FSB FINANCIAL STABILITY BOARD

Peer Review of the Netherlands

Review Report

11 November 2014

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Foreword

Financial Stability Board (FSB) member jurisdictions have committed, under the FSB Charter and in the *FSB Framework for Strengthening Adherence to International Standards*[1], to undergo periodic peer reviews. To fulfil this responsibility, the FSB has established a regular programme of country and thematic peer reviews of its member jurisdictions.

Country reviews focus on the implementation and effectiveness of regulatory, supervisory or other financial sector standards and policies agreed within the FSB, as well as their effectiveness in achieving desired outcomes. They examine the steps taken or planned by national authorities to address International Monetary Fund (IMF)–World Bank Financial Sector Assessment Program (FSAP) and Report on the Observance of Standards and Codes (ROSC) recommendations on financial regulation and supervision as well as on institutional and market infrastructure that are deemed most important and relevant to the FSB's core mandate of promoting financial stability. Country reviews can also focus on regulatory, supervisory or other financial sector policy issues not covered in the FSAP that are timely and topical for the jurisdiction itself and for the broader FSB membership. Unlike the FSAP, a peer review does not comprehensively analyse a jurisdiction's financial system structure or policies, or its compliance with international financial standards.

FSB jurisdictions have committed to undergo an FSAP assessment every 5 years; peer reviews taking place 2-3 years following an FSAP will complement that cycle. As part of this commitment, the Netherlands volunteered to undergo a peer review in 2014.

This report describes the findings and conclusions of the Netherlands peer review, including the key elements of the discussion in the FSB's Standing Committee on Standards Implementation (SCSI) on 15 October 2014. It is the twelfth country peer review conducted by the FSB and the first using the revised objectives and guidelines for the conduct of peer reviews set forth in the January 2014 *Handbook for FSB Peer Reviews.*[2]

The analysis and conclusions of this peer review are based on the Dutch financial authorities' responses to a questionnaire and reflect information on the progress of relevant reforms as of September 2014. The review has also benefited from dialogue with the Dutch authorities and private sector participants as well as discussion in the FSB SCSI.

The draft report for discussion was prepared by a team chaired by Lawrence Schembri (Deputy Governor, Bank of Canada) and comprising Mario Delgado Alfaro (Spanish Fund for the Orderly Resolution of Banks, FROB), Simon Hall (Bank of England), Terhi Jokipii (Swiss National Bank) and Ryan Tetrick (US Federal Deposit Insurance Corporation). Greta Mitchell Casselle, Costas Stephanou and Ruth Walters (FSB Secretariat) provided support to the team and contributed to the preparation of the peer review report.

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[1] See http://www.financialstabilityboard.org/publications/r_100109a.pdf.

[2] See http://www.financialstabilityboard.org/wp-content/uploads/r_140106.pdf.

Abbreviations

AFM	Authority for the Financial Markets
BCBS	Basel Committee on Banking Supervision
BRRD	Bank Recovery and Resolution Directive (EU)
CEO	Chief Executive Officer
CMG	Crisis management group
CPB	Netherlands Bureau for Economic Planning
CRD	Capital Requirements Directive (EU)
CRE	Commercial Real Estate
CRR	Capital Requirements Regulation (EU)
DGS	Deposit Guarantee Scheme
DNB	De Nederlandsche Bank
DGSD	Deposit Guarantee Schemes Directive (EU)
EC	European Commission
ECB	European Central Bank
ELA	Emergency Liquidity Assistance
ESRB	European Systemic Risk Board
EU	European Union
FSAP	Financial Sector Assessment Program
FSB	Financial Stability Board
FSC	Financial Stability Committee
GDP	Gross Domestic Product
IAIS	International Association of Insurance Supervisors
IMF	International Monetary Fund
IOSCO	International Organization of Securities Commissions
LTI	Loan-to-Income
LTV	Loan-to-Value
MID	Mortgage Interest Deductibility
MPC	Macroprudential Policy Cycle
MoF	Ministry of Finance
MoU	Memorandum of Understanding
NHI	National Mortgage Institute
NHG	National Mortgage Guarantee
NIBUD	National institute for family finance information
NLFI	NL Financial Investments
OFS	Overview of Financial Stability (DNB report)
P&C	Property & casualty (insurance)
SIB	Systemically Important Bank
SIFI	Systemically Important Financial Institution
SME	Small and Medium-sized Enterprises
SRB	Single Resolution Board
SRF	Single Resolution Fund
SRM	Single Resolution Mechanism
SSM	Single Supervisory Mechanism

Executive summary

Background and objectives

The main purpose of this peer review is to examine two topics that are relevant for financial stability and important for the Netherlands: the macroprudential policy framework and tools, and crisis management and bank resolution. Both topics were included in the key FSAP recommendations and are topical for the broader FSB membership. The peer review focuses on the steps taken to date by the Dutch authorities to implement reforms in these areas, including by following up on relevant FSAP recommendations.

Main findings

Good progress has been made in addressing the FSAP recommendations; even though work is ongoing, much has been accomplished and the Netherlands remains at the forefront of international reforms in both areas. Going forward, the authorities need to clarify further the role of the Financial Stability Committee (FSC) within the macroprudential framework. The ongoing effort to analyse and address housing market vulnerabilities will be an instructive test of its effectiveness and level of ambition. The authorities also need to close remaining gaps in the legal framework for resolution and to realign the institutional framework to ensure resolution is feasible and credible. An important driver of developments in both of these areas has been, and will continue to be, European Union (EU) initiatives.

Macroprudential policy framework and tools

The legislative and organisational reforms implemented by the Dutch authorities have introduced a comprehensive macroprudential policy framework that broadly addresses the FSAP recommendations. Cooperation and information exchange between the institutions responsible for safeguarding financial system stability have been strengthened via the creation of the FSC. Under the amended Banking Act, the central bank (DNB) now has explicit responsibility for financial stability and has created a separate department to carry out this work. In addition, DNB has been assigned the responsibility for calibrating and applying the macroprudential tools in CRD IV/CRR. A formal risk assessment and decision making process for operationalising macroprudential policy has been formulated, and macroprudential risks are being integrated within the supervisory approach. The authorities have taken steps to address the risks stemming from the housing market, also in response to FSAP recommendations. The most important challenge now consists of deploying macroprudential tools effectively in specific contexts by embedding them in existing processes and developing the required analytical and operational capabilities.

The FSC is operational but, given its recent creation and the fact that it has not yet issued many warnings or formal recommendations, it is too early to evaluate its effectiveness in attaining its mandated objectives. The authorities emphasise that the FSC is still finding its way, but that it has played a useful role as a forum for discussing key risks to the financial system and harnessing the perspectives of different authorities with a role in macroprudential policy. The FSC has also enabled the discussion of cross-sectoral issues, and has given impetus to some joint project work (e.g. on bank funding structures and investor base). In that context, the main benefit of the FSC has been to act as an overlay to the existing institutional structure, without seeking to usurp or duplicate mandates and powers of existing authorities, by enhancing coordination and information exchange across those authorities.

To further enhance the effectiveness of the macroprudential policy framework, there are three main areas where the Dutch authorities may consider taking further steps:

- *Institutional arrangements:* Institutional arrangements could be further clarified around the role of the FSC within the macroprudential policy framework in order to realise fully the advantages of having such a body. This would involve defining more clearly the role and responsibilities of the FSC vis-à-vis its member institutions; fostering greater collaboration and engagement among its member institutions by levering their comparative expertise (e.g. in joint risk assessments or impact analysis of possible policy measures); determining the role of the FSC in the deployment of certain macroprudential tools; and enhancing the FSC's communication policy and public visibility in accordance with the identified ambition level. A number of these steps can be taken within the current legal and institutional setting. Moreover, to further improve its effectiveness and to enhance its credibility as a key part of the macroprudential framework, the authorities should consider embedding the FSC in primary legislation. Finally, there is a case for reconsidering the current powers of the FSC to issue recommendations so as to include a binding requirement on recipients to act or to explain why they are not responding. Similar to macroprudential bodies at the EU level and in other countries, there is a public accountability case for recipients to be formally required to explain their response to an FSC recommendation, even if they choose not to comply.
- *Macroprudential analysis and tools for the housing market:* Significant steps have been taken in developing macroprudential tools as a result of the implementation of CRD IV/CRR. In line with the FSAP recommendation, the authorities have announced a gradual reduction in loan-to-value (LTV) limits from 106% to 100% by 2018 for new mortgage lending (alongside existing affordability tests on borrowers), and have adopted plans to reduce mortgage interest deductibility over the medium term and to limit its eligibility to new mortgages that are fully amortising. These measures are a welcome step to mitigating risks to the financial system stemming from the housing market. However, LTV ratios remain high by international standards, which can be damaging to financial stability. To date there has not been a comprehensive public assessment of the case for and against taking more extensive action to reduce vulnerabilities in the housing market. As a result, neither a desired long-run LTV level nor its transition path (beyond 2018) is clear to market participants. Policy measures to reduce housing market vulnerabilities are not necessarily limited to the LTV limit and could include, for example, the use of other prudential instruments to target high risk lending, reforms to the structure of the rental market, and other public policies to mitigate the impact on vulnerable social groups. It would be important for the authorities to undertake a comprehensive assessment of the risks stemming from the housing market and publicly lay out the relevant considerations and trade-offs under alternative policy actions to mitigate them, including their wider economic implications. Given its membership and focus on structural types of risks, the FSC is well-positioned to coordinate such an exercise.

- *Responsibility for setting LTV and LTI limits:* The government currently is responsible for setting LTV and loan-to-income (LTI) limits. Developments in the housing market are clearly critical for government objectives, particularly where affordable housing and broader social equity considerations are concerned. However, prudential tools such as LTV and LTI limits that are based on contractual arrangements between borrowers and regulated lenders should be independent from the political cycle, and should be set with micro- and macroprudential objectives in mind while being aware of their potential social and economic consequences. In the international context, the design and application of such tools is typically the responsibility of a prudential authority operating in consultation with other relevant bodies (e.g. consumer protection agency). In that sense, keeping these tools under the control of the Dutch government, without formal input from prudential bodies, may be considered inconsistent with the spirit of the FSAP recommendation to "provide supervisors with powers to vary the designated macroprudential instrument in response to developments". In order to address this issue, the FSC should play a greater role in setting LTV and LTI limits in the Netherlands. In the short term, this would involve the FSC making a formal recommendation to the government on the use of these tools. Over the longer term, the authorities should consider reallocating the powers for setting LTV and LTI limits to the FSC and requiring it to demonstrate that broader economic consequences are accounted for in any decision taken.

Crisis management and bank resolution

Major steps have been undertaken to upgrade the framework for crisis management and bank resolution in the Netherlands, with several more reforms forthcoming in the near future. The Dutch authorities should be commended for their rapid adoption and implementation of the Intervention Act, which addressed some of the FSAP recommendations. These include the establishment of a single regime for resolving banks, a clearer specification of the roles of DNB and Ministry of Finance (MoF), and the ability for the deposit guarantee scheme (DGS) to fund resolution. Work on recovery and resolution planning is also well underway, while the coordination processes established between DNB and MoF have enhanced the authorities' ability to manage the nationalisation of SNS REAAL in early 2013. The Evaluation Commission's review of that nationalisation identified some lessons for the resolution regime, but it also concluded that the powers of the Intervention Act functioned effectively and were crucial in achieving the ultimate objective of safeguarding financial stability.

Further progress in addressing the FSAP recommendations on official financial support and deposit insurance will be realised when the Netherlands transposes the EU Directives on Deposit Guarantee Schemes (DGSD) and Bank Recovery and Resolution (BRRD), and when the Single Resolution Mechanism (SRM) becomes operational. Implementing these reforms will be a considerable undertaking, but should close the remaining gaps identified in the FSAP and enhance the alignment of the bank resolution framework with the FSB's *Key Attributes of Effective Resolution Regimes for Financial Institutions* (*Key Attributes*).

Nonetheless, there are some key actions that the Dutch authorities could take to further enhance the effectiveness of the resolution framework:

- *Adoption of pending legislative changes:* The transposition of the DGSD will introduce important new elements to the Dutch DGS (e.g. minimum required *ex ante* funding, risk-based bank contributions) and address the FSAP recommendations in this area. The Intervention Act did not introduce all of the powers and instruments specified in the *Key Attributes*, partly because it was intended to adopt them in coordination with other EU countries through the BRRD. The implementation of these two Directives and the establishment of the SRM provide an appropriate context to enhance the Dutch DGS and to align the resolution regime fully with the *Key Attributes*, taking into account the experience of SNS REAAL.

- *Realignment of the institutional framework for resolution*: The Minister of Finance announced that, through transposition of the BRRD, DNB will be established as the national resolution authority and provided with important additional powers specified in the *Key Attributes*. The Dutch authorities will maintain a division of resolution responsibilities and powers between DNB and the MoF, with the latter retaining the powers to intervene in the internal governance of an institution and to nationalise through expropriation of shares. However, since the MoF's powers only apply in cases where there is an immediate and serious threat to the stability of the financial system, there may be some overlap with firms for which the Single Resolution Board (SRB) under the SRM is primarily responsible. The division of resolution responsibilities and powers that will be adopted in the Netherlands as part of BRRD transposition will need to take these factors into account to ensure an effective institutional framework. Moreover, the SRB will assume responsibility for resolution planning and decision making for systemic and cross-border banks in the EU banking union, affecting several institutions in the Netherlands. As these changes are implemented, the crisis management protocols, inter-agency Memorandums of Understanding between DNB, the MoF and the conduct regulator (AFM), and the DNB's crisis management handbook, should be updated and revised to reflect the new roles, responsibilities and relationships between the relevant authorities.
- *Balancing supervisory and resolution concerns:* The authorities have presented proposals to ensure the operational independence of the resolution function, as required by the BRRD, within the broad range of responsibilities of DNB. A recalibration of the organisational structure will be implemented within DNB that aims to balance the advantages of cooperation between the supervisory and resolution functions against the risks that the lack of full institutional independence (i.e. the resolution authority as a separate organisation) will result in resolution priorities being subordinated to other interests. The objective is that DNB's resolution directorate will be independent from, and have no role in, supervision, financial stability or monetary functions. The resolution directorate will also have sole decision-making responsibility for the implementation of resolution measures. Given the potential trade-offs between going-concern and gone-concern interests, decision making on *ex ante* measures to enhance the resolvability of institutions will be made by the DNB Board, taking into account both resolution and supervision considerations. The SNS REAAL case highlighted the importance of the supervisory or resolution authorities having the ability to require financial institutions to adopt changes to their structure, organisation or business practices to improve their resolvability. Such changes to address obstacles to resolution identified at other Dutch systemically important banks (SIBs) have not been required to date. Analysis conducted prior to the establishment

of an independent resolution directorate within DNB indicates that these changes might significantly impair firms' competitiveness. As the DNB's resolution function is established with appropriate safeguards for operational independence in place, it should continue to examine as part of resolution planning work and in collaboration with the SRB the options for, and potential costs and benefits of, requiring changes to Dutch SIBs' structures or operations in order to enhance their resolvability.

Recommendations

In response to the aforementioned findings and issues, the peer review has identified the following recommendations for consideration by the Dutch authorities:

Macroprudential policy framework and tools

- The authorities should further clarify the role of the FSC within the macroprudential framework. Under the existing legal and institutional setting, they should specify and publicly set out the nature of the FSC's involvement in systemic risk assessment and macroprudential policy. In addition, the authorities should consider: (a) embedding the FSC's role and institutional standing in primary legislation to improve further its effectiveness and enhance its credibility; and (b) strengthening accountability for FSC recommendations via the establishment of a formal 'comply or explain' mechanism.
- The authorities, working through the FSC, should undertake a comprehensive assessment of the impact of taking further steps to address housing market risks to the financial system and the economy. The assessment should analyse any identified risks, consider alternative macroprudential and other policy measures, and set out publicly the case for and against taking further actions in this area.
- The FSC should play a more prominent role in setting LTV and LTI limits to ensure that decisions on the use of these tools are made on the basis of both prudential considerations and their potential impact on consumers and the broader economy. In the short term, this could include the FSC making a formal recommendation to the government on the use of these tools. In the longer term, the authorities should consider reallocating the powers for setting these limits to the FSC.

Crisis management and bank resolution

- The authorities should continue work to transpose BRRD and DGSD promptly into national legislation in order to address the remaining FSAP recommendations on deposit insurance and resolution and to further align the Dutch resolution regime with the FSB's *Key Attributes*.
- In transposing the BRRD, the authorities clarify the roles and powers of the relevant authorities in the resolution framework and update crisis management protocols for inter-agency coordination.
- As DNB takes on the role of the designated resolution authority in the Netherlands, it should exercise the resolution function with sufficient operational independence to effectively carry out its mandate, including the ability to appropriately examine and address identified obstacles to the resolvability of SIBs.

1. Introduction

The Netherlands underwent an FSAP update in 2010 that included assessments of the Basel Committee on Banking Supervision's (BCBS) *Core Principles for Effective Banking Supervision,* the International Association of Insurance Supervisors (IAIS) *Insurance Core Principles*, and the International Organisation of Securities Commissions (IOSCO) *Principles and Objectives of Securities Regulation*.[3]

The FSAP concluded that the Netherlands had been seriously impacted by the global financial crisis, which had required substantial public support for banks and insurers. The "twin-peaks" model for supervision – with the central bank (De Nederlandsche Bank, DNB) as the prudential supervisor and the Authority for the Financial Markets (AFM) as the conduct-of-business supervisor – had been effective with a high degree of compliance with international regulatory standards. Financial institutions had improved their soundness, but high indebtedness of home buyers and the sizeable cross-border activities of Dutch financial institutions presented near-term challenges to financial stability. The FSAP recommended that macroprudential instruments be developed to lower the system's vulnerability to mortgage market shocks; that the sizeable cross-border activities of Dutch financial institutions required closer scrutiny (including data to enhance monitoring) and supervisory engagement; and that legislative reforms were necessary to strengthen crisis management and bank resolution capacity, including changes to the deposit guarantee scheme.

