The Banking Regulation Review

Tenth Edition

Editor
Jan Putnis

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THE BANKING REGULATION REVIEW

TENTH EDITION

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PREFACE

Banking regulation continues to confound the idea that views about how banks should be regulated will eventually settle down to an orthodoxy broadly accepted throughout the world.

Few global banking groups ever considered that a time would come when they would face consistent systems of regulation across the world, and still less that regulators would coordinate their activities in a way that would make life easy for those groups. Legal and compliance professionals who have worked in or with the industry since long before the financial crisis of 2007 to 2009 are generally not surprised by the examples of banking regulation diverging in many jurisdictions: in some ways it marks a return to a time when there can be no certainty that governments and regulators are all facing the same way and pulling in the same direction.

Running a global banking group continues to be a tough exercise, and the possibility of further fragmentation of approaches to regulation around the world risks adding further to the cost bases of these groups. As predicted since the UK electorate voted to leave the European Union in 2016, Europe in particular looks set to become a less cost-efficient and more complex place in which to run a cross-border banking franchise. Indeed this is already the case for the banking groups that have largely completed their Brexit reorganisations, establishing or expanding EU subsidiaries. While this has stimulated banking groups to consider cost cutting and other efficiency measures in connection with their Brexit planning, in many cases these measures scarcely compensate for the inherent inefficiency of requiring additional licensed legal entities through which to conduct business in Europe.

Aside from the largely regional challenge of Brexit, this tenth edition of *The Banking Regulation Review* is published in the midst of a number of industry developments that are challenging regulators and banks alike in all major banking centres.

The challenges are far-reaching and have no central theme, ranging from the continuing revolution in finance stimulated by emerging technologies and the related exploitation of the value of data on the one hand, to the continual revelations of the widespread use of banks for money laundering on the other.

While it is too early to say that the remarkable global consensus that emerged about prudential regulation following the financial crisis is fracturing, it is certainly eroding around the edges, with liberalising tendencies in the United States and even in the European Union.

All of these factors make work as a legal, compliance or risk professional in the sector both more interesting and more perilous than ever before: more interesting because there is so much going on, and more perilous because there seems to be more that can go wrong within banks nowadays, from misallocation of capital to business units that struggle, to whistleblowing and money laundering problems, to catastrophic IT outages.

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Money laundering issues have been particularly prominent in banking in the past year, suggesting that the industry still has a long way to go to tackle this problem. Many of the issues uncovered are legacy in nature, but the industry has much to do to convince regulators and governments that those issues will not recur.

IT problems have led to an increasingly intense debate about what can be done to improve the operational resilience of banks. This is not simply a continuation of the somewhat sterile debate about the incompatibility of many legacy banking IT systems with attempts to modernise risk management and the customer experience. Regulators have realised that operational resilience is a subject that can only be tackled effectively by making two significant changes to the way that this subject has traditionally been viewed. First, operational resilience should be considered in a holistic way, looking not only at banks' own systems but also across the whole of the financial sector at the resilience of the inter-connections between banks, financial market infrastructure and other market participants. Secondly, work on operational resilience achieves little unless it is considered with customers and other end users of services in mind. The resilience of a bank's systems is not a meaningful concept unless it delivers an acceptable level of service to customers and incorporates tolerances for the levels of inconvenience that customers may suffer in the event of extreme disruption, recognising that disruption could originate outside the bank itself.

More immediately, IT challenges in banks expose the need for effective crisis management capabilities. Recovery and resolution planning has helped some banks to develop this expertise, but has been less helpful in this respect than might have been hoped. There is no substitute for more detailed planning for crises than many banks have so far included in their recovery planning. Those who disagree with this view should consider how many banks have performed poorly when crises have hit them, and how many of those banks would have argued beforehand that their systems were adequate to cope with a range of foreseeable adverse scenarios.

Conduct risk remains high up the agenda of most banks. The final report of the Royal Commission into misconduct in the banking, superannuation and financial services industry in Australia was notable outside that country for the familiarity of almost all of its findings. Whatever the ultimate legislative and regulatory response to that report, it is a reminder that banking remains vulnerable to poor conduct unless senior management make good conduct a cornerstone of their strategy and ensure that it is embedded in the incentive arrangements for all staff who have a material influence on customer outcomes.

