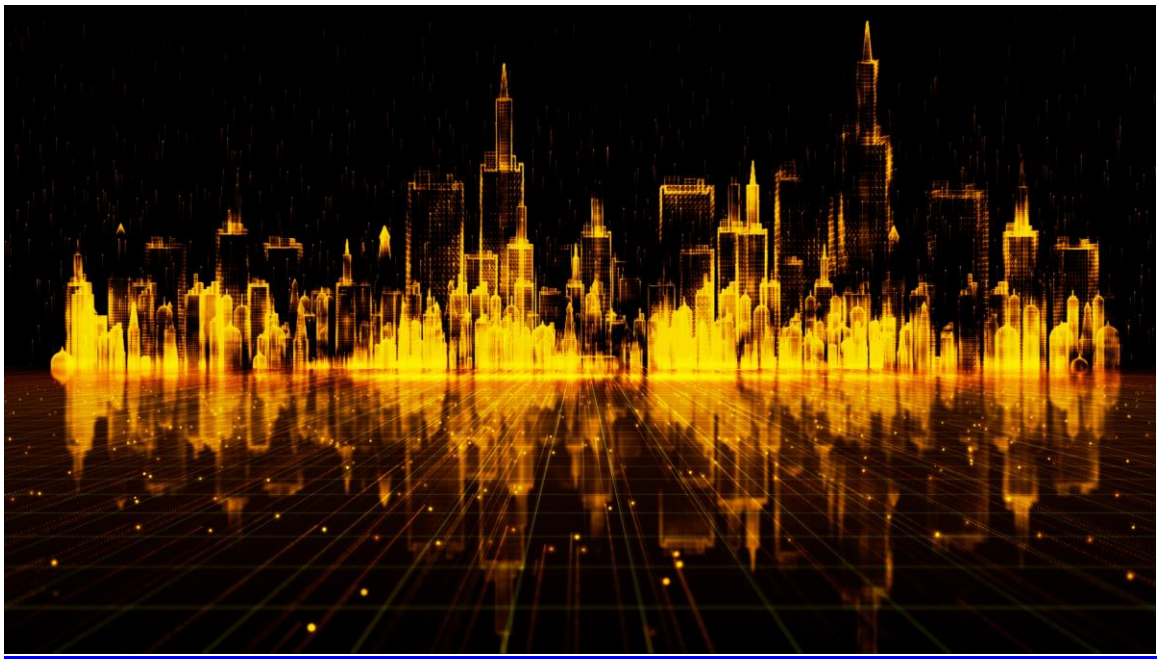
Basel iii Compliance Professionals Association (BiiiCPA)
1200 G Street NW Suite 800 Washington DC 20005-6705 USA
Tel: 202-449-9750 Web: www.basel-iii-association.com

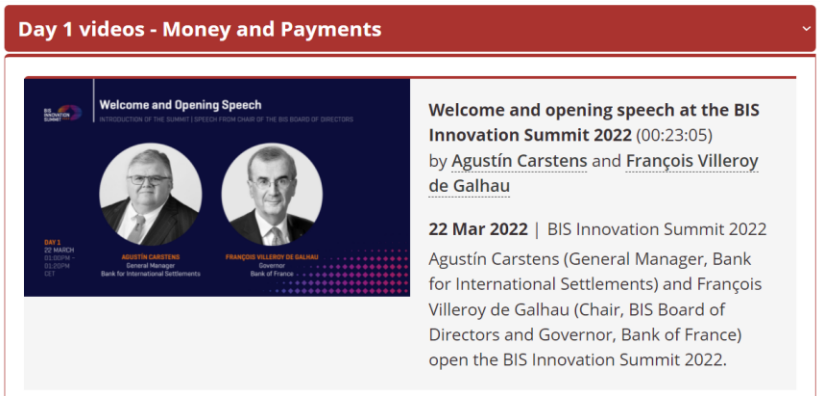


Basel iii News, April 2022

Dear members and friends,

We will start with some very interesting presentations.

The BIS Innovation Summit brings together global policymakers, senior executives from the financial and technology industries, and academics to discuss technology and innovation. Global leaders from the public and private sector discussed key issues around the future of money and payments, CBDC, DeFi, new technology in the financial system, green initiatives, and technology as an enabler for financial inclusion.



You may visit: https://www.youtube.com/watch?v=tXvV5G_qtaw

Central bank digital currencies, digital payments, and the future of money (00:46:32)
by Stefan Ingves, Patrick Njoroge, Gary Gorton and Jose Antonio Alvarez

22 Mar 2022 | BIS Innovation Summit 2022

Speakers discuss plans and challenges for the digital payments era and explore what the future might bring for money and payments from the perspectives of the private and public sectors.

You may visit: https://www.youtube.com/watch?v=xVD1ZFPzcbg

In conversation with Christine Lagarde about the future of money in the Eurosystem (00:25:49)
by Christine Lagarde

22 Mar 2022 | BIS Innovation Summit 2022

Josh Lipsky has a one on one conversation with the President of the European Central Bank, Christine Lagarde, about the future of money in the Eurosystem and the potential role for a digital Euro.

You may visit: https://youtu.be/vdqfIYj6oDc

To read more:
https://www.bis.org/events/bis_innovation_summit_2022/overview.htm

Central bank digital currencies: a new tool in the financial inclusion toolkit?

FSI Insights No 41, by Raphael Auer, Holti Banka, Nana Yaa Boakye-Adjei, Ahmed Faragallah, Jon Frost, Harish Natarajan and Jermy Prenio

Executive summary

Central banks are actively considering how retail central bank digital currencies (CBDCs) may fit with policy goals around financial inclusion.

In the second half of 2021, authors at the BIS and the World Bank interviewed nine central banks at various stages of exploring retail CBDCs and financial inclusion.

These are the Central Bank of The Bahamas, Bank of Canada, People's Bank of China, Eastern Caribbean Central Bank, Bank of Ghana, Central Bank of Malaysia, Bangko Sentral ng Pilipinas, National Bank of Ukraine and Central Bank of Uruguay.

While a CBDC, like other forms of money, has different functions (eg means of payment, store of value, unit of account, settlement asset), its link to financial inclusion is in the context of its payment properties, and hence it is the lens through which CBDC is discussed in this paper.