The main purpose of the peer review is to examine two topics that are relevant for financial stability and important for the Netherlands: its macroprudential policy framework and tools, and crisis management and bank resolution. Both topics were included in the key FSAP recommendations and are topical for the broader FSB membership. The review focuses on the steps taken to date by the Dutch authorities in these areas, including by following up on relevant FSAP recommendations. In particular, the review evaluates progress with the reforms in order to draw conclusions and policy implications as well as identify remaining impediments and lessons that could be of benefit to the Netherlands and its FSB peers.

The report has two main sections, corresponding to the two topics being reviewed. Section 2 focuses on the macroprudential policy framework and tools, including the application of that framework to address the systemic risks emanating from the domestic real estate sector. Section 3 (and Annex 2) analyses the steps taken by the authorities to strengthen crisis management and bank resolution, including in the case of the nationalisation of a Dutch bank (SNS REAAL) in 2013. In addition, Annex 1 provides background information on the structure of the Dutch financial system and on recent regulatory developments, while Annex 3 presents the follow-up actions reported by the Dutch authorities to other key FSAP recommendations; these actions have not been analysed as part of the FSB peer review and are presented solely for purposes of transparency and completeness.

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[3] See "Kingdom of the Netherlands—Netherlands: Financial Sector Stability Assessment" (IMF Country Report No. 11/144, June 2011, http://www.imf.org/external/pubs/ft/scr/2011/cr11144.pdf. All ROSC assessments and technical notes have been published (http://www.imf.org/external/np/fsap/fsap.aspx).

2. Macroprudential policy framework and tools

Background

The FSAP noted that the financial sector was dominated by systemically important financial institutions (SIFIs) that operated in diverse domestic and international markets. The financial crisis had heavily impacted those firms, with four out of the five largest financial groups subject to restructuring programs at the behest of the authorities and the European Commission (EC). While financial soundness had improved, household balance sheets were increasingly stretched and posed a risk to the banking system via the mortgage market. In response, the FSAP recommended that the authorities assign priority to developing macroprudential instruments; that they set maximum loan-to-value (LTV) ratios for new lending, and consider linking higher LTVs to higher capital ratios; that they provide supervisors with powers to vary the level of designated macroprudential instruments in response to developments; and that they announce plans to reduce mortgage interest deductibility (MID) over the medium term.

At around the same time as the FSAP, the institutional framework for macroprudential policy began to take shape in the European Union (EU), with the establishment of the European Systemic Risk Board (ESRB) in 2010. Since its establishment, the ESRB has issued recommendations[4] calling on EU member states to: designate a macroprudential authority and to establish the necessary institutional arrangements to support its functioning; assign macroprudential instruments to relevant national authorities; and articulate a clear policy strategy (see Box 1). In 2014 a set of macroprudential instruments became available to macroprudential authorities across the EU through the implementation of the fourth Capital Requirements Directive (CRD IV) and accompanying Regulation (CRR).

In the 2013 Article IV report, the IMF noted that ensuring the resilience of the banking system remained a top priority. Notwithstanding steps taken in recent years by the authorities to strengthen resilience and regulatory oversight, the Dutch financial system remains very large relative to the economy (as set out in more detail in Annex 1). The economic backdrop remains challenging since, despite signs of recovery, nominal growth is relatively weak and very low interest rates present particular challenges to non-bank financial institutions. The banking system is also highly concentrated. On the liability side, there is continued substantial dependence on international wholesale markets as a source of funding. On the asset side, domestic real estate exposures remain considerable, partly reflecting the legacy of ongoing government promotion of home ownership. The IMF has called for policies to address these risks, including via the gradual removal of distortions in the housing market.[5]

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[4] See http://www.esrb.europa.eu/pub/recommendations/html/index.en.html.

[5] See the April 2013 Article IV report for the Netherlands (IMF Country Report No. 13/115, http://www.imf.org/external/pubs/ft/scr/2013/cr13115.pdf).

Box 1: Macroprudential policy framework in the EU

Within the EU, several important steps have been taken in recent years to strengthen the overall policy framework for dealing with system-wide financial distress. One such step was the establishment of the ESRB in 2010, with legal responsibility for macroprudential oversight of the EU financial system. The ESRB has the power to issue warnings and recommendations, which are subject to a "comply or explain" mechanism. It also has consultative powers in a broad set of areas. However, the ESRB does not have the power to use instruments directly; that responsibility lies at the national level, but is subject to EU constraints.

ESRB recommendations

In a recommendation in 2011, the ESRB set out guiding principles for core elements of national macroprudential mandates, which sought to balance the need for consistency in national approaches across the EU with the flexibility to accommodate national specificities. The recommendation stated that member states should set out clearly that the objective of macroprudential policy was to safeguard systemic stability and to ensure a sustainable contribution of the financial sector to economic growth. Member states were asked to designate in national legislation an authority (or a board of authorities) with responsibility for the conduct of macroprudential policy, with the central bank playing a leading role. The authority should be entrusted with the job of identifying and monitoring risks, and be given powers to gather information (including from microprudential and securities market supervisors, and on developments from outside the regulatory perimeter). It should be tasked with acting to mitigate risks and should explain publicly its decision making, including its broader macroprudential strategies. While the authority should be accountable to national parliament, it should be operationally independent from political bodies.

The ESRB issued a follow-up recommendation to national macroprudential authorities in April 2013, requiring them by the end of 2014 to define their intermediate objectives and to assess the macroprudential instruments available to them, and by the end of 2015 to develop a policy strategy.

Macroprudential instruments

In January 2014, CRD IV/CRR came into force. The new rules provide EU Member States with a common legal framework and a set of macroprudential instruments (most of which were set out in Basel III) to mitigate systemic risk in the banking sector. The measures aim to improve resilience by requiring more and higher quality bank capital. The key elements of CRD IV/CRR are: (i) a higher quality capital base; (ii) higher minimum capital requirements; (iii) additional buffers, including a systemic risk buffer and a countercyclical buffer that can be varied through the financial cycle. The aim is to provide a single set of prudential rules for institutions throughout the EU instead of a patchwork of national rules. While a single rulebook is important for the single market, a certain degree of national flexibility in the use of macroprudential measures is still needed, as credit and economic cycles are not synchronised across the EU. This concern is even more relevant for Member States in the euro area that no longer have national monetary policy tools at their disposal. The new capital rules have procedures in place to check that the negative impact of certain national measures, if any, does not outweigh the financial stability benefits. These include legal requirements for assessment of cross border effects and notification to the ESRB and EC, which in turn may issue opinions or recommendations depending on the case at hand (see Table 1).

Single Supervisory Mechanism (SSM)

In November 2013, the SSM entered into force and will become fully operational by the end of 2014. Under the SSM, the ECB will directly supervise significant credit institutions and it will work closely with national competent authorities in their supervision of all other credit institutions. The SSM regulation foresees a shared responsibility for macroprudential policy. National authorities will retain the power to apply macroprudential measures via CRD IV/CRR instruments, as well as instruments not included in the EU legal texts, but the ECB can act to impose more restrictive requirements than those applied nationally. Good cooperation between national and European authorities is therefore crucial for the effectiveness of macroprudential policy in Europe, including in order to ensure that cross-border considerations are properly taken into account.

Table 1: Instruments under the CRD IV/CRR for macroprudential use

Instruments under the CRD					Instruments under the CRR			Other
Countercyclical capital buffer (CCB)	**Systemically important institution (SII) buffer**	**Systemic risk buffer (SRB)**	**Liquidity requirements under Pillar 2**	**Other macro-prudential use of Pillar 2**	**Higher requirements on capital / liquidity / large exposures / risk weights**	**Higher real estate risk weights and stricter lending criteria**	**Higher minimum exposure-weighted average LGDs**	**Including LTV/LTI/DSTI and LTD limits and a leverage ratio**
CRD 130, 135-140	CRD 131	CRD 133 and 134	CRD 105	CRD 103	CRR 458	CRR 124	CRR 164	National legal framework
Mandatory buffer: Member States have to decide on a buffer rate informed by a buffer guide based on the credit-to-GDP gap. Other relevant variables also have to be considered. Member States can decide to apply the CCB from 2014 and must apply it from 2016. Mandatory reciprocity up to a buffer rate of 2.5% applies from 2019.	1) Mandatory surcharge for global systemically important banks (G-SII) applicable from 2016. A surcharge between 1% and 3.5% of RWAs, depending on the degree of systemic importance of an institution. 2) Optional surcharge for other SIFIs (O-SII) applicable from 2016. A surcharge up to 2% of RWAs. 3) Combination rules between G-SII and O-SII buffers and the SRB ensure a floor/cap on all three buffers at the consolidated and subsidiary level.	Optional buffer on all or a subset of institutions. Until 2015 the competent or designated authority can set a buffer between 1% and 3% subject to notification to the European Commission, EBA and ESRB. An SRB above 3% requires authorisation by the European Commission after the EBA and ESRB have provided opinions. From 2015, the same authorisation is required for an SRB of above 3% on exposures in other Member States and of above 5% on local and third country exposures.	Optional: Competent authorities may impose specific requirements to address systemic liquidity risks. These include administrative penalties, including prudential charges that relate to the disparity between the actual liquidity position and any liquidity and stable funding requirements.	Optional: Competent authorities have the power to impose additional requirements on institutions with similar risk profiles in a similar manner if – inter alia – they pose similar risks to the financial system. These requirements include own funds and additional disclosures.	Optional: National authorities may apply stricter rules for a number of selected measures subject to an EU procedure. It has to be established that the measure is necessary, effective and proportionate, and that other specified measures cannot adequately address the systemic risk. These measures are subject to a notification and non-objection process, with the Council having the final decision on whether to block a measure if objections are raised.	Optional: Competent authorities can set higher risk weights up to 150% based on financial stability considerations, taking into account loss experience and forward-looking market developments.	Optional: Competent authorities can set higher minimum exposure-weighted average LGDs (no upper limit) based on financial stability considerations, taking into account loss experience and forward-looking market developments. Applies only to retail exposures.	Optional: Member States can assign macro-prudential instruments that are not covered by the scope of EU legislation. This includes instruments, such as LTV/LTI/DSTI limits (e.g. to dampen a boom in real estate mortgage lending or to curb excessive consumption lending), liquidity instruments, such as LTD limits, and a leverage ratio. These instruments are based on national law.

Source: ESRB.

Steps taken and actions planned

Institutional arrangements: DNB, Ministry of Finance (MoF), and the AFM work together to safeguard the stability of the Dutch financial system. Under the amended Banking Act that became effective on 1 January 2014, DNB has explicit responsibility for financial stability in addition to its responsibility for prudential supervision. The AFM contributes to the stability of the financial system through its work to ensure the proper functioning of financial markets. Since January 2014, the role of the AFM in macroprudential policy is reflected in its mandate that AFM activities are conducted '*also in the interest of financial stability*'. The MoF is politically responsible for the overall functioning of the financial system and for financial market regulation. It is also the authority that, in case of an immediate and serious threat to financial stability, has the power to nationalise a financial institution (see section 3).

In response to the recommendations of a Parliamentary Commission of Inquiry on the Financial System,[6] the MoF announced in November 2012 the creation of a new macroprudential body – the Financial Stability Committee (FSC). In order to establish this new body expeditiously, its role was set out by means of a Ministerial Decree rather than in primary legislation. The main reason for establishing the FSC was to create a forum in which the authorities with a responsibility for financial stability could meet to identify and discuss potential risks and ways to mitigate them, including by making recommendations with respect to those risks.[7] Importantly, the FSC does not take policy decisions: the decision-making powers remain with the relevant authority, which in the case of instruments detailed in the CRD IV/CRR is DNB. Rather, the FSC provides an opportunity for integrating views and setting joint priorities on issues affecting the stability of the Dutch financial system. While it is not a crisis management body, the FSC also considers how crises may affect the stability of the financial system. In addition, the FSC serves to align and coordinate the response by the Dutch authorities to warnings and recommendations made by the ESRB.

The FSC is made up of seven representatives from the authorities: three from DNB (including the President as FSC chair) and two each from the MoF and the AFM.[8] Each representative attends in a personal capacity. There are no formal independent external members, though there is scope to invite external experts as required. For example, since November 2013, the director of the Netherlands Bureau for Economic Policy Analysis (CPB), which is the government's economic research institute, has attended the meetings as an external expert. A representative of the Ministry of the Interior has also attended recent FSC meetings to discuss housing market developments. To include different points of view and to promote effective coordination, a secretariat at DNB works with staff from DNB, AFM and the MoF to prepare

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6 The de Wit Commission, a Dutch parliamentary group was set up in 2009 to examine developments and problems in the global financial system in general and in the Dutch financial system in particular. The Commission published its findings on 10 May 2010.

7 The FSC's establishment also addressed the ESRB recommendation on national macroprudential mandates.

8 The FSC members are: the DNB President, Executive Director for Supervision, and Executive Director for Monetary Affairs and Financial Stability; the AFM Chairman of the Executive Board and the Head of Strategy, Policy and International Affairs; and the MoF Treasurer General and the Director of Financial Markets. Each member may be deputised by a designated individual within the respective organisation.

the meetings. Where necessary, other relevant experts may also be invited to share their knowledge and points of view. Topics for discussion can be raised by participating institutions for inclusion in the agenda of the next FSC meeting. Meetings are held at least twice a year (and more frequently when necessary) and a work plan for the coming meeting is generally announced.[9] The first meeting of the FSC was held in December 2012 and three subsequent meetings have taken place.

The FSC can issue warnings to whoever it deems necessary, and may also issue alerts or recommendations to authorities or market participants in cases where they have a major influence on financial stability. Warnings or recommendations issued by the FSC are of a cautionary and advisory nature and are hence non-binding, with no requirement to 'act or explain', but FSC can monitor how addressees react to its warnings and recommendations. To date the FSC has not issued any formal warnings or recommendations.[10]

The FSC does not have the power to direct that certain measures be adopted nor does it decide on the application of macroprudential tools. In reaching decisions, the FSC cannot interfere with the legal tasks and responsibilities of its member institutions, and it will in general strive for consensus. Where that is not possible, a vote can be held on specific matters, though that has not happened to date. In such a case, decisions are made based on a two-thirds majority of the votes cast. To ensure a degree of independence as regards the financial stability mandate, representatives from the MoF have no voting rights with regard to FSC decisions on warnings and recommendations.

With regard to public transparency, a summary of each meeting is published on the FSC website.[11] The intention is to make all warnings and recommendations public; however, the FSC may decide not to disclose a warning or recommendation if this would be unwarranted due to possible risks to financial stability. An annual report, outlining activities undertaken and any recommendations made during the year under review, is produced for the Minister of Finance and sent to Parliament.

DNB also communicates about macroprudential developments and instruments via the semi-annual Overview of Financial Stability (OFS) report published on its website, the annual presentation and discussion on financial stability concerns of DNB President with members of Parliament, and other ad hoc publications (occasional papers etc.). Topics highlighted as risks in the OFS (reflecting the views of DNB) are subsequently discussed at FSC meetings, and this often contributes to the development of the FSC's own work program. Members decide which risks warrant further analysis and discussion. The work is then conducted by common working groups set up by the FSC, comprising member institutions. Examples of issues discussed in the FSC are developments in the housing and mortgage markets, the

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[9] The topics selected for discussion in the forthcoming (November 2014) FSC meeting are: mortgage financing (mainly LTV limits); macroprudential policy framework and the role of the FSC; implications of tax policy for financial stability; over-the-counter derivatives market reforms; and cyber threats.

[10] In its meeting in November 2013, the FSC called on Dutch banks to implement the recommendations of the Enhanced Disclosure Task Force in their annual reports for 2013, noting that if a bank was unable to comply with the recommendations it should provide information detailing the reasons. In its subsequent meeting in June 2014, the FSC found that most major banks had implemented a large part of these recommendations.

[11] See http://www.financieelstabiliteitscomite.nl/en.

establishment of the European banking union, the prospects for bank lending to the real economy, bank funding and the transparency of banks.[12]

As in other EU member states, initiatives at the EU level have been and will continue to be an important driver of the macroprudential policy framework in the Netherlands. As discussed in Box 1, CRD IV/CRR came into force in January 2014 providing the Dutch authorities with a common set of macroprudential instruments to mitigate systemic risk in the banking sector. The legislation also included mechanisms for notification and (in some cases) authorisation across a range of instruments as summarised in Table 1. In addition, the commencement of the SSM at the end of 2014 will both establish a new system of microprudential supervision and foresee a shared responsibility for macroprudential policy. In particular, under the SSM national authorities retain the power to apply macroprudential measures via CRD IV/CRR instruments, as well as instruments not included in the EU legal texts, but the ECB can act to impose more restrictive requirements than those applied nationally.

Risk assessments: Given its explicit financial stability mandate and analytical capacity, DNB carries out most of the risk assessment work discussed by the FSC. In doing so, DNB uses the FSC meetings as a means to inform and consult the other members, and to enhance its own risk assessments by identifying any gaps in its analysis and data. Within DNB, macroprudential policy decisions are taken at the Board level, with support and coordination provided by the Financial Stability Division.[13] One of the main responsibilities of that Division is to prepare an analysis of the most important financial stability risks as well as a translation of these risks into mitigating actions, as communicated via the OFS report. The financial stability function is also represented in DNB's Supervisory Council, which is directly responsible for most microprudential issues.

Risk assessments conducted by DNB are extensive and ongoing. They include bottom-up and top-down stress tests performed at the individual bank level, coupled with systemic risk assessments for banks and insurers to help determine whether institutions that are deemed systemically important require additional prudential measures.[14] In addition to the institution-specific assessments, ad hoc analyses of particular systemic risks (e.g. mortgage market, interest rate risk) are made. The risks are prioritised internally by DNB's Board and the most significant ones are included in the OFS report. While the risk assessment is led by DNB, AFM staff is included in the initial discussions and is involved in the drafting of the OFS report. This provides scope for identification and assessment of a broad range of risks, including those arising from pensions and insurance as well as shadow banking activity.

