power to:

  - engage in quasi-banking and money market operations with the prior approval of the BSP;
  - engage in trust operations subject to the provisions of the General Banking Act upon prior approval by the BSP;
  - issue bonds and other capital instruments subject to pertinent laws, rules and regulations;

- rediscount their paper with government financial institutions subject to relevant laws, rules and regulations;
- participate in special loan or credit programs sponsored by or made available through government financial institutions; and
- provide foreign currency loans and leases to enterprises that earn foreign currency through exports or other means, subject to existing laws and rules and regulations promulgated by the BSP.

- The total credit that a financing company may extend to its directors and stockholders shall not exceed 15 percent of its net worth.

- The total credit that a financing company may extend to any person, company, corporation or firm shall not exceed 30 percent of its net worth.

Market Developments

In July 1999, the BSP amended its guidelines on merger and consolidations incentives so as to expressly allow, with prior approval of the Monetary Board, concurrent directorships. In addition, the BSP now allows the amortization of goodwill up to a maximum period of 40 years.

During the period under review, the SEC approved the merger of the following financial institutions, which are mostly banks:

- DBS Saving Philippines, Inc. (surviving entity) and DBS Savings Bank, Inc.
- Equitable Banking Corporation (surviving entity) and Philippine Commercial International Bank.
- Planters Development Bank (surviving entity) and PDB Leasing Corporation.
- Prudential Bank (surviving entity) and Pilipinas Bank.
- Bank of Philippine Islands (surviving entity) and Far East Bank and Trust Company.
- Bank of Philippine Islands (surviving entity) and Ayala Insurance Holdings Corp.

One foreign company, Sun Life Assurance Company of Canada, has demutualized and converted its local branch to a servicing company. In place of the branch, a wholly-owned subsidiary, the Sun Life of Canada (Philippines), Inc. has been organized.

A domestic company, the Insular Life Assurance Co., is also in the process of demutualization, which is expected to be completed by 2001.

Several banks that own insurance companies have entered into mergers, but have continued to operate them independently from each other.

A moratorium on the establishment of new banks, including pending applications received prior to August 16, 1999, was issued by the BSP, with the following exemptions:

- establishment of a branch/subsidiary or acquisition of an existing domestic bank by a foreign bank pursuant to R. A. No. 7721 ("An Act Liberalizing the Entry and Scope of Operations of Foreign Banks in the Philippines and for Other Purposes");

- establishment of additional branches by foreign banks with existing branches; and
- establishment of new branches by merged/consolidated banks, subject to compliance with certain conditions.

Regulation and Supervision of Non-Domestic Banking Organizations

The BSP independently assesses the capital adequacy of non-domestic banks on the basis of the BSP's own (host country) standards. The required minimum capital adequacy ratio of 10 percent under the General Banking Act (GBA) is the same for domestic and non-domestic banks. The 10 percent capital adequacy ratio is higher than the BIS standard of 8 percent but does not take into account contingent liabilities, and it has only two risk weights – zero for relatively risk-free assets and 100 percent for risk assets (versus the five risk weights provided for under the Basel Accord). In addition, capital accounts under the GBA computation are not classified into tiers 1 and 2.

For Philippine branches of foreign banks, the composition of capital accounts is different from that of domestic banks. Whereas the capital accounts of such branches are computed on the basis of a "net due to" amount, domestic banks' capital accounts are comprised of capital stock, surplus reserves, undivided profits, and an "appraisal increment" resulting from appreciation in the book value of a bank's assets.

Foreign banks that do not meet the minimum host capital requirements are subjected to the same sanctions as local banks. Banks that are not able to meet the minimum capital to risk assets ratio are prohibited from making new investments of any sort except purchases of readily marketable evidences of indebtedness until such time as the minimum required capital to risk assets is restored. For banks that are not able to comply with the minimum capital requirement (absolute amount), there are non-monetary sanctions the imposition of which depend on the degree of capital deficiency incurred by the bank. Among the non-monetary sanctions are: (i) restrictions on overall loan growth/investments; (ii) suspension of authority to engage in derivative activities; and (iii) suspension of Foreign Currency Deposit Unit activities.

Non-domestic banking organizations that operate through branches are not subject to any type of asset pledge requirement.

POLAND

Developments in the Banking Sector

In 1999, economic growth in Poland was lower than projected in the annual Budget, and also lower than in 1998. Poland's Gross Domestic Product (GDP) rose 4.1 percent.

In 1999, the banking sector developed much more slowly than the year before. The total assets of the banking system grew 14.3 percent, or 4.1 percent in real terms (as against 28.7 percent and 18.5 percent in 1998), to stand at 364.4 billion zloty at year end, the equivalent of almost 60 percent of GDP, an increase of 10 percentage points since year end 1995.

Although it has been increasing steadily, the ratio of total banking sector assets to GDP remains low in Poland, whether in comparison with the countries of the European Union or with the Czech Republic and Hungary.

Consolidation and Privatization

The privatization and consolidation of Polish banking industry accelerated in the second half of 1999. The Ministry of the Treasury finalized the privatization of the following banks:

- a consortium of UniCredito Italiano SA and Allianz AG took up a majority holding (52.09 percent) in Bank Polska Kasa Opieki S.A. (August 1999);

- AIB European Investments Limited took up 80 percent of the share capital in Bank Zachodni SA (September 1999);

- foreign investors associated with Denmark's Unibank acquired a controlling interest in Bank Wlasnosci Pracowniczej SA (August 1999).

The following mergers and acquisitions occurred in the second half of 1999:

- Powszechny Bank Kredytowy SA acquired the banking business of Pierwszy Komercyjny Bank SA, incorporating the offices of the latter into its own network as of July 1;

- Bank Energetyki SA merged with Bank Inicjatyw Spoleczno-Ekonomicznych SA on November 22; and

- the consolidation was carried out of 3 banks belonging to Bayerische Hypo- und Vereinsbank AG, which took up a new issue of shares in Bank Przemyslowo-Handlowy SA by means of a non-cash consideration for equity, comprising title to 100 percent of the share capital of Hypo-Bank Polska SA and HypoVereinsbank Polska SA. The latter bank was subsequently merged with Bank Przemyslowo-Handlowy SA on November 11.

The directing bodies of Bank Handlowy w Warszawie SA and BRE Bank SA also took steps towards a merger of their respective banks with the approval of the Commission for Banking Supervision. However, the merger was not consummated owing to the emphatic objections of two shareholders in Bank Handlowy (the PZU insurance company and the Treasury). In Spring 2000, Citigroup expressed interest in purchasing a controlling stake in Bank Handlowy w Warszawie SA and received the approval of the Securities Commission to acquire up to 75 percent shares of Handlowy.

Mergers can also be anticipated among the regional banks and other institutions affiliating local cooperative banks.

As a result of consolidations, the total number of commercial banks declined from 83 at year-end 1998 to 77 at year-end 1999.

Other significant transactions in 1999 include the following:

- Belgium's Fortis Bank NV obtained 98.4 percent of the share capital of Pierwszy Polsko-Amerykanski Bank SA, thus acquiring full control over that bank.

- Germany's DG Bank AG raised its share in the equity capital of Bank Amerykanski w Polsce SA "AmerBank" to 71.1 percent.

- A controlling stake in Bank Komunalny SA was assumed in December by Nordbanken, part of the Finnish-Swedish group MeritaNordbanken.

As a result of privatizations, the number of banks with majority public-sector equity fell from 13 at the end of 1998 to 7 at the end of 1999 (with the number of banks directly controlled by the Treasury dropping from 6 to 3).

Although the number of banks with a majority private-sector interest remained unchanged, the number of banks with majority foreign equity rose from 31 to 39. At the end of December, this group of banks comprised 3 branches of foreign banks, 16 joint-stock banks under 100 percent foreign ownership, 17 with a majority foreign interest, and 3 banks indirectly controlled by foreign investors.

The banks controlled by foreign capital in fact have a market share in excess of 70 percent.

Year 2000 Date Change

Due to extensive readiness programs undertaken by the Polish banking industry, no problems were encountered in connection with the Year 2000 date change.

PORTUGAL

There has been continuing supervisory flexibility with respect to country risk assessments. During the period under review, for example, a more favorable approach has been permitted regarding loans backed by some multilateral banks, namely the International Bank of Development and Banco Latinoamericano de Exportaciones (BLADEX).

Risk-based capital ratios have been revised to permit the supervisory authority to require a ratio in excess of 8 percent when deemed necessary.

A new Securities Code has been published, simplifying the previously very detailed legislation and introducing important changes for the improvement of the capital market, including authorizing the private ownership of the Stock Exchange.

In light of the increasing complexity in supervising financial institutions, in particular as the result of the development of financial conglomerates, the Ministry of Finance has announced that efforts are underway to develop institutional cooperation among the three existing financial supervisory authorities: Banco de Portugal (banking), Instituto de Seguros de Portugal (insurance) and Comissão do Mercado de Valores Mobiliários (securities markets).

There were no significant problems experienced in Portugal in connection with the Year 2000 date change.

The authority of a non-domestic banking organization to expand its nonbanking activities in Portugal, whether directly or through acquisitions, is not subject to assessment of its capital adequacy or management by the host country regulator.

Non-domestic banking organizations that operate branches in Portugal are not subject to any type of asset pledge requirement.

ROMANIA

Organization of Financial Regulatory Authorities

Law no.32/2000 provides for the establishment of the "Insurance Supervision Commission" as an independent administrative body under the authority of the Parliament dedicated to the supervision of insurance companies and their activities. The Commission operates separately from the already existing regulatory and supervisory authorities for banks (National Bank of Romania) and securities firms (National Commission for Securities).

Regulation and Supervision of Banks

Significant Actions by the National Bank of Romania (NBR)

- Circular no.22 of September 10, 1999 amends the provisions of NBR Rule no.3/1997 regarding foreign exchange operations by liberalizing certain foreign exchange operations representing capital outputs.

- Norm no.9 of September 27, 1999 specifies how assets and liabilities are to be calculated for purposes of determining the solvency of Romanian banks, and prescribes how these items are to be reported in financial statements. According to Norm no. 9, a bank is insolvent if the value of its liabilities exceeds the value of its assets (i.e., the value of its net assets is negative).