The interviewed central banks take the view that, while CBDC is not a panacea, it can represent a further tool to promote financial inclusion if designed with this goal.

The paper explores this theme, outlining findings in three main areas:

(i) existing barriers to financial inclusion that could be addressed with the introduction of a CBDC;

(ii) CBDC design features that many jurisdictions view as critical to addressing these barriers; and

(iii) the challenges foreseen, along with legal and regulatory changes needed for CBDC implementation.

Barriers to financial inclusion differ across countries, but there were some common elements that came out in the interviews. These can be grouped into six main areas.

First are geographic barriers related to vast territories and remote locations.

Second are institutional and regulatory factors, such as a lack of public goods like identity credentials, as well as informality and a lack of consumer protection.

Third are economic and market structure issues, including limited competition, inefficiency in the financial sector and a lack of profitability of serving excluded groups.

Fourth are characteristics of vulnerability, such as barriers by age, gender, income or disability status like visual and hearing impairments.

Fifth is a lack of education and financial literacy, and sixth is low trust in existing financial services.

Some central banks consider CBDCs as key to their mandate as a catalyst for innovation and economic development.

While access to payment services has grown in recent years, it is still far from universal.

Low-income populations and those living in remote locations continue to confront barriers to digital payments.

Domestic retail payment services can be expensive, and payments across borders – particularly for low-value transfers like remittances – face even larger challenges.

CBDCs can secure the continuous provision of public money to the general public.

With CBDCs, central banks can help to speed up digital payment adoption, particularly when market size and profit potential are insufficient to motivate private sector innovation, or when established oligopolies prevent entry.

Some central banks argued that they have a role to play in applying innovation to specific access challenges.

As such, given the expanding yet uneven access to payment services, they recognise the importance of pursuing CBDC issuance.

Several central banks see CBDC more as a potential complement to existing financial inclusion initiatives.

Many jurisdictions are tackling financial inclusion barriers today with dedicated strategies to improve the provision of transaction accounts and other payment products. The entry of non-banks and agent-based models,

risk-based and proportionate customer enrolment processes, effective use of data and interoperability remain relevant.

Authorities are already expanding the network of readily available access points and developing tools to improve awareness of transaction accounts and digital money, including by promoting financial and digital literacy.

Central banks are also modernising existing payment infrastructures with the introduction of fast payment systems and leveraging high-volume recurrent payment streams. Several central banks noted that these actions, if implemented effectively, would be the most direct means to tackle financial exclusion.

These are in line with the Committee on Payments and Market Infrastructures and World Bank guiding principles of payment aspects of financial inclusion (PAFI).

To read more: https://www.bis.org/fsi/publ/insights41.pdf

Environmental, Social and Governance (ESG) risks

EBA publishes binding standards on Pillar 3 disclosures on ESG risks

▪ The technical standards aim to ensure that stakeholders are well-informed about institutions' ESG exposures, risks, and strategies and can make informed decisions and exercise market discipline.

▪ The standards put forward comparable disclosures and KPIs, including a green asset ratio (GAR) and a banking book taxonomy alignment ratio (BTAR), as a tool to show how institutions are embedding sustainability considerations in their risk management, business models and strategy and their pathway towards the Paris agreement goals.

▪ In developing this framework, the EBA has built on the recommendations of existing initiatives, like those of the Task Force on Climate-related Financial Disclosures (TCFD) of the Financial Stability Board (FSB), but has gone beyond by defining binding granular templates, tables and instructions, to ensure enhanced consistency, comparability and meaningfulness of institutions' disclosures.

The European Banking Authority (EBA) published its *final draft* implementing technical standards (ITS) on Pillar 3 disclosures on Environmental, Social and Governance (ESG) risks.

The final draft ITS put forward comparable disclosures to show how climate change may exacerbate other risks within institutions' balance sheets, how institutions are mitigating those risks, and their ratios, including the GAR, on exposures financing taxonomy-aligned activities, such as those consistent with the Paris agreement goals.

Disclosure of information on ESG risks is a vital tool to promote market discipline, allowing stakeholders to assess banks' ESG related risks and sustainable finance strategy.

The EBA ESG Pillar 3 package will help to address shortcomings of institutions' current ESG disclosures at EU level by setting mandatory and consistent disclosure requirements, including granular templates, tables and associated instructions.

It will also help establish best practices at an international level.
In line with the requirements laid down in the Capital Requirements Regulation (CRR), the draft ITS set out comparable quantitative disclosures on climate-change related transition and physical risks, including

information on exposures towards carbon related assets and assets subject to chronic and acute climate change events.

They also include quantitative disclosures on institutions' mitigating actions supporting their counterparties in the transition to a carbon neutral economy and in the adaptation to climate change.

In addition, they include KPIs on institutions' assets financing activities that are environmentally sustainable according to the EU taxonomy (GAR and BTAR), such as those consistent with the European Green Deal and the Paris agreement goals.