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[12] See the January 2013, June 2013, and November 2013, and June 2014 FSC announcements for more details.

[13] The Financial Stability Coordination Group plays a key role in that respect. It is chaired by the director of the Financial Stability Division and includes directors of most of the other divisions (all supervisory divisions as well as Financial Markets, Economics and Research, Payment systems and Legal affairs).

[14] The framework for systemic importance includes several criteria, including size, interconnectedness, substitutability, resolvability and behavioural reactions. Each criterion contains a range of (qualitative and/or quantitative) indicators. Prudential measures for firms deemed systemically important include higher capital requirements for banks, formulation of recovery and resolution plans, and higher intensity of supervision.

An organisational restructuring within DNB has facilitated the development of a formal risk assessment and decision making approach for operationalising macroprudential policy.[15] Within the Financial Stability Division, a separate department for the surveillance and analysis of macroprudential risks has been created. An important innovation adopted by DNB has been to establish an integrated semi-annual Macroprudential Policy Cycle (MPC) to link risk assessment to policy responses. The first cycle will take place during the second half of 2014. The MPC comprises the following steps:

- Initial analysis based on indicators (linked to ESRB intermediate objectives) and additional information, including by surveying DNB staff and other bodies such as the AMF, to get a first impression of the main risks;
- A Financial Stability Coordination Group discusses risks and possible implications for macroprudential instruments;
- DNB Board discusses risks and possible implications for instruments, and takes a decision on (usually three) topics that will be highlighted in the next OFS report;
- DNB staff further elaborate on the risk analysis and formulate proposals for the implementation of macroprudential instruments;
- DNB Supervisory Council is consulted on possible microprudential implications of the proposed implementation of macroprudential tools;
- DNB Board takes a decision on macroprudential instruments and on publication of draft OFS; and
- Measures are implemented, with notification/coordination procedures to relevant EU bodies and communication on DNB website and in the OFS report.

By taking decisions on a regular basis based on this framework, the MPC is expected to help to remove inaction bias and to implement instruments in a consistent way, including by identifying trade-offs between micro and macro measures.[16] In that regard, the authorities plan to publish a set of indicators that are identified as important for policy assessments and analyses. In addition to a formal and broad risk assessment on a semi-annual basis, DNB will continue to monitor risks to the system on an on-going basis. This is essential for policy decisions that might need to be taken at a higher frequency than semi-annually (e.g. quarterly obligations to set the countercyclical capital buffer rate).

Within DNB a structural separation between banking supervision and macroprudential policy exists. To ensure that the macro-micro connection is adequately preserved and that macro risks are adequately incorporated into the supervisory process, DNB launched a so-called ‘Macro register’ in October 2013. Under this approach, once certain macroprudential risks are identified (based on the MPC) and communicated (via the OFS), they are translated into supervisory actions. When assessing institution-specific risks, microprudential supervisors are expected to identify which of the macro risks on the ‘Macro register’ are relevant for the institution in question. For example, in 2013 interest rate risk was identified as having the potential to affect groups of institutions with the potential to disrupt the Dutch financial

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[15] DNB intends to publish a report in 2014 explaining its approach to macroprudential policy.

[16] Financial stability concerns are also addressed via measures to strengthen the crisis management and resolution framework, such as recovery and resolution planning etc. (see section 3).

system and ultimately the economy. Banks were therefore asked to calculate the impact they would sustain from interest rate movements.

Data: As the central bank and the microprudential supervisor, DNB has direct access to nearly all financial information reported by Dutch financial firms, and this information is available for macroprudential purposes. However, DNB currently lacks legal powers to collect information directly from institutions that are not supervised by DNB. To further enhance available information, the Dutch government has submitted to Parliament an extension of the Bank Act giving DNB powers to collect data specifically for macroprudential purposes; the legislative amendment is expected to enter into force in 2015. This includes information from institutions that are currently supervised by DNB as well as from other institutions and organisations (e.g. the land registry), and it also covers information needed to meet international obligations (BIS, IMF and FSB) that now can only be collected on a voluntary basis. This will be an important step in ensuring comprehensive and rigorous risk assessments based on data covering the entire financial system, particularly in the case of the Netherlands given the size of its shadow banking sector.[17]

In general, data covering sector-wide macroprudential developments can be shared between DNB and other authorities. The sharing of institution-specific information is facilitated by a Memorandum of Understanding (MoU) that has been signed by DNB and the AFM. While there is no FSC-specific information gateway and the MoF does not have access to institution-specific supervisory data, aggregated data suffices for most of the issues discussed in the FSC; there is also scope for information sharing with the MoF on issues pertaining to individual institutions where that is required for the purpose of the risk discussions.

Risks from the housing market and macroprudential tools: Historically, the Dutch government has pursued a policy of promoting home ownership through housing market policies, including a favourable tax treatment of main residences (see Box 2).[18] In addition, the rental sector is strictly regulated, with a relatively large social housing segment subject to rent controls that limit the incentives for growth of the private rental market.

Dutch house prices experienced a boom in the decades preceding the global financial crisis, reaching an all-time high in 2007.[19] The crisis sparked a sharp correction: real house prices have declined by around 20% since 2008 and the number of transactions has fallen considerably. The boom and subsequent bust in house prices, combined with a legacy of non-amortising mortgages, has left households with very high levels of indebtedness – in 2012

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[17] According to the FSB's October 2014 Global Shadow Banking Monitoring Report (http://www.financialstabilityboard.org/wp-content/uploads/r_141030.pdf), the assets of other (non-bank) financial intermediaries in the Netherlands at end-2013 had reached almost 8 times GDP, which is the highest ratio of all FSB jurisdictions. Special Financial Institutions based in the Netherlands comprised about two-thirds of these assets, and these are typically owned by foreign multinationals that use these entities to attract external funding and facilitate intra-group transactions.

[18] For more details, see "Investing in the Dutch housing market" by the Dutch Ministry of the Interior and Kingdom Relations, (June 2014, available at http://www.government.nl/issues/housing/documents-and-publications/leaflets/2014/05/26/investing-in-the-dutch-housing-market.html).

[19] According to the OECD, house prices rose by 228% in cumulative terms over the period 1985-2007, while consumer prices increased by only 56%.

household debt was around 310% of Gross Domestic Product (GDP), which is among the highest in the OECD.[20]

Mortgages account for about 25% of Dutch bank assets. Household lending has been one of the main drivers of banks' high loan-to-deposit ratio, which has contributed to their dependence on wholesale funding typically sourced from abroad. The structure of mortgage finance has added to vulnerabilities. A sustained period of rising prices and the emergence of specialized mortgage products to maximize tax subsidies have resulted in a large share of mortgage lending at elevated LTV ratios and limited amortization of mortgages.[21] The IMF has noted that LTV ratios on new mortgages, at an average of around 90%, are high relative to other economies (Figure 1). While recent rules have introduced a ceiling on maximum LTV ratios (see Box 2), DNB data indicates that a substantial proportion of borrowers continue to obtain mortgages with an LTV above 100% (see Figure 2).

High LTV ratios can be damaging to financial stability for several reasons. First, they are likely to reinforce the procyclicality of the housing market since, the higher the LTV ratio, the more borrowing can be increased for a given rise in property prices. Second, high LTV ratios increase the risk of losses for banks since collateral values may not be adequate to cover mortgages in the event of a downturn in the housing market. Third, highly indebted homeowners tend to be more vulnerable to economic shocks, such as loss of income or increases in interest rates, resulting in more severe economic downturns and slower economic recoveries than would otherwise be the case – indeed, IMF work suggests that recessions that followed property booms have, on average, been two to three times deeper.[22] Reducing maximum LTV ratios can therefore help to reduce the frequency and severity of losses from housing market cycles on the balance sheets of both households and financial institutions.

Box 2: Selected housing market policies in the Netherlands

The Dutch government's involvement in the housing market dates back to the late 19th century and the introduction of MID. At present, home owners are estimated to benefit each year by around €12 billion (about 2% of GDP) from the deductibility of mortgage interest from taxable income. Recently, the government announced the following measures to make the tax treatment of mortgage interest payments less generous:[23]

- Gradually reducing the marginal effective tax rate for MID on both existing and new mortgages

[20] Recent developments in, and prospects for, the Dutch housing market are set out in "Roads to recovery" by the CPB (June 2014, available at http://www.cpb.nl/en/publication/roads-to-recovery).

[21] As noted in Box 2, new mortgages at present are only eligible for mortgage interest relief if they are (at least) fully amortising on an annuity basis.

[22] See chapter 3 of the IMF's Global Financial Stability Report (April 2011, available at http://www.imf.org/external/pubs/ft/gfsr/2011/01/pdf/chap3.pdf) for details.

[23] In 2004, the government further strengthened the tax regime by taking into account realised asset gains when the previous house is sold.

from 52% in 2014 to 38% in 2042.

- Making new mortgages only eligible for MID when they fully amortise within 30 years on an annuity basis. As a result, new interest-only mortgages are no longer eligible for MID; however, old mortgages are excluded from this requirement.[24]

The government also announced in 2012 that it will permanently reduce stamp duty on houses from 6% to 2%, following a temporary reduction from June 2011.

The government provides support to the housing market via the National Mortgage Guarantee (NHG), which was first introduced in 1993. The NHG provides homeowners with a guarantee on mortgages below a certain size threshold; having such a guarantee can incentivise the lender in some cases to provide a rebate on the interest rate. If a homeowner cannot repay an eligible mortgage, the NHG will repay the bank under certain conditions (e.g. in case of unemployment or divorce). The NHG has a limited amount of own funds (less than €1 billion) out of which to pay if the guarantee is called upon but, when these funds are depleted, the government would have to step in. As a result of this implicit guarantee via the NHG, some housing market risks are shifted from the banking to the public sector.

In 2013, the outstanding stock of NHG-guaranteed mortgages was €164 billion (about 25% of GDP) while, according to the DNB, more than 75% of new mortgages were financed via the NHG. NHG mortgages have on average a higher risk profile than other mortgages – in particular, more than 50% of the NHG mortgages are in negative equity compared to around 30% for mortgages overall.

As in the case of MID, the government has decided to scale down its obligations via the NHG by:

- Reducing the eligibility threshold from €360,000 in 2009 (which was the result of a temporary increase in response to the global financial crisis) back to €265,000 as of July 2014. After 2016, the threshold will be based on the average house price, which currently stands at €211.000.
- Increasing gradually the one-off premium that homeowners need to pay (not based on actuarial estimates) from 0.55% of the value of the mortgage in 2011 to 1.0% from 1 January 2014.
- Introducing a requirement that banks bear 10% of the losses on NHG mortgages that are issued after 1 January 2014.

The government is also currently setting up a national mortgage institute (NHI) that is expected to fund NHG mortgages by issuing state-guaranteed bonds collateralized by pools of mortgages. In contrast to the other measures, the NHI will not lead to a scaling down of the NHG, but the intention is that this institute will make it more attractive for new investors, such as pension funds and foreign banks, to invest in the Dutch housing market by purchasing state-guaranteed bonds. This would help to diversify sources of funding for the Dutch mortgage market which is highly concentrated: at present, the three largest banks are estimated to have a combined market share of around 70%.

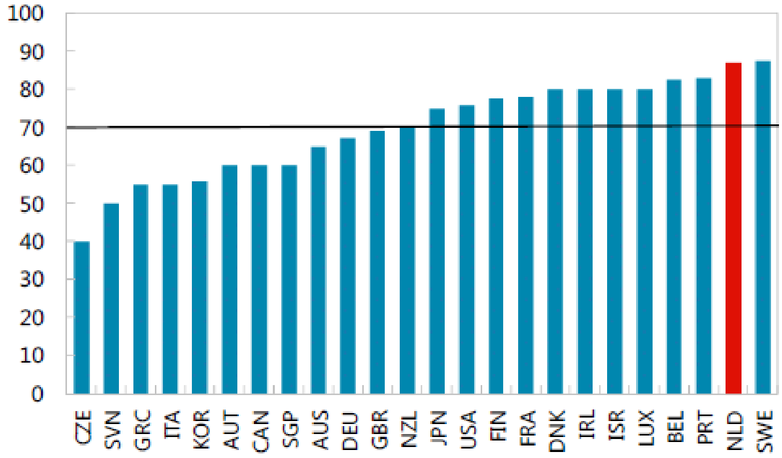
Loan-to-value (LTV) and loan-to-income (LTI) regulation

The government is also responsible for setting maximum LTV and LTI limits. In line with the FSAP recommendations, in August 2011 the government imposed an LTV cap for new lending of 106% effective from 2012; the cap will be reduced by 1% each year until it reaches 100% by 2018.

In addition, banks are obliged by law to check the affordability of every new mortgage loan. In 2013, a maximum LTI at origination, as defined in the Lenders' Code of Conduct, was incorporated into law. New borrowers must meet strict requirements governing their current and projected income. Affordability tests are based on gross household income, borrowing costs and debt service limits set by the Nationaal Instituut voor Budgetvoorlichting (NIBUD), a national institute for family finance information. The annual update of these limits is based on advice from NIBUD to the MoF, on which DNB and the AFM are consulted. In recent years, average LTIs for new mortgages have decreased from 4.5 in 2010 to 4.25 in 2013; up to the year 2000, LTI values of up to six were not uncommon.

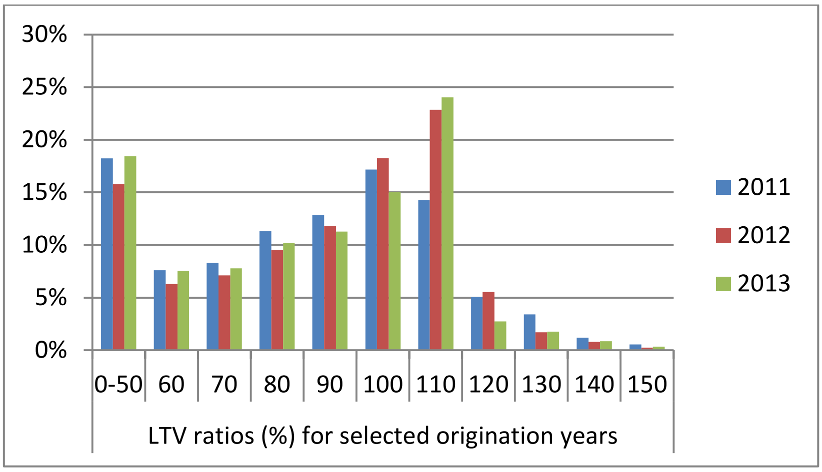
[24] Currently 35% of homeowners have an interest-only mortgage with no repayment vehicle. For more details, see the spring 2014 OFS report (http://www.dnb.nl/en/binaries/OFSuk_tcm47-306230.pdf).

Figure 1: Cross-country LTV Ratios for New Loan Mortgage Originations



Source: IMF 2013 Article IV report for the Netherlands. NLD = Netherlands.

Figure 2: LTV Ratios in the Netherlands on Recent Vintages of Mortgages



Source: DNB.

In the wake of the correction in house prices, the authorities estimate that around 30% of Dutch mortgages are ‘underwater’ (i.e. the remaining balance of the loan exceeds the current market value of the property). This can be attributed both to the recent price decline and to relatively high LTV ratios for new lending in the Netherlands. Younger households, which generally have lower savings than elderly households, are more likely to hold underwater mortgages since more of them have purchased their properties near the house price peak.

Despite the observed decline in house prices in recent years, mortgage payment arrears and losses on mortgages remain relatively low.[25] This may be attributed to the relatively low unemployment ratio (6.7% in 2013), low interest rates, the social safety net, the existence of

[25] According to the Spring 2014 OFS report, mortgage payment arrears are only 1.3%. However, it should be noted that refinancing of existing mortgages that are underwater can take place at high LTV ratios since the LTV limit only applies to new mortgages, which may have helped keep losses on mortgages low.

an affordability (LTI) limit, a strong recourse framework for creditors, as well as the favourable net wealth position of the Dutch household sector. However, the authorities noted that the burden of debt on households is one factor explaining the relatively weak economic recovery in the Netherlands (particularly in terms of consumption patterns) since the global financial crisis.

A key recommendation in the FSAP was for the Dutch authorities to assign priority to developing macroprudential instruments, including by taking measures to mitigate the build-up of risks in the real estate sector. Considerable steps have been taken to address these, although the authorities recognise that additional efforts are needed over the coming years.

First, in April 2014 and on the basis of the CRD IV/CRR Implementation Act, DNB announced that it intends to impose additional capital requirements for systemically important banks (SIBs) of between 1-3% of their risk weighted assets, to be phased in between 2016 and 2019.[26] The authorities are also preparing to operationalise the countercyclical capital buffer, but at present have no plans to introduce sectoral capital requirements or risk-weight floors as employed in some other economies.[27]

Second, other instruments that do not form part of the CRD IV/CRR toolkit but may address imbalances in the domestic mortgage and real estate market, have also been developed and employed by the Dutch authorities. In line with the FSAP recommendations, in August 2011 the government imposed an LTV cap for new mortgage lending of 106% effective from 2012, with the cap falling by 1% each year until it reaches 100% by 2018. It also announced that MID would gradually become less advantageous, especially for high earners. These measures sit alongside a government-imposed requirement for lenders to test borrowers' capacity to afford mortgages (see Box 2).

In addition to the measures already implemented, a policy paper on the Dutch banking sector was published in August 2013 following approval by the cabinet at the proposal of the Finance Minister.[28] The paper responded to the recommendations of the Wijffels Committee[29] which, among other things, advised that mortgages should be no higher than 80% of the value of the home brought about through a further stepwise reduction of the LTV ratio after 2018. In its response, the government noted that further stepwise reductions in the LTV ratio would be desirable after 2018 in the interests of consumer protection and healthier bank balance sheets, and expressed its intention to present further proposals once the housing market recovery is firmly under way.

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[26] See http://www.dnb.nl/en/news/news-and-archive/persberichten-2014/dnb306991.jsp. This systemic buffer will be 3% of risk-weighted assets for ING Bank, Rabobank and ABN AMRO Bank, and 1% for SNS Bank.