- Norm no.10 of December 20, 1999 amends Norm no.2/1999 regarding the licensing of banks.

- Norm no.11 of December 20, 1999 amends Norm no.3/1999 regarding changes in the organization of a bank.

- Rule no. 7/1999 specifies that a bank's capital shall consist of two tiers (core capital and supplementary capital), lists the components of each tier and prescribes the methodology for calculating capital.

- Rule no. 8/1999 (replacing NBR Rule no. 5/1992, NBR Rule no. 10/1992 and NBR Rule no. 4/1994) establishes a minimum Tier 1 capital ratio of 8 percent, increases the minimum solvency (Tier 1 and Tier 2 capital) ratio from 8 percent to 12 percent, and prescribes corresponding changes to banks' recordkeeping requirements. In addition, banks are required to report on a monthly basis their net loans to connected persons, own staff (and their family members) and are prohibited from lending to their own staff (and their family members) on terms more favorable than granted to unaffiliated persons.

- Circular no.2 of January 10, 2000 provides for valuation of foreign exchange assets and liabilities at prevailing market rates. In addition, it provides that revaluation reserves shall be determined on the basis of the market value of the "Lei" as published by the NBR.

- Regulation no.1 of March 30, 2000 provides the NBR greater flexibility in connection with its money market operations by authorizing its use of certain "core instruments" (e.g., outright trading, repos/reverse repos, swaps) and credits (overnight, special) to cover the refinancing needs of the banking system.

- Order no. 27 of January 18, 2000 implements NBR Regulation no.1/1999 regarding the organization and functioning within the NBR of the "Credit Risks Bureau".

Establishment of the Credit Risks Bureau

The "Credit Risks Bureau" was established on February 1, 2000 as the repository of credit-risk related information supplied by all Romanian banks. The Bureau maintains two data bases: (i) the Central Register of Credits, which records the monthly balance of bank credits, and (ii) the Register of Outstanding Credits, which records credits whose principal amount is at least 200 million lei.

Pending Bank Regulatory Initiatives:

- Issuance of new NBR Rules regarding consolidated financial reporting, the supervision of banks on a consolidated basis, the establishment of a liquidity ratio and updating the Early Warning System for identifying "problem" banks.

- Passage of legislation enabling the NBR to exercise sole regulatory and supervisory authority over the operations of credit institutions and credit cooperatives.

- Passage of legislation providing that a bank shall be deemed to be insolvent if its solvency ratio is less than 2 percent.

Year 2000 Date Change

No significant problems occurred in the banking system in connection with the Year 2000 data change.

Regulation of Derivatives and Securities Products

A rather active market in one-month financial futures contracts has developed on the Commodity Exchange in Sibiu, and consideration is being given to the development of a regulated financial derivatives market.

Market Developments

The most significant transaction during the period under review was the merger of BANCOREX into Banca Comerciala Romana S.A. on October 10, 1999.

SINGAPORE

Introduction

There has been no let-up in the government's efforts to develop Singapore into a world-class financial center. In fact, with the Asian economic crisis receding into memory and with the rebound in regional economic growth, the Monetary Authority of Singapore (MAS) has been unwavering in taking follow-up measures to ensure that the Republic emerges as a key financial hub in the region. During the period under review, the MAS has implemented a raft of measures in its continuing deregulation and liberalization of the financial sector.

Banking Developments

On October 20, 1999, MAS announced the award of Qualifying Full Bank privileges to the following foreign banks: ABN Amro Bank, Banque Nationale de Paris, Citibank NA and Standard Chartered Bank. MAS also gave another eight foreign banks Qualifying Offshore Bank privileges and awarded new Restricted Bank licenses to eight other foreign banks. These moves followed the May 17, 1999 MAS announcement of a five-year program to liberalize access by foreign banks to Singapore's domestic market.

Meanwhile, the locally incorporated banks have been gearing up to meet the competition posed by the greater access given to foreign banks. All local banking groups have established Nominating Committees which will decide on the persons most suitable and qualified to be appointed to their respective boards and to senior positions in the bank's management. In addition, the banks have retired older Directors – some of them in their eighties – and appointed younger persons (and, in some cases, foreign bankers) to replace them.

The local banks have also moved quickly to take advantage of technological means for delivering their services. They have introduced online banking to complement their branch banking. Some banks have also introduced e-banking within their existing structures; others intend to establish stand-alone e-banks. These e-banks are subject to all the current requirements imposed on traditional banks. MAS is expected to release guidelines for e-banking sometime in 2000. Similarly, a couple of banks have begun divesting certain non-core assets while others are waiting for the MAS to issue guidelines on this matter first.

Also in the interest of greater efficiency, banks in Singapore are working towards "check truncation". Under this process, checks are scanned electronically at the point of deposit. The digital image, rather than the physical check itself, is then transmitted to the clearing house for sorting before onward transmission to the paying bank. According to MAS estimates, using check truncation can save the banks some S$46 million a year.

In keeping with moves to deregulate and liberalize the banking sector, the Association of Banks in Singapore announced on July 20 1999, that it had decided to let banks pay interest on current accounts, lifting a 23-year restriction. It had also decided to allow banks to accept fixed deposits of any amount for any duration. Previously, fixed deposits could not be for less than one month unless they exceeded S$1 million and then had to be for at least seven days.

In a speech on April 3, 2000, MAS Chairman B.G. Lee Hsien Loong outlined the possibility of further banking liberalization. The MAS will track the progress of the banking liberalization program and, after reviewing its status in 2001, it will decide on further steps to open up the sector. The MAS will continue discussing with the local banks ways to increase bank transparency further (e.g., by disclosing more information on remuneration and incentive structures, related party transactions, the banks' risk profiles and their risk management processes).

The MAS is also reviewing the existing Minimum Liquid Assets and Minimum Cash Balance requirements imposed on backs and the capital requirements for financial holding companies and banking groups. This is because Singapore banks should not be unnecessarily disadvantaged vis-a-vis foreign competitors. The MAS is also reviewing bank involvement in non-financial activities and the cross-holding structures in Singapore banking groups. However, this is a complex issue which MAS will study carefully and discuss with the banks.

Developments in the Bond Market

In line with Singapore's objective of becoming a leading international debt hub in Asia for the issuing, arranging and trading of bonds and other fixed income securities, the MAS announced several measures in October 1999 which are designed to boost the local bond market. The most significant change is exemption of banks from maintaining minimum cash balance and minimum liquid asset requirements on Singapore dollar funds received from non-bank customers through foreign currency swaps which have original maturities of one year or more. The exemption is aimed at promoting more competitive pricing and boosting liquidity in the long-term swap market. At the same time, the MAS said it is considering further relaxation of guidelines on the use of the Singapore dollar, and exemption of bond holdings from restrictions under the Banking Act.

In November 1999, further moves to liberalize the Singapore dollar vis-a-vis the bond market were announced. These measures built on earlier initiatives which made it easier for foreign entities to list S$ shares and issue S$ bonds, and swap the S$ proceeds into foreign currency for use outside Singapore. The new measures included:

- removing the S$20 million consultation limit on Singapore dollar repurchase (repo) transactions with non-residents;

- allowing banks to transact Singapore dollar over-the-counter interest rate products with non-residents freely without the need for consultation with the MAS; and

- Allowing rated and unrated foreign companies and countries to issue Singapore debt denominated bonds to widen the credit spectrum of foreign entities tapping the S$ bond market.

In addition, the MAS opened up the financial guarantee Insurance business to foreign insurers in August 1999. This will provide a boost to developing bond and capital markets as it will help regional quasi-sovereign issuers with major recapitalization needs to access the bond market. Financial guarantee insurers can guarantee the bonds of regional issuers who were hit by the regional crisis and could not get investment grade ratings for their bonds. Through the guarantees, they can improve the yield or pricing of their bond issues.

The bond market measures have seen very encouraging results, as Singapore's debt market has experienced significant growth over the past two years. The outstanding amount of Singapore Government Securities (SGS) has risen from S$25.4 billion in mid-1998 to S$36.1 billion at the end of 1999, representing a 33.5 percent increase. Last year saw S$9.2 billion worth of non-government S$ issues, more than double the amount raised in 1998. Singapore statutory boards have also issued S$2.6 billion of S$ bonds since October 1998.

Foreign entities have responded positively to the liberalization of the S$ guidelines. To date, a total of more than S$4 billion worth of S$ bonds have been issued by foreign entities, including supranationals, US and European corporations and financial institutions. Asian names such as Cheung Kong Holdings and the Housing & Commercial Bank of Korea have also tapped the S$ bond market for their funding needs.

The S$100 million bond issue by Housing and Commercial Bank of Korea, Korea's largest mortgage lender, represents the first non-investment grade debt offer in Singapore. This may help open up a new source of funding for other Asian companies seeking money as the region recovers from the financial turmoil which started in 1997.

The MAS has announced further steps to improve the efficiency and liquidity of the bond market in 2000. First, to boost liquidity in the repo market, the MAS announced that it will introduce an SGS repo facility that will be available to primary dealers. This facility comprises a fixed pool of benchmark SGS bonds which primary dealers can access via a daily repo auction. The repo facility will provide another avenue to primary dealers to cover short positions in benchmark issues arising from their market-making activities, and will make it more attractive for financial institutions to be SGS primary dealers.

Second, to further encourage greater repo activity, MAS also announced that SGS held under term reverse repos with banks will qualify as liquid assets, subject to a maximum limit of 5 percent of the liabilities base. SGS obtained from reverse repos with nonbank entities will also qualify as liquid assets. In addition, MAS will allow offshore banks to engage in SGS repo transactions with non-bank customers as part of their capital market activities. Previously, only SGS obtained under overnight reverse repos with banks qualified as liquid assets. This restriction has hindered the development of the repo market.

Third, MAS will embark on a focused SGS issuance program to raise the average benchmark sizes from the current typical sizes of about S$1.5 billion to at least S$2.0 to S$2.5 billion, subject to assessment of market conditions. This is to create larger and more liquid benchmark issues to facilitate secondary trading, and substantially increase total SGS free float from the current S$12.0 billion. The MAS said that the success of recent bond auctions indicated that the market had developed greater capacity to absorb larger SGS issuance sizes without significant price pressures.