This edition covers 37 countries and territories in addition to our usual chapters on international initiatives and the European Union. Thanks are due to all of the authors who continue to devote time to this project despite busy schedules. There must be a feeling among many of the authors that banking regulation is a subject that will never settle down; that it will never return to being the rather duller subject that it was before it became a political issue more than 10 years ago.

Thank you also to the partners and staff of Slaughter and May in London and Hong Kong for supporting this book, and in particular to Nick Bonsall, Ben Kingsley, Peter Lake, Emily Bradley, Tolek Petch, Jocelyn Poon, Tamara Raoufi and David Shone.

Finally, the team at Law Business Research deserve as much credit for their patience this year as for their usual work as the publishers of this book. Thank you in particular to Gavin Jordan and Katie Hodgetts. The uncertainties that Brexit has thrown up have left a number of authors wondering what the best time to publish would be, before the realisation dawned that Brexit is likely to be a more protracted process than many envisaged and that therefore

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no one publication date would be better than any other. The other issues noted above look set to run in some form indefinitely.

Perhaps by the time the next edition of this book is published, all will be much clearer, but those of us who are endlessly fascinated by the subject of banking regulation know all too well just how unlikely that is.

Jan Putnis
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Chapter 28

NORWAY

Richard Sjøqvist, Markus Nilssen and Steffen Rogstad[1]

I INTRODUCTION

The Norwegian banking industry has developed in cycles during the past 200 years. From a minimal start, the number of banks increased rapidly until nearly each small municipality had at least one bank. During the recession in the late 1920s, many banks had to close but subsequently reopened. In the 1930s there were around 700 banks in Norway, of which 630 were savings banks. This continued until around 1970, when a rapid consolidation started. Today, there are 126 banks incorporated in Norway: around 100 of them are savings banks, while the rest are commercial banks. This includes subsidiaries (but not branches) of foreign banks. Around 40 credit institutions have opened branches in Norway; however, only a few operate as full-service banks, and many specialise in equipment financing, typically automobiles. Many credit institutions from EEA Member States have provided notification in respect of cross-border services; however, probably only a minority of them regularly provide services in Norway.

The Norwegian banking industry is dominated by two large commercial banks (DNB Bank ASA and Nordea Bank ABP) and two groups of independent savings banks (Eika group and SpareBank 1 group). Each savings bank operates independently, but both Eika Group and SpareBank 1 Group have certain joint operations and a common brand. Foreign banks, through branches or cross-border activities, are active, and hold a significant market share of business within the shipping, oil, or offshore and mainland industries.

The five largest banks in the Norwegian market (excluding those owned by a public body) measured by balance sheet value are:

a DNB Bank ASA;
b Nordea Bank ABP, Filial i Norge (a branch of Nordea Bank ABP);
c Danske Bank (Norge) (a branch of Danske Bank A/S);
d Handelsbanken, (a branch of Svenska Handelsbanken AB (publ)); and
e SpareBank 1 SR-Bank ASA.

1 Richard Sjøqvist and Markus Nilssen are partners and Steffen Rogstad is a senior associate at Advokatfirmaet BAHR AS.

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II THE REGULATORY REGIME APPLICABLE TO BANKS

i General

Norway is not a member of the European Union, but through the EEA agreement, it is committed to implementing the relevant directives for the finance industry. This means that the free establishment rule applies for EEA institutions wishing to provide services in Norway, and for Norwegian institutions wishing to offer their services within the EEA.

The combination of accepting deposits and providing credit triggers a requirement for a banking licence under Norwegian law. The main regulation applicable to banks can be found in the Act on Financial Undertakings and Financial Groups 2015 (Financial Undertakings Act). The Financial Undertakings Act is an attempt to consolidate the main financial regulations, which were previously scattered in various pieces of legislation, into one comprehensive act (implementing, inter alia, the key elements of the Capital Requirements Directive (CRD IV) and the Capital Requirements Regulation (CRR)). The Act regulates the following financial undertakings:

a banks and other credit institutions;
b finance companies;
c holding companies in financial groups;
d payment institutions;
e electronic money institutions; and
f insurance and pension institutions (not discussed in this chapter).

Banks providing investment services or investment fund services are also subject to the Securities Trading Act 2007 (implementing, inter alia, the Markets in Financial Instruments Directive (MiFID II)) or the Investment Fund Act 2011 (implementing, inter alia, the Undertakings for Collective Investments in Transferable Securities Directives).