[27] In response to the FSAP recommendation to consider linking higher LTVs to higher capital ratio requirements, the authorities note that most mortgage lending is by large Dutch banks that operate internal models (which are stress tested for different mortgage scenarios) for Basel III capital adequacy purposes, so their level of regulatory capital already varies with the risk characteristics of their mortgage portfolios.

[28] See "Banking vision paper: towards a robust, ethical and competitive banking sector" by the Ministry of Finance (August 2013, available at http://www.government.nl/news/2013/08/23/banking-vision-paper-towards-a-robust-ethical-and-competitive-banking-sector.html).

[29] A governmental advisory committee led by Herman Wijffels was set up to investigate how serviceability and stability of the banks and the banking system in the Netherlands could be improved.

Lessons learned and issues to be addressed

The legislative and organisational reforms implemented by the Dutch authorities have introduced a comprehensive macroprudential policy framework that broadly addresses the FSAP recommendations. Cooperation and information exchange between the relevant institutions responsible for safeguarding financial system stability have been strengthened via the creation of the FSC. Under the amended Banking Act, DNB now has explicit responsibility for financial stability and has created a separate macroprudential analysis department to carry out this work. In addition, DNB has been assigned the responsibility for calibrating and applying the macroprudential tools in CRD IV/CRR. A formal risk assessment and decision making process for operationalising macroprudential policy has been formulated, and macroprudential risks are being integrated within the supervisory approach. The authorities have also taken steps to address the risks stemming from the housing market, also in response to FSAP recommendations. The most important challenge now consists of deploying macroprudential tools effectively in specific policy contexts by embedding them in existing processes and developing the required analytical and operational capabilities.

The FSC is operational but, given its recent creation and the fact that it has not yet issued many warnings or formal recommendations, it is too early to evaluate its effectiveness in attaining its mandated objectives. The authorities emphasise that the FSC is still finding its way, but that it has played a useful role as a forum for discussing key risks to the financial system and harnessing the perspectives of different authorities with a role in macroprudential policy. The FSC has also enabled the discussion of cross-sectoral issues, and has given impetus to some joint project work (e.g. on bank funding structures and investor base). In that context, the main benefit of the FSC has been to act as an overlay to the existing institutional structure, without seeking to usurp or duplicate mandates and powers of existing authorities, enhancing coordination and information exchange across those authorities.

In order to further enhance the effectiveness of the macroprudential policy framework in the Netherlands, there are three main areas where the authorities may consider taking further steps. These are: strengthening institutional arrangements; enhancing macroprudential analysis and tools for the housing market; and enhancing the role of the prudential authorities in setting LTV and LTI limits.

Institutional arrangements: While good progress has been made in assigning responsibilities in the area of financial stability and macroprudential policy, additional steps could be taken to strengthen institutional arrangements. Most importantly, this would involve further clarifying the role of the FSC within the macroprudential policy framework in order to realise fully the advantages of having such a body. In particular, the authorities should review the experience to date and anticipate possible future developments – both at an institutional level (e.g. implementation of the SSM)[30] and in terms of the evolution of financial markets (e.g.

[30] In that regard and as noted in Box 1, the DNB (and, depending on its future legal status and powers, the FSC) will need to cooperate closely and exchange information with the ECB as foreseen in the SSM Regulation (http://eur-lex.europa.eu/legal-content/EN/TXT/PDF), given the ECB's role in the prudential supervision of credit institutions and in the application of certain macroprudential tasks and tools set out in EU law. Consistency with the macroprudential roles of the ECB and ESRB at the European level is also ensured through the participation of FSC members in the relevant bodies.

importance of systemic risks arising from the non-banking sector) – to determine and publicly communicate the nature of the FSC's involvement in the design and application of macroprudential policies in the Netherlands.

This would involve defining more clearly the role and responsibilities of the FSC vis-à-vis its member institutions; fostering greater collaboration and engagement among its member institutions by levering their comparative expertise (e.g. in joint risk assessments or impact analysis of possible policy measures, such as by establishing an FSC standing sub-committee to carry out some of these tasks); determining the role of the FSC in the deployment of certain macroprudential tools (see below); and enhancing the FSC's communication policy and public visibility in accordance with the identified ambition level. Based on these considerations, it would be helpful to prepare and publish a medium-term plan as well as policies and procedures for the FSC so that member bodies can carry out the necessary preparatory work and external stakeholders are clear about its agenda.

Second, drawing on the example of macroprudential bodies in other countries and the 2011 ESRB recommendation on macroprudential mandates,[31] the authorities should consider enhancing the FSC's legal status. As noted above, the FSC was established via a Ministerial decree rather than primary legislation. A number of the aforementioned steps (e.g. greater collaboration among member institutions, better communication etc.) can be taken within the current legal and institutional setting. However, to further improve its effectiveness and to enhance its credibility as a key part of the macroprudential framework, the authorities should consider embedding the FSC in primary legislation.

Finally, there is a case for reconsidering the current powers of the FSC. At present, the FSC is able to issue recommendations without any binding requirement on recipients to act or to explain why they are not responding. Similar to macroprudential bodies at the EU level and in other countries,[32] there is a public accountability case for recipients to be required to explain their response to an FSC recommendation, even if they choose not to comply.

- ***<u>Recommendation 1:</u> The authorities should further clarify the role of the FSC within the macroprudential framework. Under the existing legal and institutional setting, they should specify and publicly set out the nature of the FSC's involvement in systemic risk assessment and macroprudential policy. In addition, the authorities should consider: (a) embedding the FSC's role and institutional standing in primary legislation to improve further its effectiveness and enhance its credibility; and (b) strengthening accountability for FSC recommendations via the establishment of a formal 'comply or explain' mechanism.***

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[31] See https://www.esrb.europa.eu/pub/pdf/recommendations/2011/ESRB_2011_3.en.pdf. In fact, the absence of primary legislation underpinning the FSC led the ESRB to downgrade an otherwise very strong assessment of the implementation by the Netherlands of this recommendation. See http://www.esrb.europa.eu/pub/pdf/recommendations/2014/ESRB_2014.en.pdf.

[32] See the FSB peer reviews of Germany (http://www.financialstabilityboard.org/publications/r_140409.pdf), the United Kingdom (http://www.financialstabilityboard.org/publications/r_130910.pdf) and the United States (http://www.financialstabilityboard.org/publications/r_130827.pdf).

***Macroprudential analysis and tools for the housing market**:* The FSAP had recommended that the Dutch authorities assign priority to developing macroprudential instruments. Significant steps have been taken in this regard as a result of the implementation of CRD IV/CRR, including DNB's announcement in April 2014 to adopt one such measure (capital buffers for domestic SIBs) and its intention to regularly assess the need to activate the countercyclical capital buffer. In line with the FSAP recommendation, the authorities have introduced a maximum LTV limit for new mortgage lending (alongside existing affordability tests on borrowers), and have adopted plans to reduce MID over the medium term and to limit its eligibility to new mortgages that are (at least) fully amortising on an annuity basis. These measures are a welcome step to mitigating risks to the financial system stemming from the housing market.

As noted above, the high levels of indebtedness of Dutch households, stemming primarily from mortgage borrowing, can be a direct source of risk to the resilience of the financial system. While households in aggregate have significant wealth that offsets their indebtedness, that picture does not hold uniformly at a disaggregated level, with some cohorts (particularly younger ones) having liabilities in excess of assets. Lending to households is also associated with large external funding requirements for domestic banks, creating a source of cross-border financial fragility. Moreover, household debt presents a broader risk to durable and sustainable economic expansion; indeed the authorities note that relatively high levels of indebtedness have contributed to the slow recovery of the economy from the recent recession.

Housing market finance has been the subject of considerable debate in the Netherlands, and is a topic for future discussion by the FSC. Despite the announced gradual reduction in LTV ratios from 106% to 100% by 2018, this limit remains very high by international standards (see Figure 1) – although payment arrears and losses on mortgages have been limited to date. The authorities are concerned that the fragile state of the market would be damaged by going faster in withdrawing public support for the housing market or by implementing new prudential measures to protect banks against potential losses on those exposures. Set against that is the risk that encouraging or permitting new lending at high LTV ratios could create a further tranche of overstretched borrowers, which adds to the vulnerabilities of the already heavily exposed banking system and delays a necessary adjustment to the market. The authorities have indicated that further proposals will be presented once the recovery of the housing market is firmly under way.

To date there has not been a comprehensive public assessment of the case for and against taking more extensive action to reduce vulnerabilities in the housing market. As a result, neither a desired long-run LTV level nor its transition path (beyond 2018) is clear to market participants. The authorities argue that a further reduction of the LTV limit can have far-reaching social consequences and should therefore be implemented while taking into account the development of house prices and alongside a targeted restructuring of the housing market. On the other hand, it should be noted that policy measures to reduce vulnerabilities are not necessarily limited to reducing the LTV limit. Other measures could, for example, include restrictions on the flow of high-LTV lending as opposed to outright limits,[33] the use of other prudential instruments (e.g. sector-specific risk weights for banks' capital requirements) to target high risk lending, and broader reforms (e.g. to the structure of the rental market). These measures could also be complemented by other public policies (e.g. targeted subsidies) to mitigate the impact on vulnerable social groups. It would be important for the authorities to undertake a comprehensive assessment of the risks stemming from the housing market and publicly lay out the relevant considerations and trade-offs under alternative policy actions to mitigate them (e.g. LTV and affordability limits, additional capital requirements, structural reforms to housing market), including their wider economic implications. Given its membership and focus on structural (rather than conjunctural) types of risks, the FSC is well-positioned to coordinate such an exercise.

- ***Recommendation 2:*** ***The authorities, working through the FSC, should undertake a comprehensive assessment of the impact of taking further steps to address housing market risks to the financial system and the economy. The assessment should analyse any identified risks, consider alternative macroprudential and other policy measures, and set out publicly the case for and against taking further actions in this area.***

Responsibility for setting LTV and LTI limits*:* As regards the coherence of the framework for deploying macroprudential tools, it is notable that a number of housing policy measures fall within the government's mandate, given its historically extensive involvement in this market (see Box 2). In particular, the government has the responsibility for setting LTV and LTI limits in addition to determining tax policies, rental controls and zoning restrictions. In fact, an important lesson in this area is that a number of policy measures to address housing market risks may lie outside the realm of the prudential authorities (e.g. policies to affect the supply of new housing or the balance between purchases and rentals); in that sense, the FSC has a useful role to play in bringing together the relevant bodies to discuss the calibration and interaction of these measures.

Developments in the housing market are clearly critical for government objectives, particularly where affordable housing and broader social equity considerations are concerned. However, prudential tools such as LTV and LTI limits that are based on contractual arrangements between borrowers and regulated lenders should be independent from the political cycle and should be set with micro- and macroprudential objectives in mind, while being aware of their potential social and economic consequences. In the international context,[34] the design and application of such tools is typically the responsibility of a prudential authority operating in consultation with other relevant bodies (e.g. consumer protection agency). In that sense, keeping these tools under the control of the Dutch government, without formal input from prudential bodies, may be considered inconsistent

[33] By defining a limit on the percentage of mortgages that can be extended beyond a set LTV by each lender, the authorities can restrict (rather than halt) the provision of high LTV mortgage, while ensuring that the stock of high-LTV mortgages continues to decline over time.

[34] According to available information from the IMF and ESRB, prudential authorities are responsible for setting LTV limits in almost all FSB jurisdictions and EU member states that have such limits in place.

with the spirit of the FSAP recommendation to "provide supervisors with powers to vary the designated macroprudential instrument in response to developments".[35]

In order to address this issue, the FSC should play a greater role in setting LTV and LTI limits in the Netherlands. In the short term, this would involve the FSC making a formal recommendation to the government on the use of these tools. Over the longer term, once the recovery of the housing market is firmly under way and the need for further steps to be taken to address risks in the housing market is assessed, the authorities should consider reallocating the powers for setting LTV and LTI limits to the FSC in order to ensure that all prudential and conduct policies affecting the housing market are set in a coordinated way. In doing so, it would be important that the FSC is required to demonstrate that broader economic consequences are accounted for in any decision taken.

- ***<u>Recommendation 3:</u> The FSC should play a more prominent role in setting LTV and LTI limits to ensure that decisions on the use of these tools are made on the basis of both prudential considerations and their potential impact on consumers and the broader economy. In the short term, this could include the FSC making a formal recommendation to the government on the use of these tools. In the longer term, the authorities should consider reallocating the powers for setting these limits to the FSC.***

3. Crisis management and bank resolution

Background

In the FSAP, the IMF concluded that the authorities' efforts to contain the crisis and protect financial stability were achieved at the cost of "unprecedented levels of government financial support". It added that "as in many other crisis-hit countries, the crisis revealed weaknesses in the Dutch financial oversight and legal frameworks, both for crisis prevention and for the orderly resolution of globally active financial institutions".

The FSAP found the institutional arrangements for crisis response to be broadly appropriate, albeit with a number of caveats. While it concluded that the framework for emergency liquidity assistance (ELA) was strong, it noted that the government had been forced to take over the Dutch part of Fortis and provided solvency support to other Dutch banks. The FSAP recommended the establishment of standing budgetary authorisation for the government to avoid that official commitments for solvency become unfunded, noting that any such authorisation should be designed in a way that does not adversely impact moral hazard (for example, by ensuring that private creditors take appropriate losses). It also recommended that the authorities reform the deposit guarantee scheme so that it is *ex ante* funded, authorised to fund bank resolution operations, and enjoys depositor preference; and that the

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[35] In its most recent annual legislation letter to the MoF (used as input for the legislative cycle), DNB has expressed its desire to obtain a formal advisory role with regard to these instruments, coupled with a comply-or-explain procedure. In its response, the MoF has indicated that the current position of the DNB within the consultation process and its role as economic advisor already provides sufficient room for it to provide advice on the use of these instruments.

institutional framework for bank resolution be strengthened by shifting decision-making power from the judiciary to DNB, by specifying more clearly the respective roles of the MoF and DNB, and by establishing a single regime for resolving banks under official control, with appropriate objectives (including financial stability), tasks and powers for the official administrators.[36]

This section reviews the progress made in addressing those FSAP recommendations in the context of both ongoing domestic policy developments and international and EU regulatory initiatives (see Box 3). Particular focus on bank resolution is provided through analysis of the February 2013 nationalisation of SNS REAAL as a test case against which advances to date and future initiatives can be considered.

Steps taken and actions planned

Institutional arrangements: Since the FSAP, DNB and the MoF have remained the primary institutions responsible for crisis management. The DNB continues to be responsible for providing ELA (subject to ECB rules)[37] and administering the Deposit Guarantee Scheme (DGS), although important changes to the DGS will be implemented in 2015 with the transposition of the EU Deposit Guarantee Schemes Directive (DGSD) into national law. The most important reform to the Dutch resolution regime has been the adoption in June 2012 of the Act on Special Measures for Financial Enterprises ('Intervention Act'). This Act has substantially strengthened the powers of MoF and DNB and their roles in bank resolution. The institutional framework will change further as a result of the implementation of the BRRD and the SRM as part of the European banking union, which will lead to a realignment of responsibilities between European and domestic authorities. The BRRD requires the designation of a national resolution authority, which the MoF proposed to Parliament on 25 June 2014 should be DNB. Legislation to transpose the BRRD into national law is currently being drafted, in pursuit of the 1 January 2015 deadline for national transposition.

Official financial support: The FSAP recommended that standing budgetary authorisation be introduced to provide solvency support. To date, no such measure has been adopted and prior approval of Parliament is required before any solvency support can be provided by the government. Under the current framework, in cases that solvency concerns cannot be remedied privately, resolution measures would be taken in accordance with the Intervention Act (and in the future with national implementation of the BRRD – see Box 3).[38]

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[36] See the FSAP technical note on crisis management and bank resolution frameworks (July 2011, IMF Country Report No. 11/207, http://www.imf.org/external/pubs/ft/scr/2011/cr11207.pdf).

[37] See https://www.ecb.europa.eu/pub/pdf/other/201402_elaprocedures.en.pdf.

[38] Under the BRRD, gone-concern solvency support will only be available in extraordinary circumstances in which, provided that there has been bail-in of at least 8% of total liabilities, it will be possible to finance the resolution of the institution through the European Single Resolution Fund up to a maximum of 5% of a bank's total liabilities.

Box 3: The EU Bank Recovery and Resolution Framework

The EU is establishing a new resolution framework that comprises two primary regulatory elements: the Bank Recovery and Resolution Directive (BRRD)[39] and the Single Resolution Mechanism (SRM).[40]

The BRRD aims to implement the FSB *Key Attributes of Effective Resolution Regimes* (*Key Attributes*)[41] and harmonise the resolution regimes of EU member states. The deadline for national transposition and application is January 2015 (except for the bail-in tool, which must be applied from January 2016). Its main features are:

- EU member states must have a national resolution authority (which must have operational independence if placed within the supervisory authority) with the full range of powers specified in the directive. BRRD-compliant resolution regimes must cover all EU banks and prudentially regulated EU investment firms, and recovery and resolution plans must be developed for all such firms. Authorities must have powers to take early intervention measures prior to resolution, including the power to appoint a provisional manager.
- Partial harmonisation of the creditor hierarchy. Senior debt is *pari passu* with deposits of large corporates; deposits of small and medium-sized enterprises (SMEs) and of natural persons are preferred to senior debt; and 'covered deposits' protected in accordance with the DGSD are preferred to all other deposits.
- EU member states must create a resolution fund financed by banks (in proportion to their size and risk). Resolution funds may be used to absorb losses or to recapitalise an entity but only after at least 8% of total liabilities has been absorbed through bail-in. If the resolution authority determines that bail-in of further liabilities would put financial stability at risk, it may use the resolution fund up to a maximum of 5% of total liabilities. Once this limit is reached, and all senior debt has been bailed-in, public funds may be used.
- The possible earlier use of public funds through government stabilisation tools (i.e. temporary public ownership) in cases of systemic crisis is permitted, provided that 8% of total liabilities has been bailed-in.
- Once bail-in rules are operational, State aid rules will also apply when the Single Resolution Fund is used. Until then, the use of public funds for resolution should follow EU State aid rules for the financial sector.[42]
- Resolution colleges must be created for the planning and execution of resolution of cross-border firms. Decisions by resolution authorities of EU member states have effect in other EU member states, and resolution actions by non-EU jurisdictions can also be recognised by EU member states.