Fourth, MAS will cease performing the role of an SGS broker for primary dealers. This is to allow for the bulk of the SGS trading to be transacted through commercial brokers or through direct dealings between primary dealers, thereby making the price discovery process more transparent and efficient. Bid-ask spreads in the broking market can be expected to narrow with greater participation by primary dealers and secondary market participants.

The MAS has said that it will work closely with the financial industry to develop more measures to broaden and deepen debt market activities. These include developing the asset-backed securitization market in Singapore as well as the feasibility of establishing a mortgage corporation.

Developments in the Equities and Derivatives Markets

Major changes were made, especially in regard to the equities market. On September 20, 1999, the then Stock Exchange of Singapore (SES) amended its Listing Manual in line with some of the key recommendations of the Corporate Finance Committee (CFC) released in November 1998. The 14-member CFC had called for the SES to adopt a disclosure-based regulatory regime and ease the listing rules in order to develop Singapore into an attractive center for international fund-raising activity.

The changes to the Listing Manual included easing the roles for chain listings, reducing the minimum free float size for Main Board companies, allowing foreign companies to list on the second-board SESDAQ and the scrapping of the Foreign Board. Regarding chain listings, the SES had previously barred the listing of subsidiaries which contributed more than 50 percent of the listed parent's profits. It had also barred the listing of a holding company if its assets and business were substantially held through a listed subsidiary. Instead of using these quantitative criteria, the SES will henceforth look at the applicant's business and its commercial reasons before deciding whether to approve a separate listing.

The Foreign Board had been set up three years previously to encourage regional infrastructure companies to list in Singapore. With its abolition, regional infrastructure companies henceforth will list on a main board or SESDAQ. Also for the first time, the SES specified in its Listing Manual that SESDAQ-bound companies would not be subject to any minimum requirements on share capital, profit or operating record. However, in terms of shareholding spread, 15 percent of the shares had to be held by a minimum of 500 persons.

With these changes, local and foreign-incorporated companies need not show any minimum paid-up share capital in order to seek a listing. Previously, local companies had to have S$15 million in paid-up capital, while foreign companies had to have S$30 million. Companies will now be able to seek a Main Board listing using three alternative routes: showing

S$7.5 million in pre-tax profit in the preceding three years with at least S$1 million in each year; an aggregate profit of at least S$10 million in the preceding one to two yews; or a market capitalization of S$80 million, based on its initial public offering's (IPO) issue price. This amendment is meant to make it easy for fast-growing high-tech companies which have a short but strong profit record, or have yet to make profits, to list on the main board.

In addition, the requirement for a minimum period of "continuity of shareholder control" over Main Board-listed companies was removed. Those qualifying for listing under the S$80 million market capitalization criterion did not need to show "continuity of management" either, although the new management that took over would have to prove relevant experience and expertise. Those listing under the S$7.5 million profit rule must still have a three-year management continuity while those with S$ 10 million profit would need management continuity for one or two years. The SES will also use its discretion to allow Main Board-listed companies with market capitalization exceeding S$300 million to have a free float which was less than the previously stipulated 25 percent.

On December 1, 1999, the SES was merged with the futures exchange, SIMEX (Singapore International Monetary Exchange), to form the Singapore Exchange (SGX). The SGX thus became the first de-mutualized, integrated securities and derivatives exchange in the Asia-Pacific region. It expects to list on itself before the end of this year. In conjunction with the launch of SGX, the government unveiled new initiatives to enhance the competitiveness of Singapore's capital markets. The key changes are as follows:

Liberalized commissions

- From January 1, 2000, commissions for large trades (above S$150,000) will be fully negotiable. Minimum commission on retail trades (below S$150,000) will be lowered to 75 basis points. For approved fund managers, commissions on all trades would be fully negotiable.
- From January 1, 2001, commissions on all trades will be fully negotiable.
- For online trades, the exchange will evaluate feasibility of fully liberalizing commissions sooner, before January 2001.

Open access for foreign brokers

- From January 1, 2000, International Members will be allowed to accept trades above S$500,000, compared to above S$5 million previously. The limit will be removed altogether in January 2001.
- New members will be admitted from July 2000 and no quota on the number of new members will be set.
- New members will be able to trade directly with local investors for trades above S$500,000. The limit will be reduced to S$150,000 after one year, in July 2001, and then removed completely from January 2002.

Broadening brokers' business

- Brokers will be allowed to manage idle cash balances of clients through cash management accounts. However, they might be required to apply for a separate investment adviser's license to do so.

- Brokers will be allowed to manage money market funds and offer financial advisory services.

Capital requirements

- From January 1, 2000, dealers need only inform MAS when the aggregate indebtedness to adjusted net capital ratio exceeded 8 times.

- From January 1, 2000, the statutory minimum paid-up capital for member dealers is reduced from S$30 million to S$15 million. The minimum adjusted net capital requirements are reduced to S$5 million.

Shortened settlement period

- From March 15, 2000, settlement for share trades is three days after transaction date (T+3) compared with the previous T+5. The goal is to further shorten the settlement period to T+I.

Among other developments concerning SGX, the following are noteworthy:

- Draft prospectuses. It was announced on September 18, 1999 that a company will be allowed to issue a draft prospectus (commonly referred to as a red herring) to help determine the level of investor interest in its IPO.

- Insider trading lawsuits. Other changes allow civil proceedings against insider trading to take place. The time limit for action against insider trading was also extended from two to six years.

- Guidelines for online share offers. On February 14, 2000, the Singapore Ministry of Finance, the Registrar of Companies and Businesses and the MAS jointly issued guidelines on the public offer of shares, debentures and unit trusts on the Internet.

- Alliances with other exchanges. The SGX signed a Memorandum of Understanding (MOU) with the Australian Stock Exchange Ltd on April 12, 2000, establishing a formal linkage through which the two exchanges can share information. On April 28, 2000, an MOU was signed with the Tokyo Stock Exchange calling for general co-operation between the two Exchanges for the purpose of contributing to the development and efficient operation of the Japanese and Singaporean markets, as well as to investor protection. Meanwhile, it was reported that the Chairman of the New York Stock Exchange had hinted strongly in April that an agreement could be reached within a few months to link the U.S. market with the SGX.

Developments in Fund Management

On September 18 1999, the government announced changes to the CPF Investment Scheme (the CPF, or Central Provident Fund, is a government-run pension fund). From December 1, 1999, CPF members are allowed to invest only 50 percent (as against 80 percent previously) of their investible funds in individual stocks. However, there is no limit when the CPF savings are invested in unit trusts, fund management accounts, insurance policies, statutory board bonds and government issued and guaranteed bonds. This change will boost the fund management industry, among others.

In his FY2000 Budget Statement in Parliament on February 24, 2000, Finance Minister Dr. Richard Hu announced that the Ministry of Finance will introduce a Supplementary Retirement Scheme, expected to be implemented by 2001. The scheme will offer workers an additional method of saving for retirement. The voluntary contributions will be tax-deductible when paid in, and taxed only upon withdrawal (the scheme would be similar to the 401(k) accounts in the United States). If the scheme should become widely accepted, it would give a boost to the fund management and annuities industry.

On April 3, 2000, the MAS Chairman said that the government will put out more money for fund managers to manage. This will be over and above the fund managers' access to the large pool of CPF funds as well as government funds made available by the MAS and the Government of Singapore Investment Corporation. The government will also encourage individuals to be more active in managing their retirement savings. Not only will this help develop the fund management industry, it will also promote the desired spirit of self-reliance and personal responsibility among Singaporeans.

Developments in the Insurance Industry

The MAS announced on March 17, 2000 that, with immediate effect, it was lifting the closed-door policy on direct insurers and brokers, and the 49 percent shareholding limit on foreign ownership in locally-owned direct insurers. This is in furtherance of Singapore's aim to become Asia's premier insurance hub by 2003. The MAS Chairman had earlier given notice on August 16, 1999 that the government would throw open the doors to new direct insurers in an attempt to foster the development of a more efficient and forward-looking industry. He revealed then that the government wanted to develop a few local insurance players who could compete effectively with foreign participants in the local as well as foreign markets. But, unlike the banking industry where there was a clear rationale for partial protection – as it was critical to monetary policy, the domestic payments system and intermediation in the economy – the case for protecting local insurers was weaker.

However, the MAS said that the admission of new entrants will "be paced out to minimize the risk that the sudden entry of many new players, all intent on building up market share, will pressure new and existing insurers to pursue unsound, short-term market practices." The criteria for entry of new direct insurers would be based on their:

- domestic and international rankings;
- present and past credit ratings;

- track record and reputation with regard to compliance with regulations and the strength of internal control systems; and
- commitment to Singapore's development as a regional insurance hub and international financial center.

For new insurance brokers, the MAS also wants to see their world rankings, reputation, financial standing, track record, business plans and projections. Meanwhile, the government will encourage local insurers to merge or form strategic alliances. This applies especially to the 44 companies in the general insurance business, most of which have only a small market share.

Also, as already mentioned above, the MAS announced on August 24, 1999 that it had amended a regulation opening up the financial guarantee insurance business to foreign insurers. It said it had issued the Insurance (Financial Guarantee Insurance) (Amendment) Regulations 1999, allowing multi-line insurers and re-insurers to engage in financial guarantee insurance business, thereby easing a previous restriction that allowed only Singapore-incorporated subsidiaries of specialized financial guarantee insurers to operate in Singapore. With the amendment, foreign financial guarantee insurers are permitted to set up branch operations to do business in Singapore.

Looking ahead, the MAS Chairman said on April 3, 2000 that the MAS needs to promulgate a framework for capital adequacy that is risk-based and which enhances standards of corporate governance and market conduct in the insurance industry. This would encourage innovation in the industry and at the same time safeguard the interests of policyholders. He revealed that MAS will also work with the industry to raise disclosure standards to the levels of international best practice. He added that in developing the insurance industry the aim is to service emerging opportunities in the Asian market. The MAS will also promote new insurance activities, such as specialized underwriting skills and Alternative Risk Transfer activities.