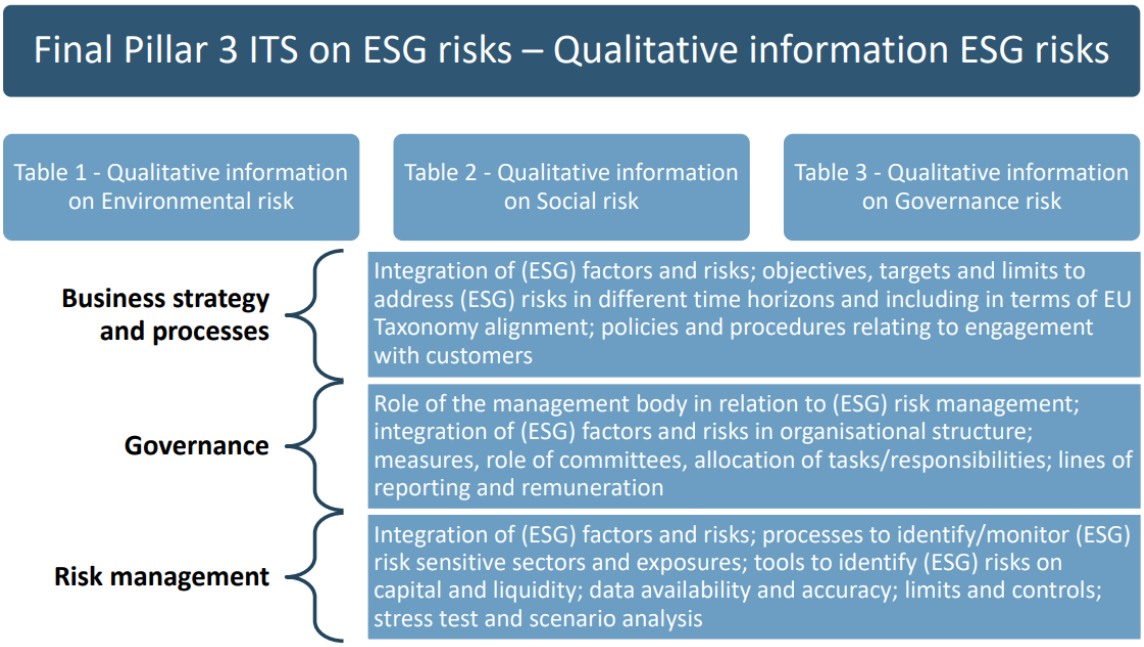
Finally, the final draft ITS provide qualitative information on how institutions are embedding ESG considerations in their governance, business model, strategy and risk management framework.

The EBA has integrated proportionality measures that should facilitate institutions' disclosures, including transitional periods and the use of estimates.

The Pillar 3 disclosure framework promotes transparency as a main driver of market discipline in the financial sector, to reduce the asymmetry of information between credit institutions and users of information, and to address uncertainties on potential risks and vulnerabilities faced by institutions.

The Pillar 3 framework on prudential disclosures on ESG risks is intended to allow investors and stakeholders to compare the sustainability performance of institutions and of their financial activities, and will support institutions in the public disclosure of meaningful and comparable information on how ESG-related risks and vulnerabilities, including transition and physical risks, may exacerbate other risks in their balance sheet.

In addition, it will help institutions in providing transparency on how they are mitigating those risks, including information on how they are supporting their customers and counterparties in the adaptation process to e.g. climate change and in the transition towards a more sustainable economy.



To read more:
https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Draft%20Technical%20Standards/2022/1026171/EBA%20draft%20ITS%20on%20Pillar%203%20disclosures%20on%20ESG%20risks.pdf

FinTech and Market Structure in the COVID-19 Pandemic Implications for financial stability

The COVID-19 pandemic has accelerated the trend toward digitalisation of retail financial services.

Comprehensive data on market shares of FinTechs, BigTechs and incumbent financial institutions in retail digital services are lacking, but proxies in the form of revenue and app downloads, and insights from market outreach suggest that BigTechs and larger FinTechs have further expanded their footprint in financial services.

In some markets, concentration measures are high, but there is no evidence yet of a generalised increase.

The observations in this report broadly support the conclusions of previous FIN reports. BigTech and FinTech firms' expansion into financial services can bring benefits such as improved cost efficiencies and wider financial inclusion for previously underserved groups.

BigTechs' financial activities in emerging market and developing economies (EMDEs) bring particular benefits in this regard. At the same time, there is potential for (rapid) market dominance.

There could be negative financial stability implications from dependence on a limited number of BigTech and FinTech providers in some markets, the complexity and opacity of their partnership activities, and potential incentives for risk taking by incumbent financial institutions to preserve profitability.

Consumer protection risks could arise from greater dependency on technology and potential data protection issues, e.g. the unauthorised use or the misuse of users' personal data.

Cloud computing by third-party service providers not subject, in many cases, to financial regulation can introduce cost efficiencies and access to innovations in artificial intelligence (AI).

But the limited number of providers of cloud services could magnify the impact of any operational vulnerability.

The growth of BigTechs in particular may give greater urgency to financial stability issues previously discussed, such as the potential for greater systemic importance of new players that may not be subject to financial regulation.

This underscores the need to address data gaps that currently hamper the assessment of the financial risks and systemic importance of BigTechs. Such data gaps make it difficult for authorities to decide whether and how to include BigTechs in the regulatory perimeter.

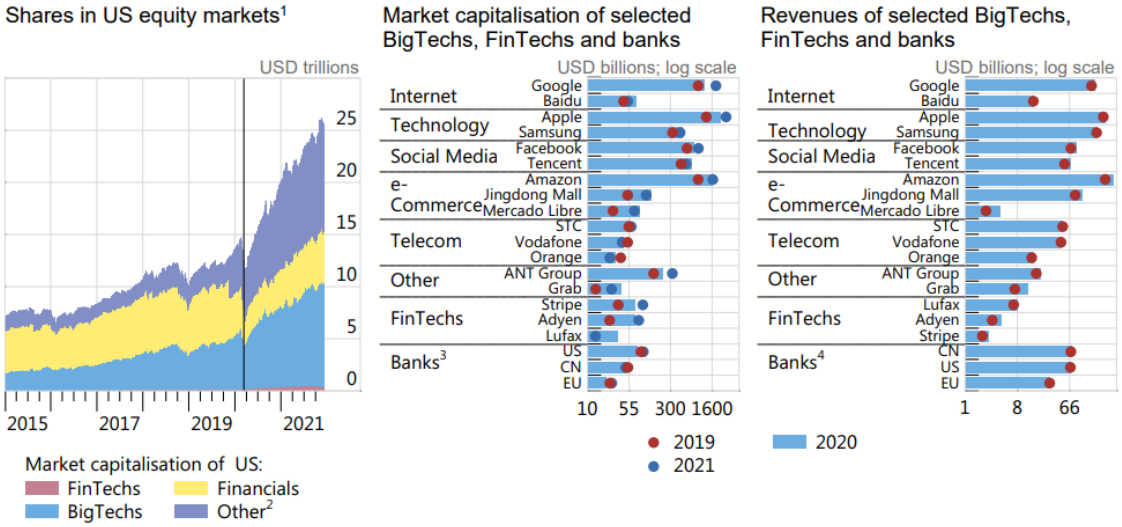
Authorities have taken a range of policy actions during the pandemic that may impact market structure and the role of FinTechs, BigTechs and incumbent financial institutions.