The SRM creates the Single Resolution Board (SRB), which is a new agency responsible for resolution of the largest banks in European banking union area (i.e. the Euro area states plus any other EU member state that opts to join), and establishes a Single Resolution Fund (SRF). The SRM is established by a regulation (except for the SRF which is included in an inter-government agreement)[43] and therefore does not require transposition. The SRB will be responsible for resolution planning and decision making in a resolution for all banks supervised directly by the ECB and all cross-border banks. National resolution authorities will remain responsible for resolution planning and resolution of all other firms (unless the SRF is used, in which case the SRB will be responsible) and for executing the SRB's decisions. The SRB will assume functions relating to resolution planning in January 2015 and, from 2016, will be responsible for resolution of EU banks.

The ECB is principally responsible for determining whether the conditions for resolution are met, although the SRB may also take the decision (but must give the ECB three days of advance notification). The SRB will then prepare a resolution scheme that must be validated by the EC in the following 24 hours. The EC may, in the first 12 hours, involve the European Council for decisions regarding the use of the SRF or the public interest condition. The resolution scheme is executed by national resolution authorities.

The SRF target size is €55 billion, to be reached in 8 years from 2016. During the transitional period, national compartments are created within the SRF for use in resolution, but these cease to exist from 2024 onwards.

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[39] See http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.173.01.0190.01.ENG.

[40] See http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.225.01.0001.01.ENG.

[41] See http://www.financialstabilityboard.org/wp-content/uploads/r_141015.pdf.

[42] See http://eur-lex.europa.eu/legal-content/EN/ALL/?uri=CELEX:52013XC0730(01).

[43] See http://register.consilium.europa.eu/doc/srv?l=EN&f=ST%208457%202014%20INIT.

Deposit guarantee scheme: While the FSAP recognised that an EU DGSD was pending, it encouraged urgent and rapid reform to the Dutch system. It recommended that the Dutch DGS be *ex ante* funded by contributions paid in proportion to banks' insured deposits, be permitted to financially support resolutions, and that depositor preference for insured depositors or the DGS itself be adopted.[44] Because the authorities decided to wait for the approval of the DGSD[45] to establish an *ex ante* funded DGS, most of these reforms have not yet been carried out (although the Intervention Act does allow the DGS to fund a transfer of deposits). However, they will be addressed through transposition of the DGSD and BRRD.

Transposition of the DGSD[46] will introduce the following elements for all DGSs in the EU: required *ex ante* funding (target level 0.8% of covered deposits); contributions by banks to the DGS will be based on the amount of covered deposits and the degree of risk incurred; the DGS may be used to fund resolution when the cost is less than it would be to pay out covered deposits; and repayment of deposits in the case of a bank failure will be gradually reduced from 20 working days to 7 working days by 1 January 2024. The coverage limit for deposits remains at €100,000 per depositor per bank (subject to exceptional protection for temporarily high deposit balances).

Even before the new DGSD was finalised, DNB began working with the MoF on the necessary legislative amendments and set a national deadline of 1 July 2015 for its implementation. Dutch banks will have to start making quarterly contributions to the DGS on this date. Depositor preference for retail and corporate depositors is required by both directives and therefore will also be part of the Dutch scheme.

Bank resolution framework: In 2011, the FSAP recommended strengthening the institutional framework for crisis management and bank resolution by establishing a single regime for resolving banks under official control with appropriate objectives (including financial stability), tasks and powers for the official administrators; and by specifying more clearly the respective roles of the MoF and DNB in bank resolution. It also recommended that decision-making power be shifted from the judiciary to DNB to improve the rapidity of resolution actions and ensure adequate attention to financial stability.

Although significant reforms will be implemented in the coming years, the Intervention Act already represents a considerable overhaul of the Dutch framework for bank resolution and addresses several of the FSAP recommendations in this area. In particular, the Act introduced new powers for DNB and the MoF in the resolution of financial institutions, including in cases where financial system stability may be at risk (see Box 4).

The DNB may intervene in failing banks and insurers at the level of operating companies, provided that the Amsterdam District Court has agreed that the following criteria for intervention are met: (a) there are signs of a dangerous development regarding own funds, liquidity, solvency or technical provisions of a bank or insurer; and (b) it is reasonably

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[44] For more details on the Dutch DGS, see the February 2012 FSB peer review report on deposit insurance systems (http://www.financialstabilityboard.org/publications/r_120208.pdf).

[45] This seemed imminent at the time of the FSAP but was then delayed until the second quarter of 2014.

[46] See http://eur-lex.europa.eu/legal-content/EN/TXT/?uri=uriserv:OJ.L_.2014.173.01.0149.01.ENG.

foreseeable that this development will not be reversed sufficiently or promptly. The principal power conferred by the Intervention Act enables the DNB to prepare a "transfer order" for the transfer, in whole or in part, of assets and liabilities (including deposits) or the shares issued by the failing institution at a fair price to a third party. However, the consent of the MoF is required to transfer ownership.

Although the Intervention Act confers administrative resolution powers, the courts retain a central role in the exercise of the resolution powers by both DNB and the MoF. First, advance approval by the Amsterdam District Court is required for implementation of a DNB transfer plan. Second, shareholders have a right to oppose a DNB decision to execute a transfer plan concerning the transfer of shares within eight days following the decision. Shareholders may also apply to the Enterprise Chamber of the Amsterdam Court of Appeal for indemnification for damage caused by the loss of shares that is not covered by the price paid by the purchaser. Finally, interested parties can appeal the exercise of Intervention Act powers by the MoF to the Administrative Division of the Council of State within ten days following the decision. The Intervention Act also provides an indemnification procedure for expropriated parties through the Enterprise Chamber of the Amsterdam Court of Appeal.

Box 4: Main Intervention Act Features and Alignment to the *Key Attributes*

The current resolution framework established by the Intervention Act has the following features:

- DNB is the resolution authority for banks and insurance companies that are failing or likely to fail.
- Through the use of a "transfer order", DNB has the power, following approval by the Amsterdam District Court, to execute:
  - the sale of the problem institution to a private party by transfer of shares;
  - the transfer of deposits of the problem institution to a private party, with funding from the DGS;
  - the transfer of the problem institution's assets and liabilities to a private party, permitting the problem institution to be split into a 'good bank' and a 'bad bank'.
- In cases where no private party is willing to take over the problem institution, DNB may effect a transfer to a bridge institution.
- The MoF also has resolution powers, but they are limited to cases where there is an immediate and serious threat to the stability of the financial system as determined by the MoF in consultation with DNB and with agreement by the Prime Minister. In such a case, the MoF has the following powers that can be applied to financial institutions, including non-bank financial companies and financial holding companies:
  - Intervention in the internal management of a financial institution;
  - Expropriation of assets, liabilities or securities issued by a financial institution.

The exercise of powers by both the DNB and the MoF is subject to the 'no-creditor-worse-off-than-in-liquidation' principle. The Intervention Act also overrides contractual early termination rights that would otherwise arise through exercise of DNB or MoF powers.

As identified in the FSB's April 2013 peer review report on resolution regimes,[47] the Dutch resolution regime is missing the following elements that are required for full alignment with the *Key Attributes*:

- Power (in non-systemic circumstances, and for DNB as resolution authority) to intervene in holding companies or non-regulated group entities.

[47] See http://www.financialstabilityboard.org/publications/r_130411a.pdf.

- Powers to require group companies to provide services to a firm in resolution or its successor (to support continuity of critical functions).
- Power (in non-systemic circumstances, and for DNB as resolution authority) to operate a firm in resolution.
- Power to write down and covert liabilities (bail-in) within resolution.
- Power to impose a temporary stay on early termination rights under financial contracts.
- Power to depart from equal treatment of creditors of the same class.
- Mechanism for recovery from the firm, its creditors or the industry, of public funds used in resolution..
- Legal provision to encourage cross-border cooperation.
- Mechanisms for giving domestic effect to foreign resolution measures.
- Powers to require changes to firms to improve resolvability.

The Dutch authorities expect to introduce these powers by transposing the BRRD.

The Dutch authorities have been developing the institutional structure, information sharing arrangements and recovery and resolution planning processes for their evolving bank resolution responsibilities. Several changes have been made to DNB's organisational structure in recent years, including the creation of a new Supervisory Division to integrate all centres of expertise and, within that, a dedicated Intervention department that is responsible for coordinating intervention measures. A MoU governing information exchange and cooperation for crisis management purposes is in place between the MoF and DNB. The MoU provides for a Mixed Working Group for Monetary and Financial Stability issues that meets regularly to discuss the stability of the financial system and policy measures taken in that regard. It also stipulates that, should DNB become aware of a crisis affecting a financial institution, it must establish a crisis management team and notify the MoF of its assessment of the situation and the crisis measures that are required.[48] Under the MoU, DNB will act as a crisis manager and will implement the crisis measures that lie within its mandate.[49] DNB maintains a crisis management manual that describes the organisation, mandates and lines of communication within DNB, and the supporting structure (Tripartite Crisis Management) to organise and facilitate collaboration between MoF, AFM, and DNB.

Nationalisation of SNS REAAL: The resolution framework established under the Intervention Act was tested on 1 February 2013 with the nationalisation of the fourth largest Dutch bank, SNS REAAL, resulting in the expropriation of the shares of SNS REAAL and the subordinated debt of SNS REAAL and SNS Bank (see Table 1 and Annex 2 for details). The nationalisation followed an extended period of public support and attempts to stabilise the bank. This began in 2008 with €750 million in state aid provided to shore up solvency at its insurance subsidiary REAAL. In 2011, DNB concluded that SNS REAAL could not effectively resolve its financial situation on its own due to increasing losses in the bank's real estate portfolio (concentrated in a recently acquired subsidiary, Property Finance). A joint MoF-DNB project group was established to evaluate a range of private, private-public and public alternatives over the course of 2012. In late January 2013, DNB informed the institution and the Minister of Finance that the solvency problems at the bank had become too severe to justify the continuation of its banking license. The Minister, in close consultation

[48] Under the Intervention Act, DNB must also inform AFM when DNB is preparing a transfer order.

[49] Where MoF involvement is needed to take action, DNB will include the MoF in the crisis management team.

with DNB, concluded that bankruptcy was not possible because of strong negative consequences for financial stability and that all other private and private-public alternatives were not available, and therefore nationalised the institution to safeguard financial stability.

Table 1: Chronology of the nationalisation of SNS REAAL

1997	Merger between SNS banking group and REAAL insurance
May 2006	Initial public offering (part of growth strategy)
Jul 2006	Acquisition of Property Finance from ABN AMRO
Nov 2008	State support of €750 MM due to solvency concerns at REAAL
2009–2010	Negative impact on group of combination of vulnerabilities and worldwide financial crisis
2010–2011	Consolidation and reorientation leading to DNB’s conclusion that SNS REAAL cannot survive independently
2012	Resolution planning—selling the insurer, public-private solution with three large banks, private equity, and transfer instrument
27 Jan 2013	DNB imposes a deadline of 31 Jan 2013 by which time SNS REAAL must meet all capital requirements
1 Feb 2013	Minister of Finance, after consultation with DNB, nationalises SNS REAAL
25 Feb 2013	The Council of State rules that the Minister of Finance was permitted to expropriate SNS Bank and SNS REAAL’s securities, including shares and subordinated debt, but not future claims
11 July 2013	Enterprise Chamber of the Amsterdam Court of Appeal rendered an interim decision that the MoF had not convincingly argued that €0 represented full compensation and ordered experts to advise on the proper value of the expropriated securities and subordinated private loans.
19 Aug 2013	The Dutch State submits a restructuring plan for SNS REAAL to the EC
9 Oct 2013	The Dutch State lodges an appeal against the interim decision of the Enterprise Chamber, seeking a Supreme Court decision on how certain aspects of the Intervention Act should be interpreted; Enterprise Chamber postpones the expert valuation procedure
19 Dec 2013	Based on the restructuring plan, the EC decides that the intervention and the proposed restructuring of SNS REAAL are compatible with the internal market
31 Dec 2013	The Dutch State transfers its shares to NL Financial Investments (NLFI), making NLFI the sole shareholder of SNS REAAL
23 Jan 2014	Evaluation Commission publishes its report on the actions of DNB and the MoF with regard to SNS REAAL

At the time of nationalisation, the State expected to incur costs of €3.7 billion in stabilising the failed SNS REAAL (€2.2 billion in new capital, €0.8 billion in written off earlier aid and €0.7 billion to isolate the real estate portfolio). That sum could have been offset to a significant extent if senior creditors had been expropriated, in addition to the shareholders of SNS REAAL and the subordinated debtholders of SNS REAAL and SNS Bank. However, on the advice of DNB, this option was not pursued because of the perceived risk of contagion to other Dutch banks, given their dependence (relative to banks in other countries) on international unsecured funding markets rather than local deposits.[50] In his Decree, the Minister cautioned that had senior creditors been impaired, Dutch markets could have faced appreciably higher funding costs and possibly the withdrawal of funding sources. Since there would have been large assessments required for the DGS had SNS REAAL gone through bankruptcy, an *ad hoc* resolution tax of €1 billion was levied on Dutch banks, partially compensating the State for its expenses.

The impact of the nationalisation on other Dutch banks is reported not to have been significant, indicating that the problems at SNS REAAL were apparent to the market for some time and perceived as being specific to that individual case. While one of the major credit rating agencies determined that the nationalisation represented a loss of implicit government support for Dutch banks, there has not been a notable effect on market prices or the behaviour of investors in debt instruments of these institutions. The authorities note that fluctuations in the credit spreads of Dutch banks since the nationalisation appear to have been driven mainly by developments in the Euro area.

The authorities continue to manage outstanding litigation and pursue exit transactions from the nationalisation. The Dutch Council of State rejected appeals by claimants to reverse the expropriation, ruling that the MoF was permitted to expropriate securities and loans issued, but upheld the right of the former shareholders to appeal the valuation of the expropriated shares. The level of compensation has also been a subject of appeals. Based on the likely outlook for SNS REAAL had the expropriation not taken place, the MoF determined that the level of compensation for affected investors should be €0 (reflecting the expected negative value of the expropriated securities and capital instruments of SNS REAAL and SNS Bank in the event of bankruptcy). In an interim decision, the Enterprise Chamber of the Amsterdam Court of Appeal ruled that the MoF had not sufficiently substantiated this valuation. The MoF has appealed the decision and a Supreme Court ruling to settle the matter is pending. Concurrently, the re-privatisation process is being mandated by the MoF and conducted though NL Financial Investments (NLFI), a foundation under Dutch law that operates as a trust to which the State transferred its shares in SNS REAAL on 31 December 2013. In 2014, in accordance with agreements with the EC, the process to sell the insurance company REAAL has been set in motion.

The Evaluation Commission, which was established by the Minister of Finance in March 2013 to investigate the nationalisation of SNS REAAL, reported its findings on 23 January 2014 (see Annex 2).[51] The Commission made recommendations on the functioning of DNB and the MoF (e.g. role of the DNB president in the governance structure for the supervision of financial institutions) and on the legal basis for interventions in the financial sector (e.g. that DNB's resolution powers should be extended to financial holding companies).

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[50] While DNB's ELA extends to banks and the banking portion of financial conglomerates, this was not required for SNS REAAL given that the failure stemmed from credit impairments unfolding over a number of years rather than any sudden liquidity outflows.

[51] See "Nationalisation of SNS REAAL unavoidable in the absence of viable alternatives" by the Dutch Ministry of Finance 23 January 2014, http://www.government.nl/news/2014/01/23/nationalisation-sns-reaal-unavoidable-in-the-absence-of-viable-alternatives.html).

Resolution planning and cross-border cooperation: DNB now requires 26 large and medium-sized banks to develop recovery plans, while resolution planning is concentrated primarily on the large SIBs (ING, Rabobank and ABN AMRO) with SNS REAAL excluded for the time being as it is undergoing restructuring. DNB is pursuing a "single point of entry" strategy for these SIBs, and is now in the process of developing operational resolution plans in collaboration with them and with the MoF. To date, however, these processes have not been accompanied by requirements for the SIBs to make significant changes to their group structures and operations to enhance resolvability. DNB has concluded that certain changes that might enhance resolvability would have material negative impacts on the competitiveness of some of institutions if adopted abruptly.[52]

In an effort to strengthen home-host cooperation and in accordance with the *Key Attributes,* DNB has established crisis management groups (CMGs) for two Dutch SIBs, ING (which has also been designated by the FSB as a global SIB) and Rabobank. The CMGs are used to share information and consider resolution strategies, operational resolution plans and resolvability assessments. DNB is in the process of finalising a cross-border cooperation agreement for ING and will also conclude another one for Rabobank.

Planned reforms to crisis management and resolution framework: A number of reforms are planned to the Dutch resolution framework building on the lessons from the SNS REAAL case and in response to the BRRD and the SRM (see above and Box 3).

Implementation of the BRRD requires the designation of a single Dutch resolution authority. The Minister of Finance has already communicated to Parliament in a letter dated 27 June 2014 his decision to propose DNB as that authority. The Minister's letter explains that this decision is based in part on DNB's existing expertise and on the potential for close coordination and information exchange between the supervisory function and the resolution function. It also describes certain safeguards designed to ensure the independence of the resolution function and appropriate coordination with the supervisory function that are expected to be put in place. While the resolution function will be independent in respect of its decision-making about the minimum amount of gone-concern loss absorbing capacity that institutions must hold and the removal of procedural obstacles to bail-in, other decisions to enhance resolvability will be shared with the supervision function of DNB.