A new Anti-Money Laundering Act was enacted with effect from 15 October 2018. The new Act and regulations have provided that the key parts of Norwegian legislation are assumed to be in compliance with the EU's fourth Anti-Money Laundering Directive and the Financial Action Task Force Recommendations.

A widely discussed subject related to this area is trade with cryptocurrencies. There has been little clarification concerning how the anti-money laundering and anti-terror financing regulations will affect this trade. This has already led to some insecurity and conflicts between financial institutions and clients that are trading such currencies. The new Norwegian legislation is aiming to address this, in particular by imposing a duty to notify the FSA before conducting such business, and that providers are subject to supervision by the FSA. The legislation is implementing the fifth Anti-Money Laundering Directive in this respect.

Finally, all financial undertakings are subject to the Financial Supervision Act 1956.

The main regulator is the Financial Supervisory Authority of Norway (FSAN). The FSAN's resources come from fees paid by the institutions it supervises. Its main purpose is to promote financial stability and a well-functioning market.

The FSAN's instruments are:

a supervision and monitoring;
b licensing;
c regulatory development; and
d information and communication.

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ii Deposit taking

Norwegian financial undertakings that wish to take deposits from the public must have a licence as a bank. Non-banking credit institutions may receive repayable funds from the public (other than deposits) by way of the issue of bonds or other comparable securities. EEA credit institutions providing services in Norway based on their home state licence (passporting) may take deposits in Norway if their home state licence allows them to do so.

iii Lending

Lending is a regulated activity, and a licence or a passport is needed. Norwegian financial undertakings without a banking licence may grant loans based on a licence as a non-banking credit institution or as a finance company, and will normally fund themselves in the bond market. Typical today are mortgage credit institutions operating in the covered bond market. These are normally owned by banks or savings bank groups, and acquire loan portfolios from the banks.

Investment firms need a separate licence to provide loans in connection with their investment activities.

iv Foreign exchange

Spot foreign exchange trading can be carried out by banks, payment institutions, electronic money institutions and finance companies as well as by foreign passported credit institutions, payment institutions and electronic money institutions, all subject to having an appropriate licence to do so.

Dealings in foreign exchange derivatives can only be carried out by an institution with an investment firm licence.

v Payment services

The Payment Services Directive (PSD1) was fully implemented into the Norwegian legislation in 2010, and the regulations implementing the public law parts of PSD2 will be effective from 1 April 2019. Simultaneously, the Ministry of Finance (MOF) has declared that the Ministry of Justice and Public Security will lay down a regulation implementing the private law parts of the Directive. The time frame for the latter is, however, still uncertain.

vi Investment services

Licences to provide investment services may be granted to banks and limited liability companies.

Banks may obtain licences in their own names or through their subsidiaries. Foreign passported firms may also provide investment services in Norway; see further below.

vii Legal structure of banks

There are two legal structures of banks available: commercial and savings.

Commercial banks have to be organised either as public limited liability companies or private limited liability companies. Pursuant to the Financial Undertakings Act, banks established after 1 January 2016 must be organised as public limited liability companies; however, those established as subsidiaries in a financial group may be organised as private limited liability companies.

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Savings banks were originally organised as independent entities without external owners. Hence, their equity capital historically consisted mainly of retained profits from earlier years. Since 1987, savings banks have been entitled to bring in external equity by issuing equity instruments, called equity certificates. These differ from shares in that they do not give holders ownership of a bank's entire equity capital. Moreover, holders have limited voting rights to a maximum of two-fifths in total in the bank's highest body, the general meeting. Around 30 savings banks, including several of the largest ones, have issued such instruments.

All banks must have a total of share capital and other equity capital of at least €5 million.

viii Branches and cross-border services

Foreign banks established within the EEA may establish branches in Norway in accordance with the EU or EEA banking directives. The prime regulator of a foreign branch is its home state regulator, but branches of foreign banks are also regulated by Norwegian rules to a certain extent, pursuant to, inter alia, the Financial Undertakings Act, and supervised by the FSAN pursuant to, inter alia, Regulation No. 1257 of 28 December 1993.