SOUTH AFRICA

Regulatory Developments

The Policy Board for Financial Services and Regulation, a statutory board with the function to oversee policy integration of financial services regulation, has been re-constituted. Included in its work program for 2000 and 2001 is a comprehensive review of regulatory structure, including the issue of whether there should be a single financial services regulator.

Significant changes to the Banks Act Regulations will be implemented on July 1, 2000 after eighteen months of research and consultation with the industry. Detail of the changes has been published on the South African Reserve Bank, Bank Supervision Department (BSD) website (www.resbank.co.za).

The most significant changes are:

- **improved asset classification –** explicit and mandatory loan classification and provisioning rules that are in line with international best practice have been incorporated into the Regulations;

- **lowering of large exposures and connected lending –** restrictions have been tightened in line with international best practice;

- **enhancement of corporate governance in banks**;

- **improved public disclosure –** more comprehensive requirements to ensure timely dissemination of information required for the assessment of banks;

- **improved reporting of market risk -** trading banks will be required to distinguish between trading and banking activities, and to calculate and report their capital adequacy requirements for trading purposes on a daily basis;

- **reduction of the limit on net effective open currency position -** net effective open position in foreign currency may now be managed to within 10 percent of qualifying capital and reserves;

- **improved cooperation between the regulator and auditors -** further reporting requirements will be introduced for external auditors of banks in order to provide additional assurance on key information;

- **improved management of risks in derivative instruments -** banks will be required to report derivative instruments separately and to distinguish clearly between certain types of contracts; and

- **more frequent and meaningful reporting -** the reporting intervals at which banks have to submit risk-based returns have generally been reduced, and most information will be calculated on average daily balances instead of month-end positions.

Year 2000 Date Change

The transition occurred smoothly throughout the financial services sector, and there were no reports of Y2K date-related problems. This was attributable to thorough preparation and careful supervision.

Banks are now poised to take advantage of large-scale technology renewal and investment, as well as systematic rationalization of systems and processes.

The Regulation and Supervision of Securities Firms, Insurance Firms, Commodities Firms and Other Non-Bank Financial Institutions

This is the responsibility of the Financial Services Board (FSB). The large-scale consolidation of legislation governing the various market participants embarked upon last year is nearing completion.

Anti-Money Laundering Initiatives

Money laundering remains an issue of concern to regulators. Although South Africa does have legislation that requires the reporting of suspicious transactions, the intelligence agency required to perform an integrated analysis of such incidents (aimed at uncovering money laundering networks) has not yet been instituted. Most banks have already implemented the basic preventive measures.

Supervision of Non-Domestic Banking Organizations

The domestic bank supervisory authority has established effective mechanisms for supervisory cooperation with host country supervisors of South African banks operating in foreign jurisdictions, as well as home country supervisors of foreign banks operating in South Africa. Host regulators have been satisfied with the conduct of South African banks in their jurisdictions.

Regulations relating to the conditions under which branches of foreign banks operate in South Africa will also change on July 1, 2000. These changes will allow branches to operate on the strength of their parents' balance sheets with respect to some prudential restrictions. Branches will also be permitted to take retail deposits for the first time.

Market Developments

In line with global developments, the South African financial system, and the banking sector in particular, are undergoing substantial structural changes. Financial institutions and markets are significantly affected by global competitive pressures, domestic competition, technological developments, evolving strategic objectives of financial institutions and the resulting changes in regulation. The pressure of deregulation and competition has resulted in major diversifications and there has occurred a decisive shift towards the emergence of financial conglomerates. The competitive environment intensified markedly as financial institutions faced global competitive pressures as well as domestic inter-sector competition. To date, however, no mergers between any of the big four banks in the South African banking sector have taken place.

Electronic Commerce and Banking

As far as electronic commerce and banking is concerned, the regulators have decided to implement regulations as the market develops and regulations are deemed necessary. The Reserve Bank is currently researching an appropriate regulatory framework for electronic commerce and banking.

SPAIN

The most important legislative and regulatory developments in the banking sector during the period under review are the enactment of the new law on securities payment and settlement systems (Law 41/1999) and the promulgation of new rules on bad debt provisions (Bank of Spain circulars 9/99 and 10/99).

Law 41/1999 incorporates into Spanish law European Union Directive 98/26/CE on secure settlement in securities payment and settlement systems with the intention to reduce legal risks arising from the temporary insolvency of the parties within the system and to encourage an efficient trans-border payment system within Europe.

As far as the Bank of Spain Circulars 9/1999 and 10/1999 are concerned, these have established, along with the traditional specific and generic provisions for bad debts, a statistical hedging fund to cover the underlying risk in asset portfolios and off-balance sheet exposures. This new hedging fund, which will be implemented in the second half of 2000, will be available for use in years of negative economic growth to reduce the impact of provisions on the profit and loss account. The calculated impact of the new fund, until it reaches the volume set as its objective (three times the historical risk for each type of asset) will be about 10 percent of the banks' annual profits.

Other recent regulations which merit mention are (i) the new law of personal data protection, which has incorporated all of the European Union Directive 95/46/CE on this subject into Spanish law, and (ii) the Royal Decree on implementation of company pension scheme commitments, which regulates how these schemes must externalize their commitments through the creation of a pension fund or an insurance policy and sets forth the requirements and conditions for banks to remain exempt from this obligation.

The most significant market development during the period under review was the merger of Banco Bilbao Vizcaya and Argentaria, two of the largest Spanish Banks.

As a final matter, it is noted that in Spain the authority of a non-domestic banking organization to expand its nonbanking activities is not subject to an independent assessment by the Spanish regulatory authorities of the capital adequacy or management of the organization as a global entity. The branches of non-domestic banks are not subject to any type of asset pledge requirement.

SWEDEN

Regulatory Developments

According to a decision in the EU Court of Justice, national law may not prohibit insurance companies from holding shares representing more than 5 percent of all voting rights in a public limited company. Sweden used to have such a law, which was repealed effective January 1, 2000.

The Parliament has also decided that public limited companies listed in Sweden have the right to buy and transfer their own shares, beginning from March 10, 2000. However, a company is not permitted to own more than 10 percent of its shares.

A new law on settlement of obligations in the financial market came into force on January 1, 2000. The law implements an EU directive on this subject and makes certain amendments to the law on trade with financial instruments.

The Government has sharpened the rules about insider trading and has decided to shorten the time for reporting of shareholdings by insiders from two weeks to five days. Those working in a security firm must report their own shareholdings to their employers. Penalties have been introduced for persons leaking delicate information.

Two thirds of the delegates at the extra-party congress of the Social Democrats voted for Swedish membership in the EMU. They also decided that the final decision shall be an object for a referendum. The governing party has consequently said yes to EMU, but when the referendum will take place is still uncertain.

Year 2000 Date Change

The year 2000 date change caused only minor problems in the Swedish financial sector, all of which were solved rapidly. No general systematic faults, virus attacks or trespassing by hackers has been reported.

Market Developments

Four large banks in the aggregate account for more than 80 percent of the volume in the Swedish credit market, making it one the most concentrated in Europe. However, in certain sectors there is significant competition, including from non-domestic banking organizations.

The large Swedish bank groups continue to expand their international operations and now include banks and other financial companies in the Nordic and Baltic States, Poland and Germany. There have been many structural mergers during the last year. SEB acquired Germany's fifth largest private commercial bank, BfG Bank, from Crédit Lyonnais. Swedbank purchased the Danish FiH Bank. The property insurance company "If" has been established, behind which are the largest insurance companies in the Nordic countries.

At the beginning of 2000, the Finnish-Swedish MeritaNordbanken announced an amalgamation with the Danish Unidanmark, resulting in the establishment of Unibank as the Danish part of a large Nordic bank. Efforts are also underway to find a Norwegian partner that would make the bank by far the largest in the Nordic region.

Electronic Banking

Technical development in the Swedish banks is very rapid. The number of Internet customers has more than doubled in the last year and is now close to two million. In response to this development, one of the four largest banks, SEB, closed 50 of its 250 branches in Sweden (more than 25 percent of its customers are Internet customers). The bank is now working on establishing a "pan-European Internet platform", primarily in Denmark and Germany initially and later in Great Britain.

Supervision of Non-Domestic Banking Organizations

A non-domestic banking organization's expansion of its nonbanking activities in Sweden is not subject to any assessment of its capital by the Swedish regulatory authority, the Finance Inspection. In general, capital is assessed on the basis of home country standards. Non-domestic banks with branches in Sweden are not subject to any type of asset pledge requirement.

SWITZERLAND

Amendments to the Banking Act

The Swiss Federal Banking Act was amended in 1999 as to the status of so-called cantonal banks and the legal basis for on-site inspections by foreign supervisory authorities.

- **Cantonal Banks.** Under the new article 3a of the Banking Act, the status of state-owned "cantonal banks" has been slightly modified. A bank may use the word "cantonal" (i.e., state) in its name only if it is chartered under a canton's law or, if chartered as a limited corporation under federal law, the canton controls at least two thirds of its shares and voting rights. It is, however, no longer required that a cantonal bank's liabilities are guaranteed by the canton.
- **Global Supervision.** Under the new article 23^{septies} of the Banking Act, on-site inspections by foreign bank supervisors in Switzerland are permitted under certain conditions. First, they have to be aimed at the consolidated supervision of a bank or other financial intermediary. Second, the customers' privacy rights must be safeguarded by the foreign authority. Third, any information gathered by foreign supervisors in Switzerland may be transmitted to foreign criminal prosecutors only if and as far as the prerequisites of mutual assistance in criminal matters are fulfilled (e.g., punishable in both countries). On-site inspections are designed as an exception to the principle that information on Swiss banks is gathered and transmitted to the requesting foreign authority by the Swiss Federal Banking Commission (SFBC) under article 23^{sexies} of the Banking Act. Information about individual depositors and owners of managed portfolios is not available "on-site" but has to be gathered and transmitted exclusively by the SFBC to the requesting foreign authority.