The SRM will substantially alter the institutional arrangements for crisis management and bank resolution in the Netherlands. For systemic and cross-border banks, the ECB and the SRB, rather than the national authorities, will be responsible for determining that conditions for resolution are met. It is expected that banks accounting for more than 85% of the Dutch banking sector will fall within the direct responsibility of the Single Resolution Board (SRB). This implies that the SRB will hold the primary responsibility for resolution decisions, including for resolution planning, for the Dutch SIBs. The Dutch authorities will remain responsible for non-systemic banks, and will have to coordinate and comply with instructions and guidance from the SRB.

[52] Changes that have been examined in this respect include restructuring to optimise the location of subsidiaries within the group for purposes of resolvability and other structural and operational modifications that would disentangle operating companies.

Lessons learned and issues to be addressed

Major steps have been undertaken to upgrade the framework for crisis management and bank resolution in the Netherlands, with several more reforms forthcoming in the near future. The Dutch authorities should be commended for their rapid adoption and implementation of the Intervention Act, which addressed some of the recommendations made in the FSAP. These include the establishment of a single regime for resolving banks, a clearer specification of the roles of DNB and MoF, and the ability for the DGS to fund resolution. In addition to the legislative framework, work on recovery and resolution planning is well underway, while the coordination processes established between DNB and MoF enhanced the authorities' ability to manage the nationalisation of SNS REAAL. The Evaluation Commission's review of that nationalisation delivered some recommendations to improve the resolution regime, but it also concluded that the powers of the Intervention Act functioned effectively and were crucial in achieving the ultimate objective of safeguarding financial stability.

Further progress in addressing the FSAP recommendations on official financial support and deposit insurance will be realised when the Netherlands transposes the DGSD and the BRRD and when the SRM becomes operational. Implementing these reforms will be a considerable undertaking, but should close the remaining gaps identified in the FSAP and enhance the alignment of the bank resolution framework with the *Key Attributes*.

Nonetheless, there are some key actions that the Dutch authorities could take to further enhance the effectiveness of the resolution framework. These involve rapid adoption of the legislative changes needed to align the resolution regime with the *Key Attributes*; reconsidering and revising certain aspects of the existing institutional framework; and enabling the national resolution authority to exercise its functions in an independent manner.

Adoption of pending legislative changes: The transposition of the DGSD will introduce important new elements to the Dutch DGS (e.g. minimum required *ex ante* funding, risk-based bank contributions etc.) and would address the FSAP recommendations in this area.[53] Moreover, as shown in Box 4, the Intervention Act did not introduce all of the powers and instruments specified in the *Key Attributes*, partly because it was intended to adopt them in coordination with other European countries through the BRRD. The implementation of these two Directives and the establishment of the SRM provide an appropriate context to enhance the Dutch DGS and to align the resolution regime fully with the *Key Attributes*, taking into account the experience of SNS REAAL.

- ***Recommendation 4:*** ***The authorities should continue work to transpose BRRD and DGSD promptly into national legislation in order to address the remaining FSAP recommendations on deposit insurance and resolution and to further align the Dutch resolution regime with the FSB's Key Attributes.***

[53] For example, the lack of *ex ante* DGS funding was a material complication that limited the options available during the 2011-2013 resolution planning period for SNS REAAL. DNB estimated that if SNS REAAL had been permitted to go through bankruptcy, the *ex post* cost to Dutch banks would amount to €5 billion. However, this assumes an estimated 85% recovery rate on SNS Bank's assets and, while recoveries were being made, the upfront costs necessary to repay depositors might have been considerably higher (which would put additional stress on the banking sector) or deposit payouts would have been delayed.

Realignment of the institutional framework for resolution**:** The Intervention Act defined the respective powers and roles in resolution of the MoF and DNB. In June 2014, the Minister of Finance announced that, through transposition of the BRRD, DNB will be established as the national resolution authority and provided with important additional powers specified in the *Key Attributes*. As a result, DNB will have the authority (extending to non-financial companies) and resolution powers (including bail-in and bridge bank) to intervene in such a way that the likelihood of MoF involvement becomes remote.

However, the Dutch authorities will maintain a division of resolution responsibilities and powers between DNB and the MoF, with the latter retaining the powers to intervene in the internal governance of an institution and to nationalise through expropriation of shares. Since the MoF's powers only apply in cases where there is an immediate and serious threat to the stability of the financial system, there may be some overlap with firms for which the SRB is primarily responsible. The division of resolution responsibilities and powers that will be adopted in the Netherlands as part of BRRD transposition will need to take these factors into account to ensure an effective institutional framework.[54]

In the case of a transfer plan approved by the Amsterdam District Court and executed by DNB, shareholders have eight days to file an appeal. In the case of expropriation by the MoF, claimants have up to ten days. In both cases, the court can potentially reverse the actions taken to resolve a failing institution, as was sought (though subsequently denied) in the case of SNS REAAL. The role of the courts was not problematic in the case of SNS REAAL, although this may in part be due to the nature of the institution's failure, which was precipitated by a relatively slow moving impairment to its real estate portfolio over a period of years. While it may be unlikely in practice that the court would overturn a transfer plan or expropriation, the uncertainty that this extended appeals period introduces may be unwelcome at a time when the authorities are focused on stabilising a failing institution.

The SRB will assume responsibility for resolution planning and decision making for systemic and cross-border banks in the EU banking union, affecting several institutions in the Netherlands. As these changes are implemented, the crisis management protocols that are currently in place will need to be modified to reflect the new roles, responsibilities, and relationships between the relevant authorities. Inter-agency MoUs between DNB, the MoF, and the AFM, and the DNB's crisis management handbook, should therefore be updated and revised accordingly.

- ***Recommendation 5*****: *In transposing the BRRD, the authorities should clarify the roles and powers of the relevant authorities in the resolution framework and update crisis management protocols for inter-agency coordination.***

Balancing supervisory and resolution concerns: The authorities have presented proposals to ensure the operational independence of the resolution function, as required by the BRRD, within the broad range of responsibilities of DNB. A recalibration of the organisational structure will be implemented within DNB that aims to balance the advantages of cooperation between the supervisory and resolution functions against the risks that the lack of full

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[54] The tools and powers of the MoF will also need to be consistent with the SRM framework as of 2016. The use of government stabilisation tools within SRM countries is not covered by the SRM Regulation.

institutional independence (i.e. the resolution authority as a separate organisation) will result in resolution priorities being subordinated to other interests. The objective is that DNB's resolution directorate will be independent from, and have no role in, supervision, financial stability or monetary functions. The resolution directorate will also have sole decision-making responsibility for the implementation of resolution measures. Given the potential trade-offs between going-concern and gone-concern interests, decision making on *ex ante* measures to enhance the resolvability of institutions will be made by the DNB Board, taking into account both resolution and supervision considerations.

The SNS REAAL case highlighted the importance of the supervisory or resolution authorities having the ability to require financial institutions to adopt changes to their structure, organisation or business practices to improve their resolvability. In particular, it showed that complex legal and financial interdependencies can make resolution more difficult, increase the potential for contagion, and frustrate some alternative solutions. Changes to firm structure or operations to address obstacles to resolution identified at other Dutch firms have not been required to date. Analysis conducted prior to the establishment of an independent resolution directorate within DNB indicates that such changes might significantly impair firms' competitiveness. As the DNB's resolution function is established with appropriate safeguards for operational independence in place, it should continue to examine as part of resolution planning work and in collaboration with the SRB the options for, and potential costs and benefits of, requiring changes to Dutch SIBs' structures or operations in order to enhance their resolvability.

- ***Recommendation 6:*** ***As DNB takes on the role of the designated resolution authority in the Netherlands, it should exercise the resolution function with sufficient operational independence to effectively carry out its mandate, including the ability to appropriately examine and address identified obstacles to the resolvability of SIBs.***

Annex 1: Structure of the financial system and recent developments[55]

Financial system structure

<u>General overview of the Dutch financial sector</u>

The Dutch financial system comprises three main sectors: banks with total assets of around EUR 2.4 trillion (400% of GDP), insurance companies with total assets of around EUR 450 billion (75% of GDP), and pension funds with total assets under management of around EUR 950 billion (160% of GDP). The financial sector has been under pressure in recent years, because of the difficult economic environment and sector-specific factors (see below). Recently, there have been some indications of economic recovery in the Netherlands and the rest of EU, which has had a positive impact on financial stability. However, some structural challenges remain. In its recently published Vision on Supervision 2014-2018,[56] DNB has formulated the key challenges for the different sectors in the upcoming years, which constitute the main priorities in supervision of DNB.

<u>Supervisory framework</u>

The Dutch model of financial supervision is characterized by a functional approach, often referred to as the Twin Peaks model. In this model, DNB is responsible for prudential supervision of financial institutions and the AFM is responsible for conduct of business supervision. The MoF is responsible for legislation on financial institutions and markets, which is primarily laid down in the Act on Financial Supervision. The Ministry of Social Affairs is responsible for the legislation on pension funds within the Pension Act.

DNB is an organization with 1,659 full-time equivalent staff, of which 768 are dedicated to supervisory activities (annual report 2013). It is structured in five supervisory divisions, three of which are responsible for direct supervision of banking, insurance and trust agencies, and pension funds and investment firms. There is a separate supervisory policy division that is *inter alia* responsible for developing and implementing regulation, and a supervisory expertise division that is responsible for internal risk management and dedicated aspects of supervision (e.g. market access, intervention, information technology risks, integrity). In addition, there is a separate financial stability division that is responsible for macroprudential policy and the financial stability tasks of DNB.

The DNB's Board of Directors consists of five members who have a joint responsibility for decision making. Within the Board, two Executive Directors are primarily responsible for supervision and one Executive Director is primarily responsible for macroprudential policy and financial stability.

<u>Recent developments</u>

Since the FSAP, several important legislative and organisational reforms have been implemented, the most important of which are:

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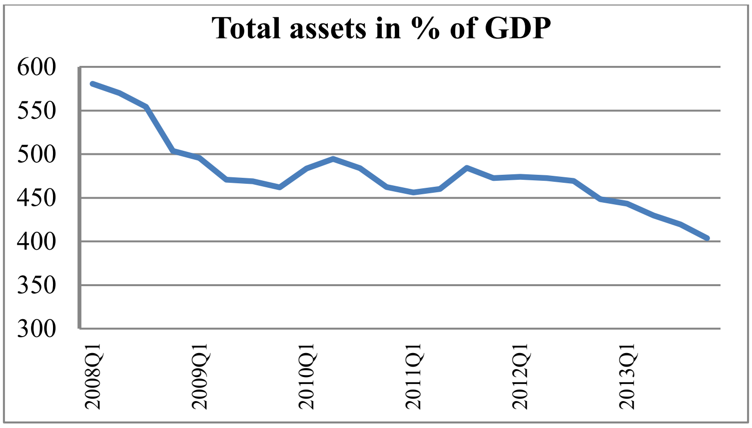
[55] Based on information provided by the Dutch authorities.

[56] See http://www.dnb.nl/en/binaries/DNB%20Supervisory%20Strategy%202014-2018_tcm47-307508.pdf.

- Creation of a new supervisory expertise division to increase supervisory effectiveness, including the creation of a separate intervention department (January 2011).
- New legislation to strengthen the governance of DNB and the AFM (February 2012) has been implemented. A Chairman of Supervision has been appointed and the Supervisory Council was created to support decision making within DNB with regard to supervision.
- The introduction of a new supervisory approach entitled Focus! (February 2012),[57] which constitutes a more risk-based, top down approach of supervision and a more thematic approach.
- The introduction of the Intervention Act (June 2012).
- Implementation of new legislation to limit the liability of supervisors (July 2012).
- Development of recovery and resolution plans (2013-2014).
- The creation of a macroprudential committee, the Financial Stability Committee (November 2012).
- Amendment to the Banking Act to give DNB explicit responsibility for financial stability (January 2014).
- Amendment to the Act on Financial Supervision to reflect that the activities of the AFM are "also in the interest of financial stability".
- The introduction of a national regime for strengthened supervision for insurance companies (January 2014).
- Implementation of CRD IV / CRR to implement Basel III. This also provides DNB with several macroprudential instruments, including the implementation of a SIB buffer (January 2014).

Banks

The Dutch banking sector has been strongly affected by the global financial crisis. The size of the sector has declined in recent years, primarily because of divestments of foreign activities (including the break-up of ABN AMRO and remedies to comply with EC requirements).



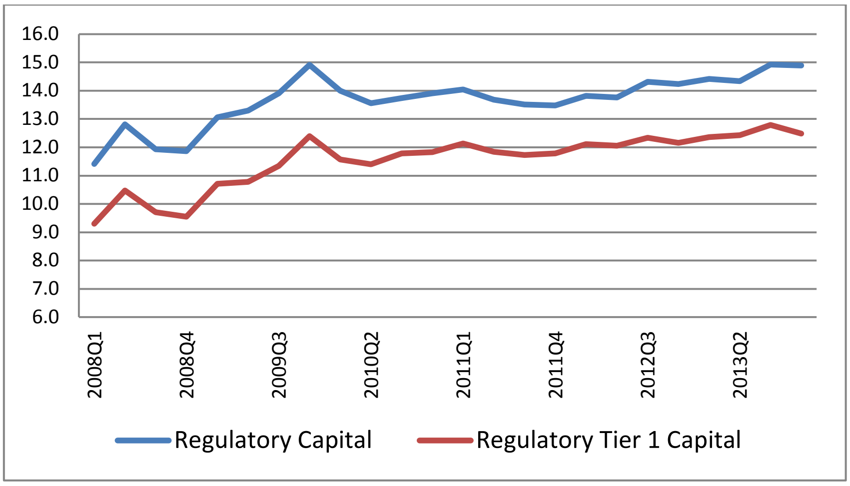
57 See http://www.toezicht.dnb.nl/en/binaries/51-225814.pdf.

In recent years, the banking sector has become smaller and more domestically orientated. It remains relatively concentrated with a few large, internationally active banks (ING, Rabobank, ABN AMRO, SNS Bank).

Structure of the Dutch banking sector 2008-2013 (year-end)[58]

	2008	2009	2010	2011	2012	2013
Total number of banks	87	84	86	87	85	88
- domestic	*31*	*29*	*29*	*28*	*27*	*28*
- foreign (subsidiaries, branches)	*56*	*55*	*57*	*59*	*58*	*60*
Total assets (mln euro)	2,994,682	2,648,109	2,713,249	2,832,155	2,687,903	2,433,722
Total assets (in % GDP)	503.75	461.96	462.39	472.78	448.48	403.83
Share of domestic banks (% of total assets)	96	96	87	89	90	92
Share of 5 largest banks (% of total assets)	87	85	84	84	82	84
Average size of banks (EUR mln assets)	34,422	31,525	31,549	32,554	31,622	27,656

The banking sector is well capitalized. Banks have increased their capital ratios and, according to the DNB, are well on track to meet the Basel III requirements.

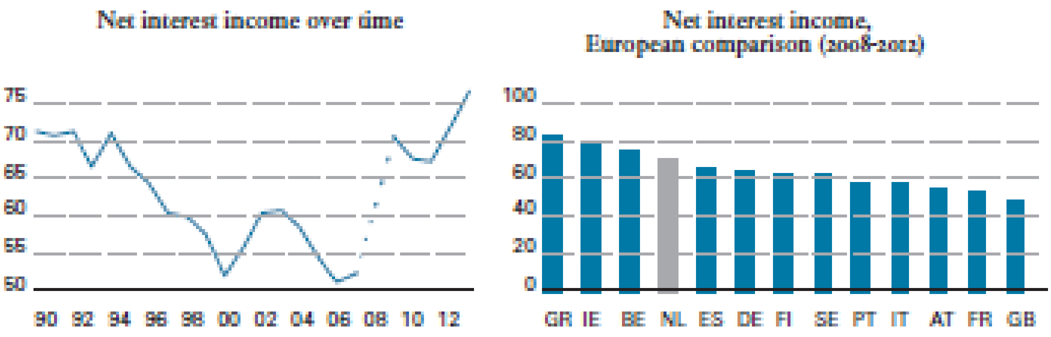


The total income of Dutch banks has declined since the financial crisis, with a renewed shift towards interest margin as the traditional source of income. At the same time, banks have reduced their expenses and therefore have succeeded to restore their operating profit.

58 The DNB website contains an extensive dataset of monetary and financial statistics for the Netherlands (http://www.statistics.dnb.nl/en/home/index.jsp).

Dutch banks return to traditional lending business

Net interest income as a percentage of total income; 2008 has been omitted because total income was negative. Right-hand chart shows median for 2008-2012



Source: DNB.

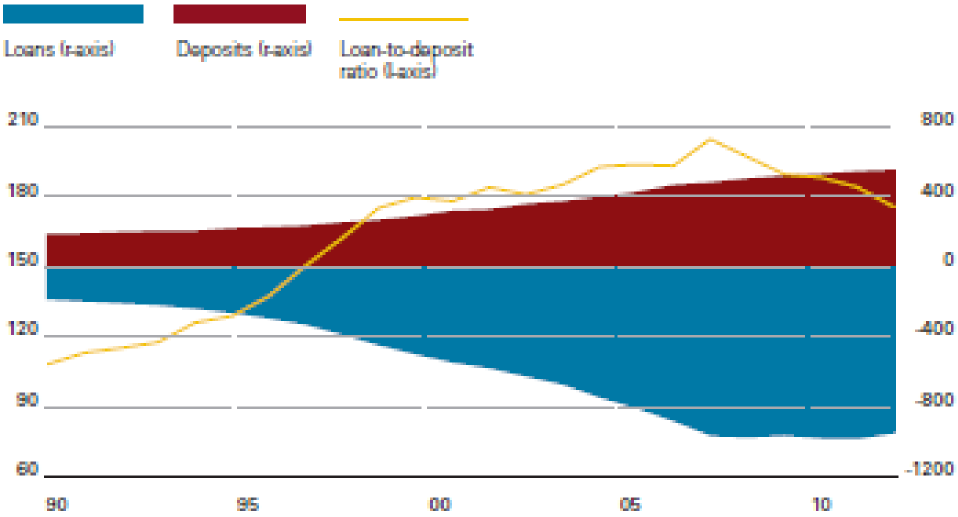
Performance of Dutch banks 2009-2013 (EUR billion)

	2009	2010	2011	2012	2013
Total income	**44.6**	**50.4**	**51.4**	**45.4**	**43.2**
Net interest income	30.0	33.1	32.9	31.0	31.4
Net fee and commission income	9.7	10.4	9.5	7.4	7.5
Other	4.9	6.9	8.9	6.8	4.3
Expenses	**45.1**	**39.9**	**41.8**	**39.0**	**36.2**
Operating expenses	31.4	32.7	31.3	30.0	28.1
Provisions	13.7	7.2	10.5	9.1	8.1
Profit/loss from continuing operations	**-0.5**	**10.5**	**9.6**	**6.3**	**7.0**

Dutch banks are dependent on international market funding, as their deposit base is smaller compared to their loan portfolios.[59] This funding gap (as measured by the loan-to-deposit ratio) reflects – among other things – the high level of mortgage debt in the Netherlands. Recently, steps have been taken to gradually remove distortions in the housing market and limit household mortgage debt (see section 2). Due to a combination of factors, the loan-to-deposit ratio has declined in recent years.