These actions relate to financial stability, competition, data privacy and governance issues.

In parallel, there is international work on third-party dependencies of the financial sector, for instance in cloud computing.

This highlights the importance of cooperation between regulatory and supervisory authorities, including those charged with overseeing the bank and non-bank sectors, and where relevant, with competition and data protection authorities.

Performance of BigTechs, FinTech and incumbents during Covid-19 **Graph 1**



[1] The vertical line denotes 11 March 2020, when the WHO characterised Covid-19 as a pandemic. [2] Calculated as the market capitalisation of S&P 500 and Nasdaq minus the market capitalisation of FinTechs, BigTechs and financials. [3] Many FinTechs are not publicly listed. In these cases, data on market capitalisation and revenues are drawn from news sources. [4] Average market capitalisation of banks in the S&P 500 index, EuroStoxx Banks index and Shanghai Composite index. [5] Average revenue, weighted by market capitalisation, of banks in the S&P 500, EuroStoxx Banks index and Shanghai Composite index.

Sources: Bloomberg, Eikon, S&P Capital IQ; FSB calculations.

To read more:
https://www.fsb.org/wp-content/uploads/P210322.pdf

The return of inflation

Agustín Carstens, General Manager of the BIS at the International Center for Monetary and Banking Studies, Geneva

Thank you very much for inviting me to give this lecture. It is a pleasure and an honour to be here today.

Being the BIS's General Manager, it will not come as a surprise to you that I have decided to devote my presentation to the issue that is top of mind for policymakers around the world, namely the return of inflation.

After more than a decade of struggling to bring inflation up to target, central banks now face the opposite problem.

The shift in the inflationary environment has been remarkable.

If you had asked me a year ago to lay out the key challenges for the global economy, I could have given you a long list, but high inflation would not have made the cut.

This evening, I will describe the rise in inflation over the past year and discuss why this came as a surprise to many.

I will argue that the pandemic and the extraordinary policy response laid the groundwork for a rapid and goods-intensive bounceback in demand which supply has been unable to fully meet.

The war in Ukraine has further disrupted supply, particularly for commodities.

I will also draw some broader lessons about the inflationary process – in particular, the need to look "under the hood" of aggregate data and models to understand how the behaviour of individual firms and workers drives inflation outcomes.

A key message is that we may be on the cusp of a new inflationary era. The forces behind high inflation could persist for some time.
New pressures are emerging, not least from labour markets, as workers look to make up for inflation-induced reductions in real income.

And the structural factors that have kept inflation low in recent decades may wane as globalisation retreats.

If my thesis is correct, central banks will need to adjust, as some are already doing.

For many years now, having conquered inflation, they have had unprecedented leeway to focus on growth and employment.

Indeed, with inflation stubbornly below target, stimulating activity hit two birds with one stone.

But this is now no longer possible, since low and stable inflation must remain the priority.

If circumstances have fundamentally changed, a change in paradigm may be called for.

That change requires a broader recognition in policymaking that boosting resilient long-term growth cannot rely on repeated macroeconomic stimulus, be it monetary or fiscal.

It can only be achieved through structural policies that strengthen the productive capacity of the economy.

To read more: https://www.bis.org/speeches/sp220405.pdf

FSB Work Programme for 2022

The Financial Stability Board's (FSB) work programme for 2022 aims to maximise the value of the FSB's global and cross-sectoral approach to financial stability policy.

The FSB's work priorites reflect that financial challenges are global in nature and affect the financial system as a whole.

These challenges include digitalisation, climate change and potentially also shifts in the macroeconomic and interest rate environment.

This note summarises the ongoing and planned FSB initiatives in 2022 organised by:

(1) priority areas of work and new initiatives;

(2) work programme items that are continuing or reaching completion; and

(3) regular monitoring and reporting.

The Annex provides an indicative timeline of the FSB's publications planned for 2022.

1. Priority areas of work and new initiatives

Supporting international cooperation and coordination on current financial stability issues.

The FSB, with its broad and diverse membership of national authorities, international standard setters and international bodies, continues to promote financial stability in a rapidly evolving financial market environment.

Against the backdrop of the Russia-Ukraine conflict and its economic impacts, the FSB is reinforcing its forward-looking monitoring to identify, assess and address new and emerging risks to global financial stability.

This enhanced monitoring is informed by the FSB's new surveillance framework.

Work will also continue on policy responses to COVID-19, including: sharing information on policy responses and the timely unwinding of the temporary measures adopted in response to COVID-19, and assessing the

effectiveness of those measures; and monitoring, with the standard-setting bodies (SSBs), the use of flexibility within international standards and consistency of policy responses with existing international financial standards.

- Work on the financial stability implications of current developments will continue in a flexible mode – including on specific vulnerabilities, policy issues and monitoring – and be adjusted as needed.

- FSB will work with SSBs to follow up on specific issues identified in the report on lessons learnt from COVID-19 for financial stability, including macroprudential aspects of buffer functioning.

- At the request of the Indonesian G20 Presidency, the FSB will report to the G20 on exit strategies to support equitable recovery for financial stability, and on effective practices and policy recommendations for addressing the effects of COVID-19 scarring in the financial sector.

Enhancing the resilience of the non-bank financial intermediation (NBFI) sector, while preserving its benefits.

The FSB will advance its work programme for strengthening the resilience of NBFI.

This work, set out in the FSB's holistic review of the March 2020 market turmoil, will be carried out within the FSB as well as by SSBs and international organisations.

- In 2022, remaining work on specific issues identified in the holistic review will be completed, including on open-ended funds (OEFs); margining practices; the liquidity, structure and resilience of core bond markets; and USD funding and emerging market economy (EME) vulnerabilities.

- In addition, work will focus on developing a systemic approach to NBFI. This includes enhancing the understanding of systemic risks in NBFI and strengthening their ongoing monitoring; and developing policies to address such risks.

Enhancing cross-border payments.

The FSB roadmap for enhancing cross-border payments contains a large number of actions, guided by a set of quantitative targets.

To help achieve these targets, specific proposals for material improvements to existing payments systems and arrangements are being discussed, as well as the development of new systems.