Special Unit for the Supervision of Big Banks

During the years 1998 and 1999, the Swiss Federal Banking Commission established and staffed a specialized unit for the supervision of the two big internationaly active banking groups (UBS AG und Credit Suisse Group).

Group of Experts on "Financial Market Supervision"

The Federal Department of Finance appointed a group of experts to critically analyze the system of financial market regulation and supervision in Switzerland. The Swiss Bankers Association (SBA) is represented in this group of experts.

In particular, it is the group's mission to assess the strengths and weaknesses of Swiss financial legislation and to compare the Swiss regulatory system with those in other countries as well as with supranational standards and guidelines. Special attention is given to recent developments such as new categories of risk and to the points of contact between banking supervision and insurance regulation.

Year 2000 Date Change

In order to make optimum millennium change preparations for Switzerland as a financial center, the Y2K Interbank Group established by the Swiss banking sector initiated a Contingency Planning project in January 1999. This included the design and operation of a Central Command Center in Zurich to monitor the Year 2000 date change with respect to Swiss financial institutions.

The Center started round-the-clock operations as planned from December 31, 1999 until January 5, 2000. The Center was staffed with representatives of Swiss banks, the Swiss National Bank, the Swiss Federal Banking Commission, the Swiss Post Office (Postfinance), the Swiss Exchange (SWX), the Swiss Interbank Clearing Center (SIC) and the securities clearing company SIS. The Center also contained a press office operated by the Swiss Bankers Association.

Regular telephone conferences and a comprehensive status reporting system ensured the Center was abreast of developments throughout Switzerland during critical periods. A Quick Reaction Team and Y2K Executive Committee ensured key decisionmakers were on hand to take action in the event of any problem or escalating crisis. The Center was also in contact with external command centers, including those run by the police, utility companies and telecom providers.

In the event, not a single problem was reported to the Center during the entire period of operation. In the Center's final press release on January 5, 2000, Werner Brupbacher, Chairman of the Interbank Group's Y2K Steering Committee, said: "The fact that we were always on hand, ready to tackle any problem, together with the fact that we were always in a position to take decisions, was of great psychological value to members of Switzerland's financial community and their customers and helped ensure that the situation was always under control."

TURKEY

Banking Law No. 4389

Enacted in June 1999, this law establishes a new financially and administratively autonomous body to undertake the supervisory functions previously exercised by the Central Bank, the Treasury and the Sworn Board of Auditors. Named the “Banking Auditing and Regulation Institution”, this organization is empowered to implement banking and related laws, issue banking regulations and coordinate with foreign supervisory authorities. The Institution is headed by the Banking Regulation and Supervision Board, which is comprised of seven members, each serving a six-year term. One of the members is appointed Chairman, and another is appointed Second Chairman. The first Board was chosen in March 2000, and the Institution will commence operations in August 2000.

Other significant provisions in the Law are as follows:

- The Board is responsible for granting and revoking banking licenses.

- The minimum capital requirement for establishing a bank is increased to 20 trillion TL.

- Lending limits are increased from 20 percent to 25 percent of capital.

- The definition of "loan" is changed to correspond to the definition applied in EU banking directives. Consequently, banks will have to reclassify their "equity participations" as loans rather than as equity, but they are given six years to effect this reclassification.

- For the first time, large exposure limits are defined in accordance with EU directives, with the limit set at 8 times capital.

- Acquisition or transfer of banks' shares representing 10, 20, 33, 50 percent and higher is subject to the Board's prior approval.

- Banks are required to establish appropriate internal control and risk management systems and to prepare their financial statements on a consolidated basis, including direct and indirect participations and partnerships.

- The Law adopts enhanced measures to address the problems of banks whose financial condition weaken.

- Responsibilities and liabilities of bank owners and managers are increased. In addition, the criminal and administrative penalties that can be imposed on banks are increased in amount and number.

Bank Regulatory Developments

Effective January 1, 2000, the Standard Ratio for Foreign Currency Net General Position/Capital Base is decreased from 30 percent to a maximum of 20 percent.

Decree No. 99/13761, published on December 21, 1999, requires that more stringent loan loss provisioning (i.e., more aligned to international standards) be applied to all new loans, as well as to the renewal of any existing loans, as of January 1, 2000. Under this Decree, banks are required to categorize their loans and other receivables into five subdivisions ranked according to recoverability and creditworthiness. Provisions are to take into account the value of any collateral securing the loan or receivable as well as the bank's ability to liquidate the collateral without legal impediment.

Effective June 30, 2000, banks are required to apply capital adequacy and foreign exchange exposure limits on a consolidated basis. As a corollary, banks are required to issue consolidated financial statements. Reporting requirements have been increased from twice a year to quarterly.

As announced in the Official Gazette on December 10, 1999, the reserve requirement ratio has decreased from 8 percent to 6 percent. On the other hand, 2 percent of domestic currency deposits is to be held as free deposits with the Central Bank. This new liquidity requirement may be met on the basis of average daily balances during the reserve requirement period rather than on a continuous, daily basis.

Tax Developments

The Ministry of Finance had contemplated radical changes in the tax law starting with the year 2000. To prepare for these changes, taxpayers were asked to declare their financial holdings by blocking them in a financial institution on a certain date. As a result, assets including cash, foreign currency, certificates of deposit and other similar assets exceeding a specified limit were blocked in one of the financial institutions operating in Turkey on September 30, 1998. These assets, however, were not investigated as to their source. The date September 30, 1998 and the new system that was contemplated were referred to as the Financial Millenium (or as the Financial Cornerstone). Taxpayers also declared the amount of income they have gained in a certain period and above a certain amount, according to the new broader definition of income brought by the Financial Millenium. However, the Tax Law postponed the Financial Millenium, and declarations made by taxpayers were not used and taxpayers paid their taxes according to the income definition in the existing tax law. Hence, there is not an obligation of declaration of the interest income earned and that will be earned by taxpayers from deposit accounts and repos between 1999-2002, whatever the amounts are. These earning will be subject to withholding tax as they used to be.

Against this background, Tax Law No. 4369 was revised in August 2000 as follows:

- The period for capital gains treatment on the sale of marketable securities is reduced from one year to three months.
- No transactions shall be carried out depending on the declarations made on September 30, 1998.
- Non-wage income tax rates are increased by 5 percentage points.
- From December 31, 1999, shares and participation certificates of mutual funds that hold at least 51 percent of their portfolios in the stocks of Turkish companies shall be valued at their purchase price, while all other marketable securities shall be valued at their market value.
- The provisional corporate tax rate on gains, that is calculated every six months, is reduced from 25 percent to 20 percent. The Board of Ministers is authorized to increase or decrease the rate by 5 points.
- Gains from the sale of immovable assets or shares in a subsidiary that add to the institution’s capital are exempted from corporate tax.

- Exemption from income tax is continued for gains derived through the sale of the issued stock (at the establishment of a joint stock company or when it increases its capital) at a price above their nominal values.

- The Board of Ministers is authorized to change the revaluation rate used in the calculation of real estate tax base between zero and the rate declared.

The Government passed a new law increasing taxes to help meet part of the huge costs resulting from two recent earthquakes in Turkey. With respect to the banking sector, the additional taxes included a tax on interest on government bonds issued before December 1, 1999 (the amount of the tax ranges from 4 percent to 19 percent, depending on the maturity of the bond) and an additional corporate tax of 5 percent.

Payment Systems Developments

The new "Electronic Fund Transfer System" commenced operation on April 24, 2000. The System incorporates enhanced risk controls and is designed to permit a greater variety and volume of payments.

Year 2000 Date Change

The banking and financial sector encountered no significant problems in connection with the Year 2000 date change.

Market Developments

Six new banks entered the banking sector in 1999. Four of these newly established banks were development and investment banks, and the other two were the branches of foreign banks. The banking license of one bank in the development and investment banking group was cancelled.

As of May 2000, the number of banks operating in Turkey (excluding the Central Bank) increased to 81, 62 of which are commercial banks and 19 of which are development and investment banks.

The management of 5 privately-owned commercial banks – Yurtbank, Esbank, Yasarbank, Egebank and Sumerbank – were taken into the Savings Deposit Insurance Fund on December 12, 1999, thereby increasing the number of banks managed by the Fund to 8.

UNITED KINGDOM

Introduction

Most UK banks delivered healthy earnings growth and returns on assets and equity last year with the help of a positive economic climate, low inflation and low bad debt experience.

But other developments highlighted the difficult climate within which they are operating. The take-over of National Westminster by the Royal Bank of Scotland emphasized the danger that a bank that seems to have lost its way can soon become a take-over target and raises the question of whether there is room for further consolidation in the UK banking industry.

Also posing a threat is the development of non-traditional sources of financial services thanks to new technology and e-commerce. Insurance companies and supermarket chains have stretched their brands into the banks' territory and do not have the significant 'bricks and mortar' costs of the traditional UK banks. Internet banks are being established to cherry pick the most profitable segments of their personal customer business. As a result, cost cutting and greater job flexibility and movement are a common feature to all banks in their UK networks.

Regulatory Developments

The past year has seen the UK regulatory regime move closer to the creation of a single regulatory body for all financial institutions – the Financial Services Authority (FSA). The Financial Services and Markets Act (FSMA) received Royal Assent in June 2000.

The legislative process resulting in the FSMA, from the announcement of the planned change, to the publication of the draft legislation in July 1998, has employed two constitutional innovations; the use of a joint Committee of both Houses of Parliament and the carrying over of the Bill from one session of Parliament to the next. In the course of parliamentary scrutiny there were 2,000 amendments and 200 hours of debate despite the fact that there was broad cross-party support for a single financial services regulator.

But the FSMA is only a framework. Before it comes into force at 'N2', probably in the third quarter of 2001, the FSA's detailed rules setting its modus operandii need to be finalized.