[59] See http://www.dnb.nl/en/binaries/OFS_Spring_2013_web_tcm47-289597.pdf for more details.

Deposits from, and loans to, non-financial companies and households in EUR billion. Ratio in percentages



Source: DNB.

With the start of the SSM, the supervision of significant banks will be transferred to the ECB. In preparation for its new task, the ECB is conducting a comprehensive assessment with an asset quality review and a stress test to validate the quality of the balance sheets of the banks. The bank-specific results are expected to be published in October. Prior to the ECB comprehensive assessment, DNB performed in 2012-2013 its own asset quality review on the commercial real estate (CRE) portfolio of banks. DNB has done an intensive, on-site analysis on the three largest Dutch banks (ING, Rabobank and ABN AMRO) to improve risk management and data quality of the portfolio, as well as to ensure more accurate valuations of collateral and associated increases in reserves and provisioning. As such, DNB has concluded that the banks currently hold sufficient buffers to accommodate expected losses on CRE exposures. This conclusion has been communicated in a public letter to Parliament.

Insurers

The insurance sector faces several structural challenges. The low interest rate environment puts pressure on the solvency position and business model of life insurers. In addition, life insurance companies are confronted with a more competitive environment, because some preferential tax treatments, including some that were specific to the insurance sector, have been limited or abolished. At the same time, their cost structure is still relatively high and they still have to work to re-establish the confidence in the insurance sector, reflecting a reputational fall-out because of selling of high-cost life insurance products.

Figures for Dutch insurers 2009-2013

	2009	2010	2011	2012	2013
Solvency ratio (%)*					
- Life	245	242	239	263	249
- Property & casualty (P&C)	321	327	302	312	302
- Health	197	188	190	187	218
Operating income (EUR million)					
- Life	2,070	180	-460	360	2,235
- P&C	1,312	1,140	849	524	700
- Health	1,335	602	586	1,360	1,529
Balance sheet total (EUR billion)					
- Life	317	338	363	391	370
- P&C	40	41	40	42	41
- Health	25	27	29	33	32

* Solvency I figures

Regulation for insurance companies has recently been strengthened with the introduction of a national solvency regime, effective 1 January 2014, including a risk based solvency requirement and an own risk assessment. This provides an important step forward to make insurance supervision more forward-looking and risk-based, in anticipation of the introduction of Solvency II, expected on 1 January 2016.

Pension funds

Dutch pension funds have suffered from the low interest rate environment. As a result, their nominal coverage ratio has fluctuated in recent years around 100%. Several pension funds, were required to develop recovery plans, encompassing an increase in premiums and – in the case of 66 pension funds – a lowering of benefits (on average with 1.9%).

Figures for Pension funds 2009-2013

	2009	2010	2011	2012	2013
Coverage ratio (real terms)	81	80	73	76	82
Nominal coverage ratio	109	107	98	102	110
Assets under management (EUR billion)	667	747	803	916	952
Number of pension funds	579	514	454	414	382

Combined with structural factors that affect the financial position of pension funds (increasing ageing process and decreasing ratio between working and retired population), there is a need to change the current structure of the pension system. In the short term, legislative changes will be proposed (planned for 1 January 2015) to make the system more stable, transparent and resilient to shocks. In the long run, a more fundamental review of the pension system in the Netherlands is necessary.

Other major regulatory reforms

The CRR/CRD IV Implementation Act was recently adopted by the Lower House of Parliament, and will enter into force once adopted by the Upper House. Based on that Act, DNB has announced that it intends to impose an additional capital buffer requirement on the four systemic banks in the Netherlands. This systemic buffer will be 3% of risk-weighted assets for ING Bank, Rabobank and ABN AMRO Bank, and 1% for SNS Bank. These buffers will be phased in between 2016 and 2019.

In addition to the implementation of CRR/CRD IV and the required increase in capital and liquidity ratios, developments in the banking sector are influenced by the creation of the European banking union. This will be an important shift in the supervision of the largest Dutch banks, where prime responsibility will be transferred to the ECB. Together with the SSM, the agreement on the BRRD and the SRM constitute an important pillar for effective European supervision and resolution.

In August 2013, a policy paper on the Dutch banking sector was published, approved by the cabinet at the proposal of the Finance Minister. The paper also responded to the recommendations by the Wijffels Committee and made a number of policy proposals, which are now being put in place (see section 2).

For insurance companies, the most important reform will be the introduction of Solvency II (expected 1 January 2016), which is expected to strengthen the solvency position and risk management within the sector. This will have to be implemented within an unfavorable economic environment, where a decreasing market share for life insurance products will put pressure on further consolidation in the sector.

For the pension sector, the government has announced that, alongside with the proposed short term revision of the Pension Act, a more fundamental review is needed towards a structurally more resilient system that adequately reflects changes in social preferences, labor market and economic developments. The future design of the pension sector will be a major source for discussion in the upcoming years.

Annex 2: Nationalisation of SNS REAAL[60]

Background

Expansion and Impairment

SNS REAAL is a Dutch financial institution created through the 1997 merger of SNS banking group and the insurance company REAAL. By the time of its nationalisation in 2013, it had grown to approximately €134 billion in total consolidated assets. SNS Bank was the fourth largest bank in the Netherlands with approximately 1.6 million savings accounts and about 1 million payment accounts, together totalling about €36.4 billion in deposits. REAAL was the second largest life insurance company and the fifth largest non-life insurance company in the Netherlands. SNS REAAL had approximately 6,700 employees and focused primarily on the private individual market and SMEs.

In the years leading up to the financial crisis, SNS REAAL pursued an ambitious growth strategy that was spurred by an initial public offering in 2006. Shortly thereafter, SNS REAAL completed three major acquisitions, including the takeover of Bouwfonds Property Finance (subsequently renamed SNS Property Finance) from ABN AMRO. During the 2008 financial crisis, SNS REAAL filed a request with the government for €750 million in capital aid. The aid was provided because of concerns about the solvency position of the insurance company REAAL at the time and possible contagion effects to SNS Bank. The aid was in the form of special equity-like instruments, and it provided the government with two supervisory board seats and veto rights on management remuneration.

The main driver of adverse developments after 2008 was increasing losses at SNS Property Finance. The size, character, and concentration of the CRE portfolio made SNS REAAL particularly vulnerable to the effects of the financial crisis. At the moment of nationalisation, the outstanding book value of SNS Property Finance's real estate portfolio amounted to about €8.55 billion, the majority of which (77%) related to properties in the Netherlands. The real estate portfolio was large relative to SNS Bank's €82.3 billion in total assets, and had a higher risk profile than the other banks' real estate portfolios due to higher non-performing loans and types of CRE exposures.

With the commercial property markets (internationally and in the Netherlands) rapidly deteriorating, SNS Bank faced high losses on its Property Finance real estate portfolio. Consequently, the solvency of SNS Bank came under pressure at a time when capital requirements were undergoing substantial tightening due to the crisis. The profits of SNS REAAL were insufficient to absorb the real estate losses and strengthen its capital buffers.

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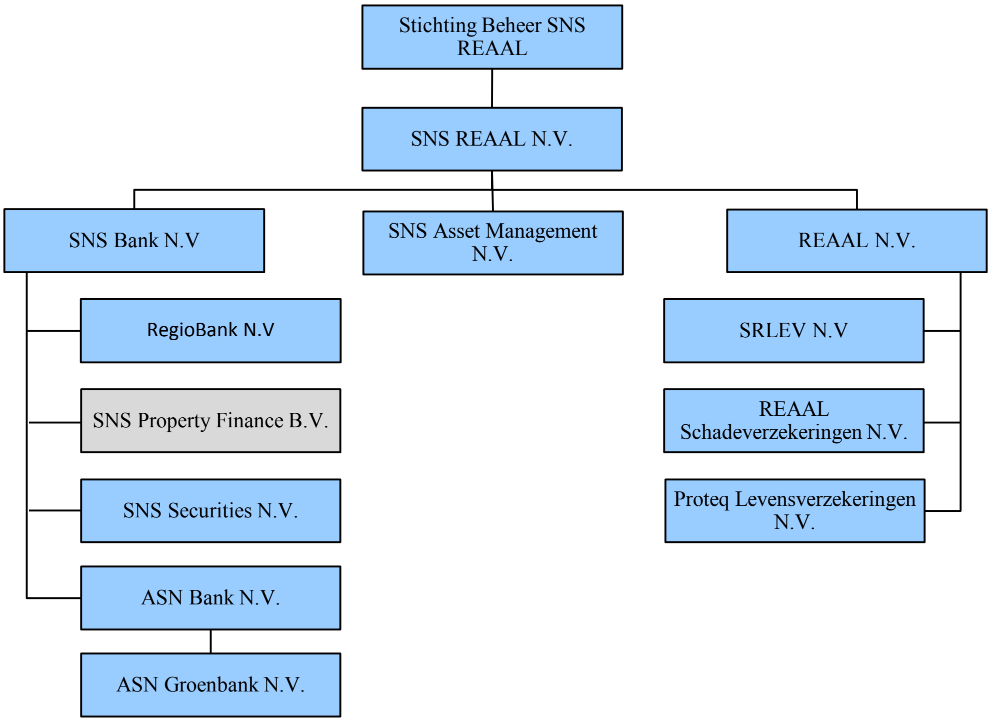
60 Based on information provided by the Dutch authorities.

Simplified Organizational Structure of SNS REAAL



Source: Ministry of Finance.

Supervisory actions and resolution planning

From 2008 onward, DNB and SNS REAAL kept the MoF informed of the situation at the company. Between 2008 and late 2011, DNB intensified its supervisory efforts to strengthen the financial position of SNS Bank, primarily by urging SNS REAAL to reduce its exposure to real estate. Beginning in 2009, DNB worked under the premise that no core capital could leave the bank before the risk exposure in the CRE portfolios was considerably reduced. Also, DNB requested that the firm draw up exit plans for the international real estate portfolio showing how, when, and at what loss this portfolio could be wound down. In mid-2011, DNB repeated its request, this time in regard to phasing-out the entire non-core real estate portfolio. In 2011, DNB also asked SNS REAAL to formulate an action plan for the repayment of the government aid and for addressing vulnerabilities that DNB had identified. When this proved inadequate, DNB requested an additional action plan. Although significant wind-down of the portfolio was achieved during this period, it proved insufficient given the ongoing deterioration of the CRE portfolio and lack of possibilities to strengthen the capital base.

In December 2011, DNB came to the conclusion that SNS REAAL could not effectively resolve its financial situation through private means. At that point, DNB and the MoF set up a joint project group to analyse possible scenarios with regard to SNS REAAL and to establish an emergency safety net should the problems escalate and require acute intervention. During 2012, various private, private-public, and public solutions were considered in order to prevent the failure of the institution, including:

- A sale of the insurer (REAAL) to a private entity, which DNB determined would not have provided sufficient relief to the remainder of the group.

- Different variations of private-public transactions, in which the other three Dutch SIBs (ING, Rabobank and ABN AMRO) and the State would participate in the bank or the holding company and isolate the portfolio of Property Finance. Negotiations in pursuit of a public-private solution were complicated by a number of factors, including the difficulty of defining the appropriate structure of a public-private transaction; additional losses in the real estate portfolio identified by Cushman & Wakefield in a new valuation report; and the absence of a guarantee that such a transaction would be consistent with existing acquisition bans and EU state aid rules.
- A transaction with a private-equity party, which ultimately proved not to be a viable solution, was abandoned on 31 January 2013.
- The application of a transfer instrument to SNS Bank based on the Intervention Act. The use of this instrument would have resulted in the undesirable failure of SNS REAAL. Furthermore, there was no interested private buyer to which SNS Bank could have been transferred.

Nationalisation

Proximate Cause of Failure

In late 2012, DNB determined that SNS Bank faced a capital deficit of at least €1.84 billion, which was twice the amount of its core capital at the time. On 24 January 2013, DNB sent a formal notification to the Minister of Finance describing the precarious condition of SNS Bank. After a consultation period, DNB sent a letter to SNS Bank on 27 January 2013 imposing a deadline of 31 January 2013 to meet all capital requirements or else present a final solution that would de facto lead to remedying the identified capital deficit in the short term. SNS REAAL's share price had declined appreciably in the recent past, dropping to below €1 (compared to its introduction price of €17). Its problems had also caused it to be shut out of the capital markets. In the absence of a convincing and final solution for SNS REAAL, which market participants were anticipating, the auditor's statement would be negative or the financial statements would have be compiled on a liquidation basis rather than on a continuing basis, which would likely have led to further and possibly severe deterioration of public confidence.

SNS REAAL's response to the DNB's letter did not offer sufficient certainty that the identified capital deficit could be addressed in the short term. Additionally, the joint DNB-MoF project group that had been working on public-private options determined that none of the options they considered had proved viable. DNB subsequently informed the MoF that it no longer considered it sound for SNS Bank to continue to carry out its banking operations.

Rationale for Use of Intervention Act Powers

In his letter to parliament on the nationalisation of SNS REAAL, the Minister of Finance explained that, due to its large deposit base, DNB considered SNS Bank to be a systemically important institution. Its failure would have triggered immediate and massive recourse to the DGS. Because the DGS in the Netherlands is funded on an *ex post* basis through a levy on the industry, this would have heavily impacted other banks, potentially straining their capital buffers. Additionally, the financial markets continued to be fragile, so the potential bankruptcy of one of the country's largest banks might have undermined confidence in the

Dutch financial system, resulting in the downgrading of other banks and of the Dutch government. Furthermore, over 1 million account holders would have been temporarily prevented from using their payment accounts, which the Minister of Finance stated would have put them in financial difficulty, possibly causing social unrest.

The failure of the holding company, SNS REAAL, was also determined to pose unacceptably high risk to financial stability, as it was so closely intertwined with SNS Bank that the latter would have been unable to function properly without the former. Shared services of crucial importance to the continuity of SNS Bank, including risk management, treasury, information technology, and personnel, were being provided by the holding company. DNB also perceived a contagion risk to confidence in other Dutch financial institutions, whereby the failure of SNS REAAL might have caused market participants to curtail lending to other institutions with a similar profile.

Because the failure of SNS Bank and SNS REAAL had to be avoided, given their systemic status and since, in view of the above deadlines, there was no viable alternative available, there arose a serious and immediate danger to financial stability. On 1 February 2013, having assessed SNS REAAL's situation in close consultation with DNB and the risks its failure posed to the Dutch financial system, the Minister decided to nationalise SNS REAAL under the Intervention Act to safeguard financial stability.

Application of Intervention Act Powers

The intervention consisted of five elements:

1. Expropriation of the shares of SNS REAAL and of subordinated debts of SNS Bank and SNS REAAL and the Core Tier 1 capital securities of the Stichting SNS REAAL.
2. Recapitalisation of SNS REAAL and SNS Bank by the state.
3. Isolation of SNS Property Finance in a real estate management organisation and a guarantee regarding the funding of that management organisation.
4. A bridging loan by the State to SNS REAAL.
5. Imposition of a one-off levy on Dutch banks to finance part of the intervention costs.

International coordination of the SNS REAAL intervention was limited to the discussions and approval process with the European Commission and information of the ECB. The extent and significance of international activities did not require further coordination with other national supervisors in order to carry out the resolution. Foreign supervisors were informed prior to the nationalisation because of potential market effects and the impact of the use of the burden-sharing measures on creditors.

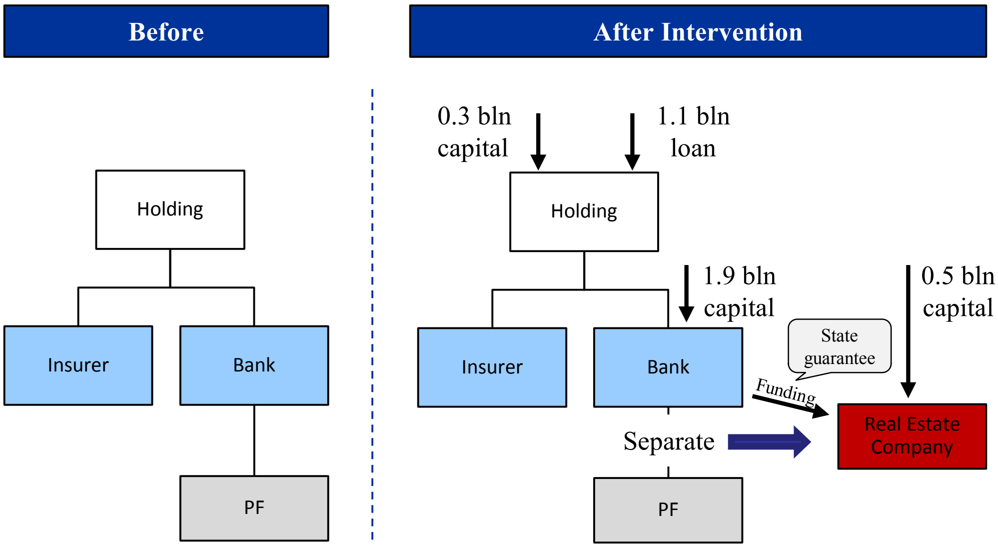
The State incurred costs of €3.7 billion in the nationalisation to stabilise SNS Bank:

- €2.2 billion in new capital injections;
- €0.8 billion to be written off earlier aid; and
- €0.7 billion to isolate the real estate portfolio.