Foreign banks established within the EEA may also provide cross-border services in Norway pursuant to EU or EEA passporting rules. Foreign banks providing cross-border services in Norway are to a lesser degree regulated and supervised by the FSAN.

Banks established outside the EEA must have a Norwegian licence to provide banking services in Norway through a branch. A licence to provide cross-border services is not available for such entities.

III PRUDENTIAL REGULATION

i Relationship with the prudential regulator

Entities under supervision file various reports with the FSAN on which it may comment or raise questions. Communication between the FSAN and an entity under supervision will normally be in the form of written correspondence. The FSAN also has the power to give specific directives to an institution, but this is rarely done, as the supervised entities will normally follow the FSAN's guidance. The FSAN bases its supervision and monitoring of the market on global standards.

From time to time, the FSAN will conduct a physical inspection of a bank, normally with a couple of weeks' notice. The object of such inspection varies, but an evaluation of the bank's ability to monitor risks will normally be a main area of interest, as will money laundering routines. The FSAN divides risks into four categories: credit, market, liquidity and operational.

The instruments available to the FSAN are listed in Section II. The main purpose of the FSAN, according to its strategy document for the period from 2019 to 2022, are to promote and secure financial stability and a well-functioning market through six sub-goals:

a solid and liquid finance institutions;
b robust infrastructure;
c investor protection;
d consumer protection through good information and advice;
e efficient crisis management; and
f prevention of economic crime.

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In its strategy, the FSAN has identified the following supervisory priorities:

a macroeconomic supervision;

b solvency supervision of financial institutions;

c supervision of the distribution of loans and trading of pension savings schemes, collective investment vehicles and other financial instruments;

d supervision of financial infrastructure, payment, trade and settlements systems; and

e supervision of compliance with the money laundering regulations.

ii Management of banks

The promulgation of the Financial Undertakings Act implies a modernisation and coordination of the corporate governance requirements of banks, which, inter alia, means that the Norwegian requirements are brought in line with international developments. As a result, certain previously required management structures, such as a committee of representatives and a control committee, are no longer required.

Commercial banks are organised either as public limited liability companies or, if established prior to 2016, as private limited liability companies, and are as such required to have a board of directors and a chief executive officer (CEO). Note, however, that a bank established as a subsidiary in a financial group may still be organised as a private limited liability company.

The general meeting is the highest body of both savings and commercial banks. The general meeting of a commercial bank is governed by the ordinary company laws. In savings banks, at least three-quarters of the members of the general meeting shall be persons who are not employed by the company. The details regarding the election of members to the general meeting in a savings bank shall be set out in the company's articles of association.

Banks with more than 200 employees might have a corporate assembly, if so agreed between the bank and a majority of the employees. The corporate assembly will have tasks such as to elect members of the board of directors and the chair of the board of directors, to supervise the board, the management and the bank's operations, and to decide in cases regarding major investments.

Banks must, as a main rule, have an audit committee, a compensation committee and a risk committee, all consisting of members of the board of directors. The purpose of the audit committee is to support and advise the board of directors with respect to, for example, internal control systems, risk management and auditing of the bank's financial statements. The compensation committee draws up proposals and issues recommendations to the board of directors regarding remuneration, and acts generally in an advisory capacity with respect to remuneration and other important personnel-related matters. The purpose of the risk committee is to support and advise the board in its role as supervisor and governing body of risk and risk control.

In addition, for banks with securities listed on a regulated market in Norway, the Norwegian Code of Practice for Corporate Governance will apply.[2] The Code is based on the comply or explain principle, whereby companies must comply with the Code of Practice or explain why they have chosen an alternative approach.

2 The Code of Practice is issued by the Norwegian Corporate Governance Board: see www.nues.no.

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Banks operating in Norway through a branch are not subject to the regime described above, but must nevertheless register a CEO or similar contact person with the Norwegian Business Register and the FSAN, and may also choose to have a Norwegian board of directors.

If a Norwegian branch or subsidiary of a foreign bank is subject to an internal group approval regime, the extent to which the branch or subsidiary may pass on customer information to other members of its company group will depend on the nature of the information. While Norwegian law does not contain an absolute prohibition against such arrangements, any information sharing will be subject to, inter alia, applicable banking confidentiality and data protection rules. Most foreign banks with a presence in Norway operate through a branch, which enables a more efficient flow of information between the branch and its head office. In addition, since banks are subject to strict rules with respect to risk control and capital requirements on a consolidated basis, there is a legitimate need for reporting. The law has been rather unclear on these questions, but the Financial Undertakings Act does explicitly allow for such sharing of information, as set out in Section IV.