These Rules and Evidential Provisions, along with supporting Guidance will be encapsulated in the FSA Handbook in four main blocks:

Principles
Business Standards
Regulatory Process
Redress

The FSA's Principles set the overall standards by which any financial services firm, be it a bank, insurance company or independent financial advisor are expected to conduct themselves. There are 11 Principles which require a firm to:

- *conduct its business with integrity;*
- *use due skill, care and diligence;*
- *organize and control its affairs responsibly and effectively, with adequate risk management systems;*
- *maintain adequate financial resources;*
- *observe proper standards of market conduct;*
- *pay due regard to its customers' interests and treat them fairly;*

- *communicate information to its customers clearly, fairly and in a way that does not mislead;*
- *manage conflicts of interest fairly;*
- *take reasonable care with its advice and discretionary decisions;*
- *arrange adequate protection for customers' assets; and*
- *deal with its regulators openly and co-operatively.*

The other three blocks will deal with prudential standards, conduct of business and market abuse as well as authorization, enforcement and the FSA's supervision process.

The industry is particularly concerned about the FSA's attitude to enforcement in the new regime, which could make it 'prosecutor, judge, and jury'. Over the course of the parliamentary scrutiny of the FSMA the FSA's role has been made more administrative and less judicial, with firms being given the right to refer enforcement decisions to an independent Tribunal. This Tribunal will be able to assess all the evidence for itself. Although procedural rules for the Tribunal have yet to be published it is to be hoped that they will allow for a swift, fair and cost effective resolution of issues so that cases do not become bogged down in legal procedures.

Post N2, the FSA will identify a number of key regulatory themes to which it will devote its attention and there will be less routine monitoring of small, low-risk firms and fewer rules. Themes will be selected based on their urgency, the impact they may have on firms and whether they can deliver measurable outcomes - the FSA is required to be efficient and economic in its use of resources and to assess the cost and benefits of regulatory burdens.

The FSA is already piloting thematic projects including:

- *e-commerce and its consequences for consumers and risk management in firms;*
- *the impact on consumers and firms of a low inflationary environment;*
- *treatment of customers after the point of sale; and*
- *the interface between money laundering and financial exclusion.*

This risk-based approach is designed to change the culture of regulation – previously compliance with rules and regulations might have been seen as a substitute for genuine risk management. Now an assessment will be made of the firm's risk management practices. The more the FSA believes that there is a strongly embedded compliance culture and effective risk management function the less intrusive into the firm's activities it will be.

Social exclusion

New competitors for the banking market such as supermarket and Internet-based banks, which are not burdened with a costly branch network, have forced banks to reconsider the viability of a number of their more marginal outlets. They have come under pressure for closing little used branches as their customers adopt different ways of managing their money, such as telephone or Internet-based banking, remote ATMs and cash back at supermarkets. Perhaps unfairly, it is often the last bank to leave a local community that suffers the greatest public opprobrium.

The issue of financial and social exclusion has come into the political limelight. Government is concerned that whilst most people in Britain have benefited from rising living standards, those in the poorest communities have fallen behind. It contends that the economic opportunity for these people to improve their lot is restricted by a lack of access to bank accounts and other financial services.

A further driver for government is that it wishes to pay social security benefits directly into bank accounts, saving significant administration costs and cutting fraud. Axiomatically, this cannot be done unless the poorest elements in society have a basic account.

The UK banking industry has responded to calls that it play its part in reducing social exclusion by developing basic bank accounts which provide a debit card and withhold credit until both the customer and the bank feel comfortable with it. A number of banks have also formed alliances with the Post Office so that banking services can be delivered through its 18,500 strong national network. Shared branches are another option that is being reviewed. Banks are also starting to work with locally based credit unions which can be best placed to contribute to help the less well-off by encouraging them to save and providing low cost, small loans as well as financial education.

While the traditional British clearing banks are keen to ensure everybody has access to basic bank accounts, they do not expect to make money on basic accounts. Banks are more likely to provide loss-making products to reduce financial exclusion if government recognizes that it benefits too from this and plays its part in creating incentives to ensure all the different stakeholders in this debate are satisfied. A particular problem is that government currently expects only traditional branch-based banks to provide basic accounts, thereby exacerbating the pressure from new, non-branch banks.

The Cruickshank Report

In November 1998 the UK Chancellor commissioned a report (the Cruickshank Report) on competition in the UK banking market (apart from investment banking). Issued earlier this year, the report asserted that banks are making excess profits and that there are competition failures in the small business sector and in the provision of payment services. The special treatment given by government to banks, whereby competition controls are not applied very strictly in recognition of the importance of the financial infrastructure, was also criticized.

The main recommendations of the report were that:

- the small business banking sector should be referred to the Competition Commission;
- a new payments regulator – PayCom - should supervise the licensing of payments networks;
- there should be better information to help customers find the best banking deal available; and
- there should be a stronger policy framework for the government's approach to banking services.

The UK government has acted on the first two recommendations and agreed to take the other two forward. This despite the report's acknowledgement that international comparisons showed the

UK to be one of the cheapest and most innovative banking market places and the industry's belief that the report's conclusions were based on very tenuous analysis so should not form the basis for government policy.

Taxation

A number of developments in tax legislation have affected banks over the past year. Among these are:

- *Reporting of investment income collected for and interest paid to non-UK resident individuals*

The Finance Bill 2000 requires UK banks to report to the Inland Revenue annual details of interest paid to non-UK resident individuals. It also requires banks to report details of non-UK source dividends and interest dividends collected for individuals. The changes apply to income collected or paid from April 2001. Detailed regulations will be published in the autumn of 2000. Information collected by the Inland Revenue will be made available to the tax authorities of a number of other countries, but only if there is a reciprocal agreement for similar information to be supplied by the foreign tax authority.

The new legislation is closely linked to the proposed changes to the European Union's draft directive on taxation of cross-border savings income. In June 2000, the EU finance ministers reached a preliminary agreement in principle that the directive should be based on an exchange of information about cross-border interest payments to individuals. This replaces the previous proposal that would have allowed each country to deduct a withholding tax as an alternative to providing information. The EU states are committed to promoting similar measures in dependent territories and entering into discussions with key countries outside the EU (including the United States and Switzerland).

- *Double tax relief for companies*

From March 31, 2000, new legislation governing credit relief for underlying tax on foreign source dividends will come into force. It will no longer be possible to average tax rates on dividends from high and low tax countries by channelling shareholdings through an offshore holding company (typically in the Netherlands). By such "mixing" it was often possible to achieve an underlying tax rate close to the UK corporate tax rate. A limited form of onshore mixing will be introduced but will favour investments held directly rather than through an offshore holding company. It is possible that a number of UK-owned multinational groups will need to reorganize their corporate structure.

- *Innovative tier 1 regulatory capital*

In response to British Bankers' Association representations the Inland Revenue formally agreed that tax relief should be given for interest payments on innovative tier 1 regulatory capital.

- *Foreign exchange, financial instruments and interest payments*

The Government has decided to consult on ways of simplifying the corporate tax treatment of income and expenses arising from exchange rate movements, financial instrument transactions and corporate interest payments.

- *Foreign currency tax returns*

The ability of certain trading companies to file tax returns and calculate taxable profits in non-sterling currencies has been extended to investment holding companies. Indeed, any company, trading or non-trading, that prepares accounts in a foreign currency will be required to calculate taxable profits in that currency for accounting periods commencing after December 31, 1999 (or, by election, after June 30, 2000).

- *Group relief for capital losses*

It will now be possible for UK resident companies within a group to offset capital gains in one company against capital gains in another. Similarly, relief can be obtained between a UK branch of a foreign company and a UK resident subsidiary.

- *Group relief for trading losses*

From April 1, 2000 it will be possible to set trading losses of a UK branch of a foreign company against profits of a related UK company. Similarly, trading losses of a UK company can be offset against profits of a UK branch of a related foreign company.

The Euro

There remains considerable uncertainty as to the possible entry of the UK into the single European currency, and banks are not prepared to make a significant investment in system changes required to accommodate the euro until a firmer timetable is established. The UK Treasury has published its second Outline National Changeover Plan (after consultation with the banking industry among others) which sets out a provisional model of how different sectors of the economy might migrate to the euro during the transition period.

This would involve the wholesale financial markets and large corporates using the euro from the point of UK entry and smaller businesses and individuals switching over later in the transition period. So volume demand for euro retail banking services might not occur until, say, one year after UK entry. This possibility of a phased scenario is based on the experience of the first wave of EU Member States.

The changeover plan also discusses progress in a number of different areas including public sector planning, public information campaigns, and aspects of cash changeover.

Although the UK is not yet a participant in the single European currency, the City of London is already fully engaged in trading euro-denominated foreign exchange, money market instruments and securities and has been since the birth of the euro at the beginning of 1999.

Conclusions

The environment in which UK banks operate continues to change, spurred by technological, regulatory, cultural and societal developments. In order to survive in this developing marketplace, banks will have to focus even more on what their customers' want and tailor delivery channels and craft prices accordingly. But the wider choice and transparency that tougher competition brings will be good for the UK consumer, who is destined to benefit from the turmoil currently affecting the UK banking industry.

UNITED STATES

Enactment of Financial Modernization Legislation: The Gramm-Leach-Bliley Act

Expanded Powers for Financial Holding Companies

Enactment of the Gramm-Leach-Bliley (GLB) Act on November 12, 1999 culminated efforts over the last two decades to pass comprehensive financial modernization legislation that enables the combination within an affiliated financial group of an entire array of financial activities ranging from commercial banking to securities underwriting and dealing, insurance underwriting and merchant banking. The GLB Act provides banking organizations two options for engaging in these expanded financial activities:

- The activities may be conducted through nonbank subsidiaries of bank holding companies that qualify as "financial holding companies" (i.e., each depository institution subsidiary must be (and remain) "well capitalized" and "well managed" and have at least a "satisfactory" rating in addressing the financial needs of its community under the Community Reinvestment Act (CRA)). For these purposes, a depository institution subsidiary is "well capitalized" if it has a minimum Tier 1 and total risk-based capital ratio of 6 percent and 10 percent, respectively, and a minimum leverage ratio (Tier1capital to total assets unadjusted for risk) of 5 percent. Bank holding companies that do not qualify as financial holding companies may continue to engage in the more limited range of activities determined by the Federal Reserve Board prior to enactment of the GLB Act to be "closely related to banking" (this includes underwriting and dealing in corporate debt and equity securities subject to the so-called "Section 20"revenue restrictions prescribed by the Board).