Furthermore, as part of the intervention, the State extended loans totalling €1.1 billion and guarantees worth €5 billion.

A one-off resolution tax of €1 billion to be paid to the Treasury in 2014 was levied on Dutch banks in proportion to each bank's share of the total amount of deposits guaranteed by DGS on 1 February 2013. The Minister reasoned that the banks would have suffered severe consequences if SNS Bank had failed. The levy is not tax deductible.[61]

Structure of SNS REAAL Before and After Intervention



Source: Ministry of Finance.

In conjunction with the nationalisation, the Chief Executive Officer and Chief Risk Officer of SNS REAAL were replaced. The Chair of the Supervisory Board resigned and his duties were assumed by the Deputy Chair.

Impact on Creditors

Council of State—Appeal of the Decree

The nationalisation eliminated all shareholder value and all subordinated debt-holder value, which amounted to losses of around €240 million and €1.67 billion respectively. Fitch Ratings noted that the decision to have junior bondholders take a full loss was one of the harshest impositions on this asset class at a rated bank since the onset of the Euro area crisis. Senior bondholders were left unaffected due to the risk that haircutting them would have a material negative impact on the cost and stability of funding provided to other Dutch banks.

Hundreds of claimants lodged appeals seeking reversal of the decree with the Administrative Jurisdiction Division of the Dutch Council of State. They argued the problems at SNS REAAL did not pose an immediate threat to financial stability and that state intervention represented a violation of civil rights.

[61] See "State of Netherlands nationalizes SNS" by the Ministry of Finance (1 Feb 2013, (http://www.government.nl/news/2013/02/01/state-of-the-netherlands-nationalises-sns-reaal.html).

On 25 February 2013, the Council of State decided that the Minister was entitled to expropriate the securities and subordinated private loans of SNS REAAL and SNS Bank, but not the future claims. Therefore, any such claims can still be made against SNS REAAL or SNS Bank.[62] A number of stakeholders have referred the appeal procedure at the Council of State to the European Court of Human Rights (ECHR) for review.

Enterprise Chamber—Appeal of the Level of Compensation

The expropriated parties have a right to compensation by the State, comprising full reimbursement of the damage that they incur as a direct and necessary result of losing their securities and subordinated private loans. The Enterprise Chamber of the Amsterdam Court of Appeal establishes the level of compensation. The Minister refused to pay shareholders and subordinated debt-holders any damages, arguing that if he had not stepped in, SNS REAAL would have gone bankrupt and investors would not have received any value. Hence, the Minister's offer of compensation was €0. Various claimants appealed the Minister's offer to the Enterprise Chamber.

On 11 July 2013, the Enterprise Chamber issued an interim ruling stating that the Minister had not convincingly argued that €0 represented full compensation and appointed experts to advise on the proper value of the expropriated securities at the moment immediately before nationalisation. On 9 October 2013, the State lodged an appeal against this ruling, in part because this was the first time that the Intervention Act had been applied and the State wanted the Supreme Court to rule on how certain aspects of the law should be interpreted before the assessment by experts, as recommended by the Enterprise Chamber, got underway. It is not yet known when the Supreme Court will issue its ruling. In the event that the Enterprise Chamber rules that compensation is due, the State will have to pay the shareholders and subordinated debt-holders accordingly.

Unrelated to the proceeding before the Enterprise Chamber, the Minister requested shortly after the nationalisation that SNS REAAL conduct a fact-finding investigation to ascertain whether there had been any irregularities in the offer or advice concerning third series participation certificates of SNS Bank seized during the nationalisation. Based on the investigation, and before the Enterprise Chamber ruled, SNS Bank offered to pay €53 million to holders of the participation certificates on 11 July 2013. SNS REAAL stated that it did not properly inform investors of the risks associated with buying these securities, which were sold in June 2003. At the time of the publication of SNS REAAL's 2013 annual report, 97% of clients had accepted the offer.

Review and Evaluation

Evaluation Commission—Review of the Actions of DNB and MoF

On 5 March 2013, the Minister of Finance announced an inquiry into the actions of DNB and the MoF and the interaction between them with regard to SNS REAAL. An inquiry

[62] See "Dutch Minister of Finance makes offer for compensation due to the nationalisation of SNS REAAL" by the Ministry of Finance (4 March 2013, http://www.government.nl/news/2013/03/04/dutch-minister-of-finance-makes-offer-for-compensation-due-to-the-nationalisation-of-sns-reaal.html).

Commission was set up, which heard experts and key persons (e.g. former Executive and Supervisory Board members of SNS REAAL) and inspected documents of MoF, DNB and SNS REAAL. Its report was published on 23 January 2014.[63]

The report concluded that DNB, as the supervisory authority, was insufficiently alert to the risks of SNS REAAL's strategy of expansion and takeovers in the period between 2006 and 2009. The expansion weakened the buffers of SNS REAAL and raised the risk profile of the banking and insurance businesses.

In late 2008, SNS REAAL had to appeal to the MoF for state aid. In the view of the Evaluation Commission, the MoF failed to act on its responsibility to make a clean sweep at SNS REAAL at the time aid was provided. The state aid did not mark the start of a radical restructuring of SNS REAAL, such as resolving the bottlenecks in the mutual financing arrangements between the parent company of SNS Bank and REAAL. At the same time, SNS REAAL became caught up in the problems at Property Finance, the CRE loans portfolio that weighed heavily on the balance sheet of SNS Bank. From late 2008 to late 2011, responsibility for a radical and imperative restructuring was primarily placed with the management board and the supervisory board of SNS REAAL.

When it became apparent to DNB in late 2011 that SNS REAAL had insurmountable problems, the supervisory authority and MoF opted for a more active stance, but the Evaluation Commission was critical of the fact that it took more than a year before the ultimate solution of nationalisation was achieved. Sale or divestment of parts of SNS REAAL might have been a possibility in 2009, but in 2012 it was no longer feasible. Only in the second half of 2012 did the MoF gradually take charge. The MoF informally contacted the EC, which was too late in the opinion of the Evaluation Commission. The MoF insisted that the financial sector should make a substantial contribution to a solution. This ultimately took the form of a €1 billion levy, to be borne by a not particularly strong banking sector.

The Evaluation Commission made *inter alia* the following recommendations:

- The Minister of Finance should set clearer terms for state aid and appoint a trustee to supervise stricter compliance with the requirements attached to state aid. This is instead of state-appointed supervisory board members, who are in an impossible position and who proved ineffective in safeguarding the public interest.
- DNB should choose a clearer governing structure that places ultimate responsibility with its president. That responsibility should include public accountability for the supervision of financial institutions, alongside her or his other tasks.
- Create an explicit legal basis for the establishment of "living wills" by all financial institutions aimed at, among other things, dealing with complex interdependencies.
- The scope of DNB's resolution powers should be extended to financial holding companies.

[63] See "Nationalisation of SNS REAAL unavoidable in the absence of viable alternatives" by the Ministry of Finance (23 January 2014, http://www.government.nl/news/2014/01/23/nationalisation-sns-reaal-unavoidable-in-the-absence-of-viable-alternatives.html).

European Commission—Temporary and Final Decisions

In its decision of 22 February 2013, the EC granted temporary approval for the capital injection of €2.2 billion in SNS REAAL, €1.9 billion of which was to be passed through to SNS Bank, and the bridge loan issued by the State to SNS REAAL in the amount of €1.1 billion. Final approval was granted on 19 December 2013, based on the restructuring plan submitted by the MoF on 19 August 2013.

In line with the restructuring plan submitted, the State committed to two structural measures regarding the balance sheet of SNS REAAL:

- Separation of the Property Finance activities into a bad bank that will gradually wind down the portfolio; and
- Divestment of the insurance subsidiary REAAL, which includes all insurance and asset management activities of SNS REAAL.

The transfer of the Property Finance shares to the State took place on 31 December 2013. The separation of the Property Finance activities resulted in a substantial reduction of risk-weighted assets and is an important measure to further restore viability of SNS REAAL. It should also have the effect of facilitating access to capital market funding for SNS Bank.

SNS REAAL committed to the divestment of the insurance subsidiary REAAL. The State and SNS REAAL committed to use the future proceeds of the divestment of REAAL to reduce the double leverage on the balance sheet of SNS REAAL. The holding company SNS REAAL will be wound down. The entity resulting from the restructuring will be a standalone bank focused on banking for retail and self-employed clients. The State has committed to privatising SNS Bank in due course.

The decision of 22 February 2013 stipulated, among other things, that until the final decision, SNS REAAL was not permitted to carry out any acquisitions (acquisition ban) or make payments on hybrid instruments (hybrid debt call and coupon ban). In its final decision of 19 December 2013, the EC set a number of conditions and restrictions that, unless otherwise stated, will apply until the end of the restructuring period in December 2017. The principal conditions and restrictions among others are:

- An acquisition ban will apply for a period of three years starting from the date of the EC decision;
- SNS REAAL will not advertise the fact that it is State-owned or make any reference to any State support received in its communications with existing or potential customers or investors;
- SNS REAAL will refrain from making any payments on the hybrid debt instruments outstanding at the time of the EC decision, unless those payments stem from a legal obligation, and will not call or buy back those instruments without prior EC approval;
- Restrictions apply to the remuneration of employees and senior management until the end of the restructuring period or until SNS REAAL has repaid the state aid;
- SNS REAAL commits to transfer the administrative structure currently borne by the holding company to the bank and the insurance company; and

- SNS REAAL commits to the phasing out of any financial interdependence between the banking and the insurance activities.

In 2014, SNS REAAL set in motion the process to sell the insurer REAAL, in line with the EC agreement. The Minister will mandate that NL Financial Investments, which exercises shareholders' rights in SNS REAAL on behalf of the State, start and execute the REAAL sale process. REAAL will be sold by means of a controlled auction, as indicated in the letter to the House of Representatives of December 2013.[64]

[64] See "REAAL sale process to start this summer" by the Ministry of Finance (6 June 2014, http://www.government.nl/news/2014/06/10/reaal-sale-process-to-start-this-summer.html).

Annex 3: Follow-up of other key FSAP recommendations

This Annex presents the follow-up actions reported by the Dutch authorities to key FSAP recommendations that are not covered in sections 2 and 3. The actions mentioned below have not been evaluated as part of the peer review and are presented solely for purposes of transparency and completeness.

Recommendations	*Steps taken to date and actions planned (including timeframes)*
Twin Peaks	
Provide the DNB and AFM greater discretion to put in place enforceable rules. The lack of sufficient rule making authority leads to ad hoc approaches that risk becoming arbitrary and subject to legal challenge.	DNB and AFM derive their rule making authority, from regulation that is determined by government (parliament). Within their mandate, DNB and the AFM have operational independence to set rules to effectively fulfil their legal tasks. This is supported by different possibilities for enforcement on the basis of the Act on Financial Supervision. Increasingly, supervisory rules are determined by directly applicable European regulation (CRR or binding technical standards by EBA) based on maximum harmonisation. There is a well-structured and transparent process if DNB or AFM are of the opinion that regulation is not sufficient and additional rules or powers are needed. In addition to regular, top-level discussions with the Ministry of Finance (as prime responsible legislator), DNB and AFM each year send a letter, which is made public, in which DNB and AFM express their proposals for legislative changes that are deemed necessary for the conduct of their supervision. The Minister responds to these requests in a letter to Parliament (see latest version in link below). http://www.rijksoverheid.nl/documenten-en-publicaties/kamerstukken/2013/07/08/wetgevingsbrief-financiele-markten.html
Afford legal protection to DNB and the AFM as institutions, for their official actions, except in cases of gross negligence or wilful misconduct, in line with practice in many neighbouring countries.	Since 1 July 2012, new legislation is in force to limit the liability of DNB and the AFM. http://www.eerstekamer.nl/wetsvoorstel/33058_wet
Continue integration of DNB staff across banking, insurance, and pensions functions, so as to draw the synergies of having a single regulator.	A new organisational structure has been implemented with the creation of a cross-sectional Division that contains expertise centres for specific elements of supervision. In addition, a separate risk management department has been created to strengthen internal procedures and risk management. In addition, the governance of the Board has been changed,

	effective 16 February 2012, to emphasize the different responsibilities of DNB with the President responsible for central bank tasks and a Chairman of Supervision, primarily responsible for prudential supervision. http://www.dnb.nl/en/about-dnb/organisation/governance/index.jsp This is supported by the creation of a Supervisory Council, where all relevant supervisory issues are discussed. The Supervisory Council is chaired by the Chairman of supervision, and contains all Division Directors from the different supervisory Divisions. The new Board of Directors of DNB has also renewed the Mission Statement of DNB (project Polaris). One of the pillars that have been identified is to strengthen synergy within DNB. This is further developed in an internal project with proposals to assign cross-sectoral responsibilities to one responsible Division Director. For example, Division Directors have been given a coordinating role in the most important cross-sectoral policy themes. Also, several initiatives have been set-up to promote job-shifting between Divisions.
Microprudential bank and insurance supervision	
Establish routine reporting requirements to strengthen monitoring and risk modelling.	An internal project (Cesar) has been set up to strengthen data management within DNB. The Ministry of Finance has introduced a draft legislative proposal to strengthen the powers of DNB to collect and use data needed to fulfil its task of financial stability http://www.internetconsultatie.nl/uitvoeringsbesluitbankwet1998
Intensify supervision of large international financial institutions, with greater emphasis on group supervision and soundness of business models. Greater international cooperation, beyond participation in colleges of supervisors, is warranted.	With the creation of the banking union, the primary responsibility for the large, significant institutions will be transferred to the ECB. It is expected, that this will intensify supervision (as evidenced by the intensive comprehensive assessment that is currently conducted) In addition, DNB will continue to fulfil its role in supervision. Every four years, DNB publishes its Vision on Supervision, which sets out the strategic orientation of DNB for the upcoming years. In the Vision 2010-2014, DNB announced a shift in the focus of its supervision, by i) looking beyond individual institutions and intensifying the macro-approach of supervision and by ii) explicitly including business models & strategy and behaviour & culture into their supervisory strategy and a more . http://www.dnb.nl/en/binaries/DNB%20Supervisory%20Strategy%202010-2014_tcm47-238092.pdf Recently, the Vision for 2014-2018, was published which concluded that these elements have now become integral part of the supervision of DNB. In 2012, a new supervisory approach was introduced (“Focus!”) reflecting the reorientation of the supervision of DNB. Focus! internalizes the broader scope of supervision and encompasses

	qualitative elements of supervision, with the inclusion of two separate risk drivers: i) business models and strategy and ii) behaviour, culture and governance. The new supervisory approach makes more use of a risk based approach through ex-ante classification. It also includes a multi-disciplined and sector wide approach by strengthening the macro-orientation and thematic supervision. http://www.toezicht.dnb.nl/en/4/2/14/51-225810.jsp In recent years, specific attention has been paid to intensify group supervision. In addition, the financial stability Division has developed recovery and resolution plans, to better manage the resolvability of large international groups.
Adopt more proactive and decisive approach, including timely off-site inspection and corrective actions that rely less on moral suasion.	In August 2010, an Action Plan was announced to make supervision of DNB more comprehensive and intrusive. http://www.dnb.nl/en/binaries/From%20Analysis%20to%20Action_tcm47-239499.pdf The identified actions were supported by a change in the organisation of DNB, including – inter alia – the creation of a separate intervention department to intervene timely and effectively when needed. This department coordinates the supervisory approach of troubled institutions and advises on the use of formal measures. In addition, a dedicated risk management department has been set-up to strengthen internal control within DNB.
Securities market	
Strengthen the AFM's ability to enforce issuers' compliance with financial reporting standards.	The AFM's ability to enforce issuers' compliance with financial reporting standards has been strengthened by amendments to the Act on financial reporting by i) removing the limitations faced by the AFM when requesting information from issuers in order to assess the accuracy of their financial statements (effective 1 January 2014) ii) removing the Chinese walls preventing the sharing of information between the departments of the AFM (effective 1 January 2013).
Strengthen the regulatory and supervisory framework for management companies of collective investment schemes (CIS).	In July 2011 the European Alternative Investment Fund Managers Directive (AIFMD) was published which covers among others these aspects. This directive has been implemented in Dutch legislation and has become effective as of 22 July 2013.
Pensions	
Develop a communication plan on recent and prospective changes in pay-outs to stakeholders.	The responsibility for communication lies with the funds themselves. In addition and in close collaboration with the Federation of the Dutch Pension Funds and the Ministry of Social Affairs and Employment, DNB has set up communication about the number of funds that need to lower their entitlements.

	http://www.dnb.nl/nieuws/nieuwsoverzicht-en-archief/nieuws-2013/dnb285723.jsp New legislation for pension funds is under development and draft legislation has recently been proposed by the government (April 2014). DNB works closely with the Ministry of Social Affairs to implement new legislation to make the pension system more transparent and resilient. Together with the new draft legislation, the Ministry of Social Affairs has announced that it will start a broad public debate about a fundamental review of our pension system. DNB supports this decision, which will make people more aware of the nature, entitlements and risks of their pension contract.
Require incorporation of professional Board members for pension funds beyond a minimum size, and provide legal authority that allows direct supervision of core pension.	In 2013, new legislation has been introduced to strengthen the governance of pension funds. Key element is the reinforcement of countervailing powers in the governance structure and improving quality, including the possibility to create seats for professional board members. http://www.eerstekamer.nl/9370000/1/j9vvhwtbnzpbzzc/vjbgbnrjbpz4/f=y.pdf DNB already has - through the board of the fund - powers to supervise all core pension activities, even if outsourced (core responsibilities can never be outsourced).