The FSB will continue to coordinate with CPMI and other SSBs and international organisations in implementing the FSB roadmap to enhance cross-border payments.

- In 2022, the FSB has committed to complete a number of actions under the roadmap, including the development of an approach to monitor progress against the quantitative targets; identification of gaps or areas for enhanced implementation in standards; and work on enhancing data sharing.

- The FSB will deliver to the G20 a progress report on the overall roadmap and the development of key performance indicators to monitor progress towards the quantitative targets.

To read more: https://www.fsb.org/wp-content/uploads/P310322.pdf

FSB Statement Welcoming Smooth Transition Away from LIBOR

Following years of preparation, the end of 2021 marked a major milestone in the transition away from LIBOR and the FSB welcomes the smooth transition to robust alternative rates across global markets, primarily overnight risk-free or nearly risk-free rates (RFRs).

The absence of any significant market disruptions is a testament to the magnitude of market participants' efforts and the level of attention from the regulators and industry bodies to support the transition to RFRs.

Stocktake of end-2021 transition

All GBP, EUR, CHF, and JPY LIBOR panels, as well as the 1-week and 2-month USD LIBOR settings, ceased as of end-2021.

The 1-, 3- and 6-month GBP and JPY LIBOR settings are being published temporarily on a synthetic basis to support legacy contracts.

While key panel-based USD LIBOR settings will continue until end-June 2023, this is intended to support the run-off of a substantial proportion of legacy contracts.

US Banking Supervisors as well as many other authorities in FSB jurisdictions have strongly encouraged firms to cease new use of USD LIBOR after end-2021, subject only to some limited exceptional use to support an orderly transition.

It is important to continue to build market liquidity of products referencing robust RFRs and to use SOFR across global markets.

The transition in GBP, EUR, CHF, and JPY LIBOR shows that RFRs can be used successfully in a wide variety of markets including bonds, derivatives and lending markets.

There has already been a significant and smooth transition away from USD LIBOR for many markets.

New activity in USD over-the-counter derivatives and capital markets products is predominantly linked to SOFR now.
Additionally, the transition from USD LIBOR to SOFR appears to be progressing smoothly in lending markets.

Use of SOFR has increased in exchange traded derivatives, however greater progress will need to be achieved in certain markets, such as in Eurodollar futures and options markets, where significant LIBOR-linked activity remains.

Key messages for 2022-23

Given the significant use of USD LIBOR globally, the FSB emphasises that firms must have plans in place to ensure their preparedness for the cessation of the USD LIBOR panel.

The FSB continues to support a smooth transition of legacy LIBOR contracts as part of a wider market transition to robust RFRs that will not reintroduce the vulnerabilities experienced with LIBOR.

The FSB again highlights the Statement on Credit Sensitive Rates by the Board of the International Organization of Securities Commissions (IOSCO).

Firms should have already ceased new use of USD LIBOR. It has been repeatedly emphasised by authorities that the continuation of some USD LIBOR settings through to end-June 2023 is intended only to allow legacy contracts to mature.

In addition, it affords market participants more time to take the necessary steps for the conversion of legacy contracts.

Between now and end-June 2023, firms with USD LIBOR exposures should take the steps set out in the FSB's Global Transition Roadmap.

To ensure financial stability, it is important that market participants transition from LIBOR and other IBORs that are set to be discontinued.

The FSB continues to encourage adoption of overnight RFRs and active transition away from USD LIBOR before June 30, 2023 where appropriate.

The FSB recognises that in some cases there may be a role for RFR-derived term rates and has set out the circumstances where the limited use of RFR-based term rates would be compatible with financial stability.

The FSB also continues to support engagement with emerging markets and developing economies (EMDEs) to maintain a smooth transition from LIBOR to RFRs, across all global markets.

The FSB encourages firms to maintain momentum in active transition of legacy LIBOR contracts that reference synthetic GBP and JPY LIBOR settings.

The FCA has been clear that synthetic LIBOR is a temporary bridging solution to allow more time for legacy contracts to transition to robust RFRs. Synthetic LIBOR rates cannot be guaranteed beyond end-2022. For JPY LIBOR, the FCA's intention is that it will cease at end-2022.

The FCA has announced that, during the course of 2022, it will seek views on retiring 1-month and 6-month synthetic sterling LIBOR at the end of 2022, and on when to retire 3-month sterling synthetic LIBOR. It should be noted that active transition remains the best way for parties to retain control and certainty over their contractual terms.

The FSB plans to conduct a follow-up assessment in H2 2022 to identify any remaining transition and supervisory challenges to support LIBOR transition effort.

Surfing on behalf of consumers

BaFin Federal Financial Supervisory Authority

Do banks and insurers provide information about alternative dispute resolution mechanisms on their websites and in their small print? BaFin investigated the situation.

When most people hear the words "surf days" they think of sun, sand and metre-high waves. But for BaFin staff the term is an important supervisory tool in an era of increasing digitalisation. Supervisors visit selected companies' websites to gain an overview of how specific supervisory issues are handled.

BaFin's Consumer Protection Directorate (VBS) looked at banks' and insurers' websites on two surf days in 2021. The goal was to check whether the companies were complying with their duty to provide information on alternative dispute resolution mechanisms under section 36 of the German Act on Alternative Dispute Resolution in Consumer Matters (Verbraucherstreitbeilegungsgesetz – VSBG) to the extent necessary. The Directorate found that most companies were already compliant: only in a few cases did the supervisors have to require changes.

The background to the surf days was a ruling by Germany's Federal Court of Justice (Bundesgerichtshof – BGH) on the VSBG dated 22 September 2020 (case ref.: XI ZR 162/19). This specified that companies have to inform consumers about alternative dispute resolutions mechanisms both on their website and in their general terms and conditions of business. "Alternative dispute resolution mechanisms" are defined as conflict resolution methods that can be pursued instead of court cases.

Alternative dispute resolution

The term "alternative dispute resolution" is used to describe conflict resolution methods that can be pursued instead of court cases. Many banks and insurers have signed up to the dedicated consumer dispute resolution entities that have been recognised by the Federal Office of Justice (Bundesamt für Justiz).