As for remuneration policies and practices, new regulations were brought into effect as of January 2015 based on the CRD IV. In accordance with the Directive, it is not possible to award remuneration on more than 100 per cent of the basic salary. The CRD IV does, however, allow for remuneration of up to 200 per cent in some cases for EU Member States, and the MOF has implemented the same approach. The Norwegian remuneration rules are applicable regardless of the size, nature, scope or complexity of institutions. Accordingly, Norwegian regulations are in some ways stricter than those set out in the CRD IV and the European Banking Authority (EBA) guidelines, which includes, inter alia, the principle of proportionality.

iii Regulatory capital and liquidity

Norwegian banks are subject to ongoing capital adequacy requirements, which implement EU directives based on the Basel III regime. Financial groups are considered on a consolidated basis. In line with the recommendations of the Basel Committee on Banking Supervision, the regulatory approach in the Financial Undertakings Act is divided into three pillars:

a Pillar I – calculation of minimum regulatory capital: banks shall at all times fulfil the own funds' requirements reflecting credit risk, operational risk and market risk. The current requirement is that a bank's own funds shall constitute at least 8 per cent of a calculation basis reflecting such risks. The Common Equity Tier 1 (CET1) capital ratio requirement is at least 4.5 per cent and the Additional Tier 1 capital ratio requirement is at least 6 per cent. Own funds can be in the form of core and supplementary capital. Core capital will typically consist of equity capital, while supplementary capital can be hybrid capital or subordinated loan capital. The capital requirements must be complied with at all times. Banks are obligated to document their fulfilment of the requirements by reporting quarterly to the FSAN;

b Pillar II – assessment of overall capital needs and individual supervisory review: banks must, inter alia, have a process for assessing their overall capital adequacy in relation to their risk profile and a strategy for maintaining their capital levels. The FSAN reviews and evaluates these internal capital adequacy assessments and strategies, and it may take supervisory action if not satisfied with the result of an evaluation process; and

c Pillar III – disclosure of information: banks are required to disclose relevant information regarding their activities, risk profile and capital situation.

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In addition to the minimum capital standards, Norway has adopted the following buffer standards:

a a capital conservation buffer of 2.5 percentage points in addition to the minimum CET1 capital ratio;

b a systemic risk buffer of 3 percentage points in addition to the minimum CET1 capital ratio and capital conservation buffer;

c if the financial undertaking is defined as systematically important, it has a buffer of 2 percentage points in addition to a minimum CET1 capital ratio, capital conservation buffer and systemic risk buffer; and

d a countercyclical capital buffer of 2 percentage points in addition to the CET1 capital ratio, capital conservation buffer, systemic risk buffer and, if applicable, the buffer for systematically important institutions. This buffer will increase to 2.5 percentage points from 31 December 2019.

If a financial undertaking does not meet the buffer standards, it is required to develop a plan on how to increase its CET1 capital ratio, and cannot pay dividends or make bonus payments without approval from the FSAN.

The capital requirements for banks and other financial institutions in Norway are described in detail in Chapter 14 of the Financial Undertakings Act (which implements the capital and liquidity rules in the CRD IV and the CRR). For credit risk and market risk, the calculation basis may be found using either risk weights specified in regulations, or in accordance with internal procedures. Operational risk may be calculated using one of three calculation methods: share of average income (basis method), share of income within each business area multiplied by a loss indicator determined by the MOF (template method) or internal measuring methods (foundation or advanced).

Contrary to EU law, the MOF has decided to maintain the 80 per cent Basel I floor for banks that calculate capital on the basis of internal models. However, the Minister of Finance has indicated that this floor will be removed when the CRD IV and the CRR are incorporated into the EEA agreement, which is expected during 2019.

Since July 2014, all Norwegian banks are required to report their liquidity coverage ratio and net stable funding ratio to the FSAN.