  The respective primary bank regulators (e.g., the Office of the Comptroller of the Currency (OCC) in the case of national banks and the state banking agencies in the case of state-chartered banks) and functional regulators (e.g., the Securities and Exchange Commission (SEC) in the case of securities broker-dealers, and state insurance commissioners in the case of insurance companies) oversee the bank and specialized nonbank subsidiaries of a financial holding company, with umbrella oversight of the consolidated group entrusted to the Board.

- The GLB Act also authorizes national banks, with the approval of the OCC, to engage through "financial subsidiaries" in the expanded financial activities that are permissible for financial holding companies, except merchant banking and insurance underwriting. Among other conditions for the establishment of a financial subsidiary, the national bank must be (and remain) "well capitalized" and "well managed" and have at least a "satisfactory" CRA rating. The activities of national banks and their financial subsidiaries are overseen on a consolidated basis by the OCC, with the appropriate functional regulator responsible for oversight of individual financial subsidiaries.

International banks are eligible under the GLB Act to be treated as financial holding companies, and thus engage in the expanded financial activities permissible for financial holding companies, subject to capital and management standards "comparable" to those required for domestic institutions. The GLB Act directs that these standards be applied by the Board, "giving due regard to the principle of national treatment and equality of competitive opportunity." In its exercise of this authority, the Board has adopted a regulation requiring that international banks that seek to become financial holding companies have a Tier 1 and total risk-based capital ratio of at least 6% and 10%, respectively (for banks from countries that have adopted risk-based capital standards consistent with the Basel Accord, this determination is made on the basis of home country standards), and a minimum leverage ratio (Tier 1 capital to total assets unadjusted for risk) of 3%. International banks that do not satisfy these criteria nevertheless may become financial holding companies if the Board, in its discretion, determines that their capital is "otherwise comparable to the capital that would be required for a U.S. bank owned by a financial holding company." In addition, the Board's regulation calls for a finding by the Board that the management of an international bank as a global entity "meets standards comparable to those required of a U.S. bank owned by a financial holding company."

While the Board has been flexible in applying these standards to international banks, the requirements it has imposed in its regulation have been the source of considerable debate and comment. The Institute, the European Commission and others have raised particular concerns regarding the Board's imposition of a <u>leverage test</u> on international banks, regardless of whether an international bank is subject to any such test under its home country capital standards. In this connection, it has been suggested that the "well capitalized" standard applied to international banks should be based entirely on the internationally agreed upon Basel risk-based capital methodology and that international banks should not be subject to a leverage requirement as a condition to expanding their nonbanking activities in the United States unless and until such a requirement were incorporated into the Basel Accord.

Merchant Banking Activities

As indicated above, merchant banking activities authorized under the GLB Act are permissible only if conducted through a financial holding company. Financial subsidiaries of national banks are prohibited from engaging in merchant banking activities for at least five years after enactment of the GLB Act. The Act provides that at the end of this five-year period, the Board and the Treasury Department, based on their assessment of the experience of financial holding companies, may jointly adopt rules authorizing financial subsidiaries to engage in merchant banking activities permissible for financial holding companies subject to such terms and conditions as they may jointly deem appropriate.

In May 2000, the Board adopted an interim rule restricting both the aggregate amount of merchant banking investments that a financial holding company may have at any time and the period of time that a merchant banking investment may be held, both of which were opposed by the industry. At the same time, the Board proposed that financial holding companies deduct 50 percent of the value of their merchant banking investments for purposes of determining their regulatory capital. This proposal, which has not been finalized, was the subject of Congressional hearings at which serious concerns regarding the anticipated adverse implications of such a requirement were expressed.

Section 114

A provision of the GLB Act with potentially great significance to international banks is Section 114, which, as applied to international banks, provides the Board authority to impose restrictions on relationships or transactions between a *U.S.* branch or agency and any *U.S.* affiliate of an international bank. Reflecting efforts by the Institute, the European Commission and others, the inclusion in the GLB Act of a geographical limit on the scope of the Board's authority over international banks under Section 114 clarifies that such authority does not apply to the *non-U.S.* operations of international banks vis-à-vis their U.S. affiliates (e.g., head office funding of U.S. securities and other affiliates).

Securities "Push Out" Provisions

In connection with its emphasis on functional regulation, the GLB Act requires that banks (including the U.S. branches and agencies of international banks) transfer to SEC-registered broker-dealers all of their securities activities except those specifically identified in the Act as being permissible for banks to continue to conduct directly. These so-called "push out" provisions are effective in May 2001, 18 months after enactment of the GLB Act. Questions have arisen regarding the scope of the statutory exemptions from the push out, particularly as they relate to banks' conduct of their private banking activities.

Regulatory Developments

Regulations under the GLB Act: Privacy

At the federal level, the most significant regulatory developments during the period under review related to implementation of the GLB Act. In addition to the regulations discussed above regarding the application of the GLB Act's "well capitalized" and "well managed" standards to international banks and the regulatory restrictions applicable to the conduct of merchant banking activities by financial holding companies, regulations implementing the GLB Act's privacy provisions were adopted. These provisions require each financial institution to disclose to those of its individual (but not corporate) customers its policies and procedures with respect to protecting and disclosing to affiliates and non-affiliates "nonpublic personal information" relating to the customer and to give each such customer the opportunity to "opt out" of disclosure of such information to non-affiliates.

Although the new privacy requirements thus generally apply only to individual rather than corporate customers, and therefore are expected to have less of an impact on international banks than domestic banks, those international banks that have U.S. private banking operations or otherwise offer financial services to individual customers in the United States face potentially significant new compliance burdens. To provide financial institutions adequate time to develop the procedures and systems necessary meet these requirements, the regulators have delayed the date for full compliance with the regulations until July 1, 2001, although they have stated that institutions are expected to begin compliance efforts substantially before that date and have instructed their examiners to begin reviewing implementation efforts as part of their regularly scheduled examination over the coming year.

Loan Loss Reserves

During the year, controversy regarding the appropriate accounting treatment for loan loss reserves resurfaced as the American Institute of Certified Public Accountants (AICPA) issued a draft proposal providing that a reserve may only be recorded when a bank can document an actual loss. The industry and the bank regulators have expressed their strong opposition to this proposal, with the regulators issuing proposed guidelines endorsing the current practice of reserving for losses that have not yet occurred based upon management's best estimate of the probable amount of losses that will occur given current information and events. The regulators' proposed guidelines remain open for comment until November 6, 2000.

Federal and State Asset Pledge Requirements

The Institute is continuing its efforts to seek substantial reductions in the asset pledge requirements applicable to U.S. branches and agencies of international banks under federal and state law. Under these provisions, branches and agencies are required to keep on deposit with a bank in the state in which they are located liquid assets such as U.S. government securities that are held free of any encumbrance and thus would be readily available to the appropriate agency in the event of their liquidation.

At the federal level, the International Banking Act of 1978 provides that branches and agencies licensed by the OCC must at all times pledge assets in an amount equal to at least 5 percent of their total third-party liabilities. Requirements under state laws vary. For example, branches and agencies licensed by the State of Illinois are not required as a general matter to pledge assets, although the Commissioner retains the discretion to impose an asset pledge requirement when deemed "necessary and appropriate". New York-licensed uninsured branches and agencies are currently subject to an asset pledge requirement equal to 5 percent of their third-party liabilities. For a number banks, this requirement results in the pledge to the Superintendent of Banks of hundreds of millions of dollars (and, in certain instances, more than $1billion) of assets.

The Institute has proposed that the regulatory cost and burden resulting from existing asset pledge requirements be reduced by (i) capping the amount of assets required to be pledged at a level substantially below current federal and state requirements and (ii) permitting the pledge of a broader range of assets in satisfaction of the requirement (i.e., any asset that is acceptable as collateral at the Federal Reserve Discount Window).

Year 2000 Date Change

No significant problems were experienced by the financial services industry in connection with the Year 2000 date change. The successful transition to the new millenium was the result of the extensive preparations undertaken throughout the industry in conjunction with the guidance provided by the regulatory authorities.

Anti-Money Laundering Initiatives

"Know your customer" (KYC) issues were an important focus of Congressional hearings held in the second half of 1999 with respect to Russian money laundering activities and Citibank's private banking business. These hearings resulted in the introduction of legislation at the end of 1999 that seeks to combat money laundering activities conducted from outside the United States through a combination of enhanced regulatory requirements and expanded federal enforcement powers.

This legislation would create a private banking statutory KYC requirement for domestic depository institutions (including U.S. branches of international banks) and contains other provisions imposing KYC requirements in connection with transactions by such institutions with a "foreign entity" or involving a payable-through account maintained for a "foreign banking institution." In addition, the legislation would prohibit a depository institution from opening or maintaining a correspondent banking account for a foreign banking institution unless the foreign banking institution is (or is an affiliate of a banking organization that is) subject to comprehensive supervision or regulation on a consolidated basis by the appropriate home country authority.

On the enforcement side, the legislation would enhance U.S. law enforcement agencies' power to prosecute money laundering, expand the list of activities outside the United States that can provide the basis for a money laundering prosecution in the United States and extend the jurisdiction of federal courts to the non-U.S. offices of international banks in connection with actions to impose on such banks civil money penalties for money laundering in the U.S.

No action has been taken on this legislation. However, on June 8, 2000, the House Committee on Banking and Financial Services approved the "International Counter-Money Laundering and Foreign Anticorruption Act of 2000" (H.R. 3886). This legislation, which is different from the legislation discussed above, would provide the Treasury Department broad discretionary authority to identify specific foreign jurisdictions, financial institutions and classes of transactions that are of "primary money laundering concern" to the United States and to impose on domestic financial institutions, including the U.S. branches and agencies of international banks, "special measures" to address these concerns. Such measures range from enhanced due diligence ("know your customer") requirements to the prohibition of opening or maintaining certain accounts in the U.S. through which money laundering transactions could be effected. While the approach taken in H.R. 3886 is more flexible than that of the earlier legislation, concerns have been expressed regarding the potential breadth of the discretion accorded the Treasury Department and how the special measures might be implemented.