These give consumers an independent, cost-effective, and efficient way of clarifying and resolving any disputes that arise. Further information on this topic and an overview of the most important dispute resolution entities, ombudsperson schemes and complaints offices for customers in the German finance industry can be found on BaFin's website. You may visit: https://www.bafin.de/EN/Verbraucher/BeschwerdenStreitschlichtung/StreitSchlichtungsstellen/StreitSchlichtungsstellen_node_en.html;jsessionid=2DC57AEED7B2B810A4ABB7449BB0A3CC.1_cid500

A broad-based sample

BaFin selected 50 credit institutions and 30 insurance undertakings for its investigations. The institutions included savings banks, cooperative banks and private banks of different sizes and from different regions.

The insurers comprised 10 life insurers, 10 health insurers and 10 property/casualty insurers. The goal was to have as representative a sample as possible.

Banks: most results were satisfactory

The banking surf day revealed that 40 out of the 50 institutions complied with their duties to provide information in full. The references to alternative dispute resolution mechanisms provided both on their websites and in the terms and conditions that are accessible there complied with the statutory requirements. However, BaFin discovered that four institutions had what were in part material defects.

Either the websites provided no information at all on out-of-court dispute resolution mechanisms or the information given was imprecise. For example, foreign dispute resolution entities that do not actually have jurisdiction were mentioned or institutions that have not been approved for alternative dispute resolution, such as the European Central Bank, were listed.

Insurers: most undertakings provide information

The surf day for the insurance sector revealed that all undertakings with an Internet presence that were investigated had published the necessary reference to out-of-court dispute resolution mechanisms on their websites.

In addition, BaFin checked whether the insurers, like the banks, had added an appropriate reference in the general policy conditions that are accessible via their websites.

A total of 15 undertakings published their current general policy conditions directly on their websites – something they are not actually obliged to do. However, only six of these general policy conditions contained all necessary information on alternative dispute resolution, whereas nine insurance undertakings did not provide the information for some tariffs at least.

Defects are being remedied

The banks and insurers for which BaFin discovered defects during its surf days have all reacted and have rectified, or promised to rectify, the errors in their general terms and conditions or their general policy conditions.

Authors

Julia Halm, Market Supervision concerning the Conduct of Insurance Undertakings towards Consumers
Christian Pampel, Policy Issues, Consumer Protection Forum and Consumer Advisory Council

Project Ellipse
An integrated regulatory data and analytics platform

Executive summary

A transformational shift in the volume, speed and variety of data is driving the innovative use of financial technology, leading to rapid changes in the financial landscape.

At the same time, regulatory authorities still rely on the collection of template-based supervisory data, which has remained largely unchanged.

Supervisors are faced with the challenge of needing to assess rapidly evolving risks to business models and technology-driven changes that may affect financial stability, with regulatory data that are infrequent and collected according to legacy frameworks.

In January 2021, the BIS Innovation Hub Singapore Centre and the Monetary Authority of Singapore (MAS) launched Project Ellipse.

With the support of the Bank of England (BoE), the International Swaps and Derivatives Association (ISDA), Financial Network Analytics (FNA) and Accenture, Project Ellipse explores how technology solutions could enable supervision to be more forward-looking, insights-based and data-driven, using an integrated regulatory data and analytics platform.

Importantly, the Ellipse prototype combines both structured and unstructured sources of data that are relevant to current events in real time.

Advanced analytics are then applied to those integrated data sources to provide supervisors with early warning indicators, analytics and prudential metrics.

Project Ellipse was undertaken in two phases. In Phase 1, the project investigated how data-driven supervision could be enabled by machine-executable digital reporting, using a cross-border common data model.

Our exploration found that regulatory reporting requirements can be expressed in unambiguous machinereadable logical reporting instructions underpinned by a consistent data model.
Programmatic specifications of the steps for generating regulatory reports can also be published alongside regulations to ensure a clear understanding of the expected data at the most granular level.

With additional logical instructions based on the same data model, supervisors could also automatically query the underlying transaction data and generate regulatory metrics referencing that standardised data.

Phase 1 illustrated the possibilities and the efficiencies that could be gained if machine-executable reporting using common data models were to be adopted.

This could also increase the volume of granular data available to supervisors, as needed to enable the use of advanced analytics.

In Phase 2, the project took existing large exposures regulatory data and integrated these with unstructured data.

Advanced analytics such as machine learning and natural language processing were applied to these data sources to make risk correlations and to analyse sentiment, alerting supervisors in real time of issues that might need further investigation.

Network analytics were also used to demonstrate how exposures could be mapped, indicating possible systemic risks to the banking system.

The Ellipse platform prototype was developed, which can extract insights from the mined data and display these via dashboards as early warnings for supervisory attention.

The second phase of Project Ellipse demonstrates how a single platform could be built so that authorities could benefit from “on demand” access to timely and integrated sources of data to help support and inform their supervisory assessments.

The BIS Innovation Hub’s Project Ellipse is a prototype that authorities can test in their own environments and which may help them to explore new solutions.

It also presents an opportunity for the global regulatory community to further consider, explore and collaborate on common solutions to future-proof the data and analytical capabilities of supervisors.

To read more: https://www.bis.org/publ/othp48.pdf

Table 1 — Challenges of regulatory reporting

1 Template based, aggregated

Regulatory requirements are often template-based and call for aggregated data, meaning that data sets are fixed to a use case and hence the data received cannot be easily reused for other purposes. New reporting requirements are needed whenever additional or ad hoc information is needed.

2 Data are inconsistently described

Reporting data are often sourced from reporting firms' legacy data systems, which may not be integrated. This often results in heterogeneity of data for any given product or transaction – both within a bank and across different banks – as different systems will describe these data differently.

CHALLENGES FACED

3 Infrequent, backward looking

Regulatory reports are submitted to supervisors from reporting entities on an infrequent basis (eg every month or quarter). At times of heightened risk, the need for up-to-date data increases but, given the static nature of regulatory reports, supervisors may not have the timeliest data to make informed judgments.

4 Different sources of data are not integrated

Information contained in regulatory reports is often linked to other types of information that may point to emerging risks, but these sources of information are not connected. For instance, information sourced from market data and news often gives the first indication of emerging risks but it is difficult for supervisors to scan through the vast volumes of market and news data to assess which point to a need to take early action.