Local branches of banks incorporated outside Norway are not subject to this regime, but are primarily subject to the regime in the jurisdiction of the bank.

iv Recovery and resolution

A Norwegian bank cannot be subject to ordinary insolvency proceedings (e.g., bankruptcy) in the same manner as a Norwegian company or private individual. Instead, banks experiencing financial difficulties will be subject to resolution pursuant to the rules of the Bank Recovery and Resolution Directive (BRRD) as implemented in Chapter 20 of the Financial Undertakings Act. The BRRD was implemented in Norway from 1 January 2019. The FSAN has not yet determined the minimum requirement for own funds and eligible liabilities (MREL) for individual Norwegian banks, but it is expected that this will happen during 2019. The FSAN has indicated that the banks will be granted a reasonable transitional period to fulfil the MREL. It is still unclear how the BRRD2 will affect Norwegian banks, but it is expected that Norway will adapt the legislation to the final text of BRRD2 when it is ready.

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A notable feature of the Norwegian banking regulations is the generous deposit guarantee scheme, which currently covers deposits of up to 2 million kroner. In connection with the implementation of the BRRD and the Deposit Guarantee Scheme Directive, both in January 2019, the EU has exerted pressure to lower the deposit guarantee scheme coverage to the EU level of €100,000. Nevertheless, the Norwegian guarantee coverage level has been upheld, and the Parliament Standing Committee on Finance and Economic Affairs has requested the government to continue talks with the EU in order to maintain the Norwegian guarantee level. Hence, it is still uncertain whether the Norwegian guarantee coverage level will be lowered or not.

IV CONDUCT OF BUSINESS

The Finance Agreements Act 1999 (which implements the Consumer Credit Directive) imposes certain conduct of business obligations upon banks, especially when dealing with consumers. In short, the Act provides that banks have a general duty to properly inform their clients, often in writing, and to ensure that a client has understood the information he or she has received. The Act also sets certain limits with respect to the kinds of materials and procedural provisions that can be included in a financial agreement (e.g., a loan agreement). A great number of the Act's provisions can be derogated from in a bank's dealings with business customers, but the Act is mandatory with respect to dealings with consumers.

Pursuant to Section 4 of the Finance Agreements Act, trade organisations for banks, insurance companies and other financial institutions in Norway have, with the Norwegian Consumer Ombudsman, established a mediation board for consumer complaints with respect to banks and banking products. However, the mediation board's resolutions are non-binding on the parties.

There have been discussions regarding a new Finance Agreement Act. The Ministry of Justice and Public Security sent a draft of a new act on public hearing in 2017. The draft received considerable criticism from various interested parties. The Minister of Justice has stated to Parliament that the Ministry of Justice and Public Security is currently considering the various comments received during the public hearing and aims to issue a proposal to Parliament for a new Finance Agreement Act during 2019.

Norwegian banking confidentiality rules are set out in the Financial Undertakings Act Sections 9-6, 9-7 and 16-2. The main rule is that, in the absence of a statutory exception, any non-public information concerning a bank or its customers that the bank's officers, employees or anyone who carries out an assignment for the bank, such as external auditors and lawyers, gain knowledge about in their position within the bank, is subject to a duty of confidentiality. The confidentiality obligation is directed both at the individual and the bank itself. In principle, the obligation extends to internal disclosure within the bank, but exceptions are available with respect to internal disclosure on a need-to-know basis.

Several exceptions apply to this main rule. Disclosure can be made without regard to the confidentiality obligation if:

a the customer consents to disclosure;

b disclosure is needed to fulfil requirements for reporting, control and internal governing within a banking group;

c the disclosure is made to another finance institution pursuant to specific rules in the Financial Undertakings Act;

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d the disclosure is required pursuant to the Money Laundering Act 2018 or similar regulations;
e the disclosure is requested by the police or prosecuting authorities;
f the disclosure is made in a civil or criminal court proceeding pursuant to a decision by the court;
g the disclosure is made to certain other authorities, such as tax authorities, competition authorities, the FSAN or the Norwegian stock exchange, and in accordance with specific regulations; or
h to a certain extent, for the purpose of establishing a central client register in a banking group.

This list is not exhaustive, and illustrates that the main rule of absolute confidentiality is subject to quite a few exceptions. A breach of the confidentiality obligation is a criminal offence punishable by a fine or, if considered a serious offence, imprisonment for up to three years.