No further action has been taken on H.R. 3886 or any other anti-money laundering legislation. With its adjournment scheduled for before the upcoming Presidential election, Congress has yet to develop any consensus on the various anti-money laundering legislative proposals that have been introduced, and the prospects of enacting any such legislation this year are thus diminishing.

Tax Matters

Global Dealing Regulations

The Institute has continued its discussions with the Treasury Department and Internal Revenue Service (IRS) regarding finalization of the proposed global dealing regulations issued in March 1998. The proposed regulations are of great significance to the international banking community. When finalized, they will dramatically improve the substantive rules governing the U.S. taxation of the securities, derivatives and foreign currency dealing operations of international banks and their affiliates.

Under the proposed regulations, the amount of profits from a cross-border dealing operation that are taxable by the United States—regardless of whether the U.S. activity is conducted through a branch or a corporation or partnership—is to be determined on the basis of the arm's length principle generally applicable to other transfer pricing situations. Thus, the portion of the profits taxable by the United States would be limited to the relative economic value of the contribution of the U.S. branch or affiliate to the activity.

While the Institute has expressed its strong support for the overall approach of the proposed regulations, it has criticized certain specific aspects, including their approach to capital and risks associated with capital. On the basis of its discussions, the Institute is optimistic that the final regulations will allow for greater flexibility in the treatment of this issue.

Interest Expense Deduction

Throughout 2000, the Institute has continued its discussions with the Treasury Department regarding the approach that is being explored by the Treasury Department and an OECD Steering Committee of possibly adopting a uniform international approach, based on the Basel risk-based capital standards, for determining the amount of interest expense that a multinational bank would be entitled to deduct for tax purposes in the various countries in which the bank conducts business.

The Institute has raised the concern that adoption of a Basel-based approach to determining a bank's deductible interest expense could have a significant adverse impact on the worldwide tax position of many multinational banks. Preliminary indications are that the Basel-based approach generally would increase the amount of capital allocated to a multinational bank's U.S. and other non-home country branches (because banks tend to concentrate their low-risk weighted assets in their home office), thereby shifting deductible interest expense from the U.S. and other branches to the home country and increasing the tax burden on multinational banks outside their home country. (The overall impact of a Basel-based approach on the worldwide tax position of any particular bank will, of course, depend on the interplay of numerous factors.)

Moreover, the Institute believes that even after allocating capital to the various branches of a bank under the Basel-based approach, those branches could not conduct the business that they conduct or fund their activities at the attractive borrowing rates that they incur if they were treated as completely separate entities unrelated to the bank. Accordingly, adjustments need to be made for the intangible benefits that arise from each branch being part of the bank as a whole.

The Institute has prepared and circulated for comment a more developed summary of the arguments that the Institute has been articulating against the use of a Basel capital-based approach, which includes a possible alternative approach for determining a multinational bank's deductible interest expense in individual countries. Very generally, under this approach, a bank's worldwide capital would be allocated among its branches in accordance with the relative amount of assets shown on the books of each branch, as determined for financial (or regulatory) accounting purposes (i.e., not on a risk-weighted basis and without regard to off-balance sheet exposures). However, adjustments would be made for (1) branch-booked assets that do not generate income taxable in that country and assets that generate taxable income but are booked elsewhere, and (2) securities repos and other situations in which direct tracing is appropriate.

A consensus has been developing that the Institute should submit this alternative approach to the Treasury Department and the IRS for consideration by the OECD Steering Committee.

Developments Regarding Qualified Intermediaries (QIs) and IRS Withholding Regulations

On May 15th, the IRS released further guidance regarding the QI procedures and also revised the final withholding regulations in a variety of technical respects, in response to comments from the Institute and other interested parties.

The final withholding and reporting regulations, which will become effective on January 1, 2001, will require extensive changes to the operating systems and procedures of international banks and their affiliates, and most financial institutions will need to expend substantial time and effort during this year to modify their operational systems and procedures to comply with the regulations, regardless of whether they become QIs. The QI procedures are intended to reduce in certain important respects the information gathering and reporting burdens that non-U.S. financial intermediaries and their customers would otherwise bear under the new rules.

In response to criticism by the Institute and other interested parties, the IRS announced that it would not restrict the QI procedures to financial institutions operating in countries with which the U.S. has a tax treaty or information exchange agreement. However, the IRS will continue to insist that the institution's country must have "know your customer" ("KYC") rules that are acceptable to the IRS before the IRS will enter into a QI agreement with the institution. An important exception is that the IRS will permit a branch of a financial institution (but not a separate affiliated legal entity) located in a country without acceptable KYC rules to be part of the financial institution's QI agreement provided that the branch agrees to apply the institution's home country KYC rules.

The IRS also announced that it will apply stricter audit and enforcement standards to financial institutions and their branches that are located in countries that are tax havens or that impose bank secrecy rules.

VENEZUELA

Developments Regarding the Regulation and Supervision of Banks

Since the banking crisis of 1994-1995 the financial system has been declared in a state "financial emergency". A series of financial emergency laws have been enacted to address the situation through the creation of financial emergency boards.

On October 22, 1999, The Financial Regulation Law was enacted establishing a new directing body for the financial sector, the Financial Regulation Board. The Board is to be the directing body for the sector until a new banking law is passed. It is composed of five members: the Minister of Finance, who is the head of the Board, the president of the Central Bank, the Superintendent of Banks, the president of the Deposit Guarantee Fund (FOGADE – the state deposit insurance corporation) and a government representative selected by the President of the country.

Financial assistance for failing banks has to be approved by the Financial Regulation Board. In the event the amount of financial assistance provided exceeds 75 percent of the deposit insurance fund, the Central Bank is required to provide funds from the Treasury or from the public issue of government bonds. The provision of financial assistance triggers the immediate substitution of the failing bank's management and the transfer of majority ownership of the bank and its related companies to FOGADE. If necessary, the Executive Branch can order the bank's nationalization.

Upon liquidation of a bank, FOGADE is required to pay each depositor up to 4,000,000 bolívares (approximately US$ 5,800.00), although the Financial Regulation Board has the discretion to require payment of all deposits, as was recently the case in connection with the resolution of an investment bank, CAVENDES.

Venezuela applies capital requirements consistent with the Basel Accord. In July 1999, the Office of the Superintendent of Banks announced an increase in bank's minimum capital requirements, both risk-adjusted and non-risk adjusted. The timetable laid down is to increase risk-adjusted capital requirements from 9 percent in September 1999 to 12 percent in December 2000 through three 1-percent increases spread over the period. The non-risk adjusted capital requirement will increase during the same period from 7 percent to 10 percent.

Since 1994, the deposit insurance premium charged by FOGADE has been equal to 2 percent of a bank's total deposits. As discussed below, on August 28, 1999, this amount was decreased to 0.5 percent.

In August 1999, the Central Bank raised the legal requirement from 15 percent to 17 percent of total deposits, with a 1- percent of investments penalty for non-fulfillment. In August, the portion of the legal requirement required to pay interest was raised from 4 percentage points to 6 percentage points.

The Central Bank has also established limits on the net foreign currency position permissible for commercial and universal banks, thrifts and money market funds. The applicable limit depends on the type of activity conducted by an institution, its risk profile and its control systems. Real estate and leasing companies are subject to a limit equal to 5 percent of capital, whereas the limit for investment banks, commercial banks and universal banks is 15 percent of capital.

Since October 1999, banks have been authorized to issue commercial paper with the prior approval of the Comisión Nacional de Valores (the chief securities regulatory body). To be eligible to issue such paper, a bank must have at least 10,000,000,000 bolívares (approximately US$14.5 million) in capital.

Market Developments

Consolidation continues throughout the financial system. The system is now composed of 87 institutions, including 41 universal and commercial (specialized) banks. Since July 1999, one universal bank and one commercial bank were established, while two investment banks, a savings and loan bank, a money market fund and a leasing company ceased operations.

On August 28, 1999 the Minister of Finance, the Venezuelan Banking Association, the Office of the Superintendent of Banks and the Venezuelan Central Bank signed an accord with a series of commitments designed to reduce interest rates on loans and increase interest rates on deposits. The package includes a reduction in the contributions payable to FOGADE) (see above) and the assessments charged by the Office of the Superintendent of Banks. It also contemplates that the Central Bank will increase the percentage of the legal requirement to be remunerated. The Superintendent also agreed to reduce general provisions from 2 percent to 1 percent of loans in order to finance the margin reduction. Banks were required to reduce their spreads by 3 percentage points by increasing deposit rates and reducing loan rates.

Pursuant to the accord, the Banking Association retained a renowned consulting firm to produce a study about the efficiency of the banking system. The study found that the high proportion of checks as a proportion of total transactions was affecting the efficiency of the system. It recommended that modernization of the payments system, including the more aggressive introduction of electronic transactions, be given priority.

This study served as a starting point for a series of initiatives both in the public sector and in the industry. For example, the Banking Association has established several working groups focused on implementing these initiatives and developing incentives to diminish the role of checks and enhance the use of electronic transactions.

Even before the study, the Banking Association and the Central Bank have been working together on a modernization plan for the payment system. The new system will be a real time one, and will allow truncation of checks and other instruments of both low and high value. It is anticipated that the system will be implemented sometime in 2001.

The Banking Association has proposed to the government a fiscal incentive plan to promote mergers and acquisitions in the banking sector. The plan is under current consideration by the Ministry of Finance.

Seven major institutions announced in January the introduction of the electronic money card MONDEX, which uses chip technology for low-value transactions.

The banking sector is actively collaborating with the Executive Branch in a series of programs aimed at reactivating several industries that have been seriously affected by recession. The industry has negotiated lending quotas for the agricultural, automotive and small industry sectors which contemplate the application of differential lending rates for these sectors.

Supervision of Non-Domestic Banking Organizations

The authority of a non-domestic banking organization to expand its nonbanking activities in Venezuela is not subject to an assessment of its capital and management as a global institution, although an assessment is made of the banking organization's operations in Venezuela and its compliance with the applicable requirements of Venezuelan law, which in general are the same as those applied to domestic banks (except with respect to representative offices, which are prohibited from taking deposits).