Table 2 — Possible solutions explored in Project Ellipse

1 Granular data

The collection of granular data from reporting entities could replace the need for authorities to request information using templates. It could also enable authorities to reuse those data for different use cases. Supervisory metrics could also be derived using granular data, as opposed to requiring reporting entities to aggregate the required data prior to submission.

2 Common data models

Differences in the description of data for similar products and transactions across banks can be addressed using data standards and common data models. Granular reporting requires a common understanding by authorities and financial institutions of what these data are, so that financial institutions can map their operational data to a common "input" before the required data can be reported. Supervisory metrics could then be derived using programmable rules that reference machine-readable and machine-executable common data models.

SOLUTIONS EXPLORED

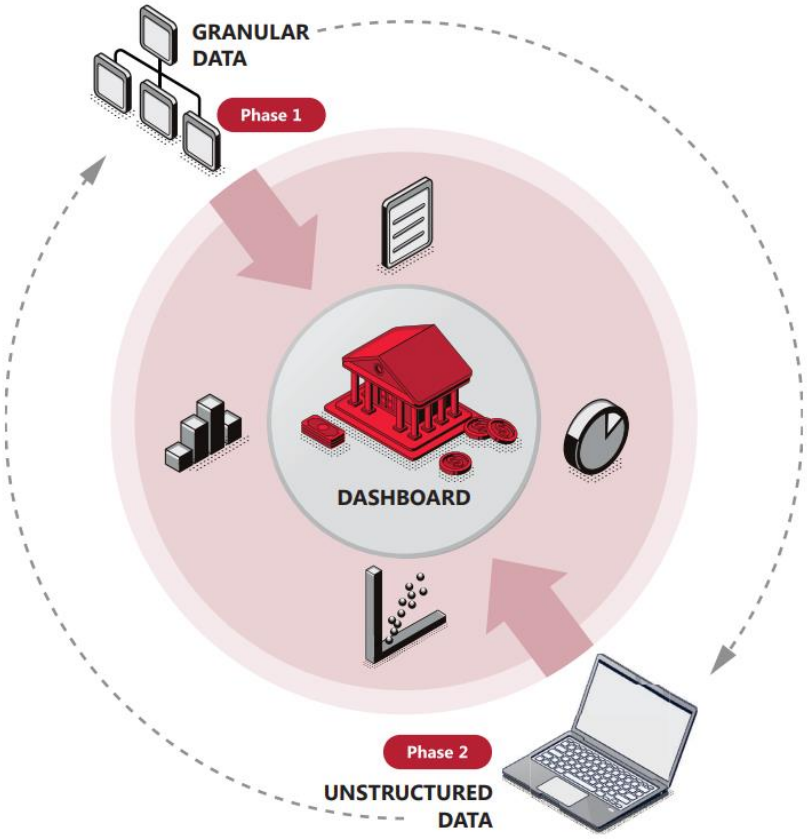
SOLUTIONS EXPLORED

3 Real-time information

Real-time insights using advanced analytics could be derived from large volumes of unstructured data that would supplement the granular reporting available. This would provide supervisors with additional indicators and early warnings of any at-risk exposures of reporting entities.

4 Integration of structured and unstructured data

Integrating granular data from reporting entities with other sources of unstructured information such as news and market data on the same platform would obviate the need for supervisors to spend time manually scanning for information. Advanced analytics such as AI and ML could be used to make risk correlations and analyse sentiment, alerting supervisors in real time of issues that may need further investigation.



EBA publishes revised Guidelines on common procedures and methodologies for the supervisory review and evaluation process

The European Banking Authority (EBA) published its final revised Guidelines on common procedures and methodologies for the supervisory review and evaluation process (SREP) and supervisory stress testing.

The revisions aim at implementing the amendments to the Capital Requirements Directive (CRD V) and Capital Requirements Regulation (CRR II) and promoting convergence towards best supervisory practices.

The changes to these Guidelines do not alter the overall SREP framework but affect its main elements, including:

(i) business model analysis,

(ii) assessment of internal governance and institution-wide control arrangements,

(iii) assessment of risks to capital and adequacy of capital to cover these risks, and

(iv) assessment of risks to liquidity and funding and adequacy of liquidity resources to cover these risks.

The main amendments are aiming at:

- better articulating the principle of proportionality, through the categorisation of institutions and the application of the minimum engagement model;

- fully incorporating the assessment of the money laundering and terrorist financing (ML/TF) risks, in line with the EBA Opinion on how to take into account ML/TF risks in the SREP;

- reviewing the provisions on Pillar 2 capital add-ons and the Pillar 2 guidance, to ensure they reflect a purely micro-prudential perspective and appropriately implement the separate stack of own funds requirements based on the leverage ratio;

- aligning the assessment of the interest rate risk in the non-trading book, as well as the assessment of liquidity risk and liquidity adequacy with the current regulatory framework;

- enhancing the dialogue among institutions and supervisors in relation to the setting of the Pillar 2 requirements.

Legal basis and background

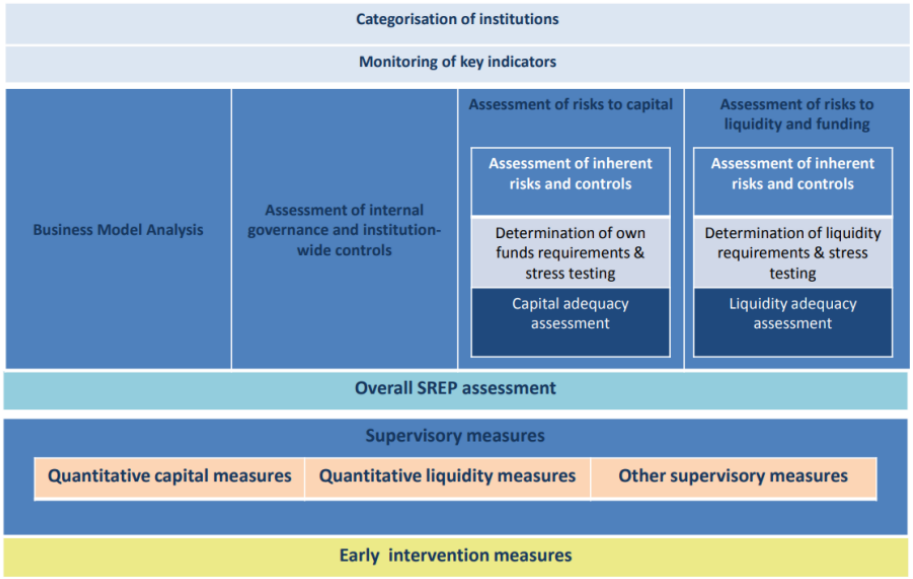
The EBA has developed these Guidelines in accordance with Article 107(3) of the CRD, which mandates the Authority to foster sound and effective supervision and to drive supervisory convergence across the EU. These Guidelines are addressed to all competent authorities across the EU.