V FUNDING

The main funding sources for Norwegian banks are deposits from customers, which amount to around 40 per cent of funding and the bond market (both domestic and international), which amount to around 20 per cent of the banks' total funding. A number of Norwegian banks have also established euro medium-term note programmes.

Another funding source is the raising of regulatory capital (see Section III.iii). Banks also fund themselves through credit lines with domestic or foreign third-party banks.

An increasingly important source of funding is the covered bond market. The Norwegian covered bonds legislation allows banks to set up specialised mortgage credit institutions, which in turn issue covered bonds to investors. The bonds are backed by a pool of specific types of mortgages (usually residential) or public sector loans acquired by the issuing mortgage credit institutions. The mortgage credit institution must be licensed as such, but it does not necessarily have to be affiliated with the bank from which it has acquired the mortgages.

As of the second quarter of 2018, the proportion of market funding with a residual maturity of more than one year was at 66 per cent. This has significantly increased over the past ten years, which in turn implies a lower liquidity risk of Norwegian banks. Only the largest Norwegian banks have access to the international capital markets, and Norway's largest bank, DNB Bank ASA, is an important source of funding for smaller banks. Norges Bank (the Norwegian central bank) offers certain funding to banks on a secured basis, and also acts as lender of last resort.

VI CONTROL OF BANKS AND TRANSFERS OF BANKING BUSINESS

i Control regime

The shares of a commercial bank and the equity certificates of a savings bank are freely transferable, unless the bank's articles of association state otherwise. There are no limitations under Norwegian law on the rights of non-residents or foreign owners to hold and vote for a commercial bank's shares or a savings bank's equity certificates. The Financial Undertakings Act does, however, contain non-discriminatory ownership control rules. Pursuant to these

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rules, an acquisition of ownership in a bank that represents 10 per cent or more of the sum of the capital or the votes, or that otherwise gives the right to exercise significant influence on the management of the bank and its business, requires prior authorisation from the FSAN and the MOF. The same rules apply to holding companies of banks.

Ownership by closely committed persons is consolidated, and convertible loans are deemed to be included in a person's holding.

Whether authorisation shall be granted is regulated in the Financial Undertakings Act and pertinent regulations, the main consideration being whether the acquirer is deemed fit and proper to exercise such influence over the financial undertaking as the qualified holding will enable. Additionally, the MOF must make an assessment as to whether the acquisition is sound in light of the financial undertaking's current and future business. The application will contain, inter alia, information about the following:

a current and proposed holding of shares;

b the acquirer's other business and available financial resources;

c ownership in other financial undertakings; and

d the purpose of the acquisition. If the financial undertaking in question will become a subsidiary, a plan for the organisation and activities of the group must be submitted.

An application for authorisation shall be decided within 60 business days of the FSAN having confirmed that it has received the application, but this may be prolonged if the MOF or the FSAN deem that additional information is necessary or desirable in connection with the fit and proper assessment.

The above applies not only to acquisitions resulting in a qualified holding, but also to acquisitions increasing an (already) qualified holding to a total holding of more than 20, 30 or 50 per cent, as the case may be.

Banks and other financial undertakings are subject to limitations on their ability to grant security for their assets. As a main rule, the FSAN's permission is necessary for a bank to grant security for assets representing more than 10 per cent of its core capital. Exceptions apply to security granted for real estate, as well as security transactions entered into in accordance with market practice and on standard arm's-length terms.

In relation to an acquisition of a commercial bank, the bank will be restricted under Norwegian corporate law from providing capital or security in support of the acquisition.

By a letter dated 12 December 2018, the MOF has ordered a study on the Norwegian ownership rules. The mandate of the study is, inter alia, to consider whether the Norwegian law on ownership for banks is in accordance with EEA law. The deadline for submitting the report to the MOF was 15 March 2019.

ii Transfers of banking business

Transfers of customers' deposits would, as a starting point, require the consent of each customer in accordance with ordinary rules relating to the transfer of debtor positions. Even if consent is given, it is at present technically impossible to transfer a customer's unique bank account from one bank to another. This is due to the fact that Norwegian bank account numbers are assigned systematically, and serve a special identification function: for instance, the first four digits of an account number are used to identify the bank with which the account is registered. In other words, the account number belongs to the bank and not to the customer. It has been proposed to enact legislation that would enable customers to retain their account number when changing banks, but this has yet to be resolved.

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With respect to loans, Section 45 of the Finance Agreements Act provides that banks may transfer loans without the borrowers' explicit consent only to other financial undertakings (as defined in the Financial Undertakings Act). Transfers of loans from banks to non-financial undertakings require the borrowers' consent. Until 2015, the Norwegian financial legislation contained special securitisation rules that allowed for the transfer of loans from a financial institution to a non-financial institution without active consent from the borrowers in connection with a securitisation transaction. However, these rules were abolished when the Financial Undertakings Act came into effect on 1 January 2016.

The Financial Undertakings Act also contains a provision regarding the transfer of substantial portfolios of loans or other receivables by banks and other financial undertakings. If the portfolio to be transferred is deemed substantial in light of the involved companies' business, consent from the MOF is required to effect the transfer. The exact scope of application of the provision has yet to be clarified.

If a bank's business is transferred by way of a merger or demerger in accordance with the applicable Norwegian company legislation, customer consent will not be necessary with respect to loans or deposits that, as a result of the merger, have been transferred to a new legal entity. The acquiring party in a merger or demerger is considered to automatically assume all rights, obligations and liabilities of the acquired party without the need for customer consent. However, mergers and demergers of banks must be applied for and are subject to the consent of the Norwegian regulator.

VII THE YEAR IN REVIEW

No major changes took place in the Norwegian banking market in 2018. The Norwegian banking industry retained strong profit levels. Both pre-tax profits and return on equity rose as compared to 2017, and the former is currently at roughly the same level as it was prior to the international financial crisis. Moreover, the overall net interest income of the banks has increased, while operating expenses have decreased as compared to 2017. This is partly due to the industry's focus on digitalisation and streamlining, and Norwegian banks are among the most efficient in Europe according to figures from the EBA. The unsecured consumer loan market was strong in the first three quarters of 2018, and figures show a 12 per cent increase in distributions as compared to 2017.

Moreover, the capital adequacy of the Norwegian banks has been further strengthened, and the banks' combined own equity is at nearly 16 per cent as of September 2018. This increase is mainly because of a decline of the average risk weights due to high growth in lending with low risk weight, and the implementation of to internal ratings-based models.

Similarly, the Norwegian deposit guarantee scheme has further stabilised. As of June 2018, the scheme covers approximately 60 per cent of the total deposits in Norwegian banks.

The MOF has prolonged the temporary regulation imposing stricter requirements for mortgage lending until 31 December 2019, with some alterations. Furthermore, an interim regulation on unsecured consumer loans came into effect on 12 February 2019. The regulation requires financial institutions to undertake more extensive assessments of their customers when distributing unsecured loans to consumers. Accordingly, the banks must, inter alia, ensure that a customer can bear an interest increase of five percentage points, and that the total debt does not exceed five times his or her annual salary. Moreover, amortisation

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of unsecured loans must be made monthly, and with not more than a five-year amortisation profile. Work on creating a debt register related to consumers has continued, and we expect that such register will be operative during 2019.

As described in Section II, a new Anti-Money Laundering Act was enacted in October 2018. During 2018, Parliament enacted changes to the Securities Trading Act (STA), effective from 1 January 2019, which incorporates MiFID II into the STA. Simultaneously, the Stock Exchange Act was repealed, and the relevant provisions are now to be found in the revised STA.

VIII OUTLOOK AND CONCLUSIONS

We expect a number of legislative changes to the Norwegian banking industry in 2019.

First, we expect that the government will propose a new Finance Agreement Act during 2019. We expect that this new Finance Agreement Act will comprise, inter alia, the above-mentioned interim regulation on unsecured customer loans.

Secondly, a number of EU directives are expected to be implemented in Norwegian legislation during 2019. Forthcoming implementation of and amendments to the EEA Agreement are expected to result in less gold plating, and special Norwegian rules for banks and other financial market participants. Both the CRD IV and the CRR are expected to be incorporated in the EEA shortly. Furthermore, the MOF has initiated preliminary work on implementing the Packaged Retail and Insurance-based Investment Products Regulation. While these directives will require certain amendments to the current Norwegian banking law, we do not expect any radical changes to the current legislative environment for banking activities.

Moreover, as outlined in Section II.v, the PSD2 is expected to be implemented during 2019. This will most likely lead to new participants in the Norwegian financial market.

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Appendix 1

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