SREP is an ongoing supervisory process bringing together findings from all supervisory activities into an institution's comprehensive supervisory overview.

These Guidelines also aim at achieving convergence of practices followed by competent authorities in supervisory stress testing across the EU in accordance with Article 100 of Directive 2013/36/EU.

To read more:
https://www.eba.europa.eu/sites/default/documents/files/document_library/Publications/Guidelines/2022/EBA-GL-2022-03%20Revised%20SREP%20Guidelines/1028500/Final%20Report%20on%20Guidelines%20on%20common%20procedures%20and%20methodologies%20for%20SREP%20and%20supervisory%20stress%20testing.pdf

Figure 1. Overview of the common SREP framework



Full disclosure - coming to grips with an inconvenient truth

Frank Elderson, Member of the Executive Board of the European Central Bank and Vice-Chair of the Supervisory Board of the ECB, at the 14th European Bank Institute Policy Webinar on the ECB's supervisory approach on climate-related and environmental risks, Frankfurt am Main

Some years ago, Andrea Enria, the Chair of the Supervisory Board, gave a speech, precisely at an EBI conference, calling for greater transparency in prudential supervision.

When describing the role of transparency and information disclosure, he echoed the words of Supreme Court Justice Louis Brandeis:

"Sunlight is said to be the best of disinfectants; electric light the most efficient policeman".

This couldn't be truer for climate-related disclosures, too. As I have said before when discussing the supervision and prominence of climate-related and environmental, or C&E, risks, we can only tackle a problem once we get a good grip on its shape and size. Some information may be uncomfortable to face up to – but bringing it to light is the first step in making progress.

When it comes to climate change, the information on what Al Gore famously dubbed an inconvenient truth is indeed getting bleaker by the day.

The most recent IPCC report confirms the dramatic consequences of not taking immediate action: additional global warming of up to 1.5 degrees Celsius in the near term would increase climate hazards, and present numerous risks to ecosystems and human society.

Europe is particularly badly affected, as temperatures here continue to rise above the mean and, despite our efforts to reduce CO2 emissions, we lag far behind in terms of what we need to do to adapt to some of the inevitable consequences.

It is time we face the facts. As citizens, as institutions, and as all actors in the economy – including of course banks.
It is essential that banks share with their stakeholders detailed information on their exposures to C&E – risks. Only then can we all effectively work together to address the consequences of climate change.

This is why today I would like to draw your attention to another important landmark in the ECB's supervision of C&E risks: the publication of our second stocktake on the transparency of banks' disclosures of their C&E risk profiles.

The European and international agenda on climate

Publishing this update is part of our supervisory agenda on climate. As you know, C&E risks have been one of our supervisory priorities for some years now and we have started treating them just like any other prudential risk.

In this context, we have been rolling out a series of corresponding supervisory activities.

In 2020 we published our guide on climate-related and environmental risks, which outlined our supervisory expectations relating to the management and disclosure of C&E risks.

In 2021 we published a self-assessment benchmarking report. And in 2022 we launched the climate risk stress test and a thematic review of how banks incorporate C&E risks into their processes, a fully-fledged supervisory exercise, involving teams responsible for the day-to-day supervision of banks.

At the same time, we are gradually integrating C&E risks into our regular supervisory methodology, and how banks manage these risks will ultimately impact their Pillar 2 capital requirements.

The ECB’s supervisory actions on climate are part of broader international efforts to advance the supervision and regulation of C&E risks.

At global level, the Basel Committee on Banking Supervision recently concluded a public consultation on draft supervisory principles for the prudential treatment of climate-related risks, and the input they received is now being reviewed with the aim of finalising those supervisory principles.

This is part of a broader workplan of the Committee to evaluate how to consider climate-related financial risks in all pillars of the Basel framework. Supervision, regulation and – the topic of the ECB report that is published this morning – disclosures.

The importance of transparent disclosures

There is growing international awareness of the great value of transparent disclosures. Disclosures that are clear and easy to understand tend to benefit any company, banks included.

Generally, companies have strong incentives to publish frank and meaningful disclosures because transparency is usually rewarded by investors; it helps reduce uncertainty and allows all interested parties to feel they are making safe investments based on trustworthy data.

This is particularly true for climate-related and environmental risks. As the materiality of physical and transition risks increases by the day, investors are on the lookout for those companies that proactively take these risks into account in their daily operations and across all their activities. One of the essential functions of financial markets is to price risk and thus support informed and efficient capital allocation decisions.

The accurate and timely disclosure of current and past operating and financial results is central to this function. To make it concrete: the more transparent banks are about their C&E risk profiles and their concrete efforts to align their portfolios with the Paris Agreement, the easier it is for market participants to compare banks, reward those which are taking the necessary steps to adopt risk management practices aligned with a carbon-neutral economy, and re-evaluate those with misaligned trajectories.

Transparent disclosures also create a certain level of peer and stakeholder pressure, which is essential to making companies properly manage their risks. Investors and asset managers are seeking to develop and market portfolios that are aligned with the sustainability objectives of their own clients. As such, they are becoming increasingly demanding about corporate C&E disclosures.

Banks' own shareholders are becoming increasingly demanding, too, especially concerning banks that have publicly committed to achieving net zero targets. In fact, failure to disclose meaningful follow-up information on their climate commitments has already led to significant litigation and given rise to heightened reputational and legal risks for some banks.

Recent regulatory and legislative initiatives reflect growing international awareness of the great value of transparent disclosures on C&E risks. In Europe, large banks will have to disclose climate-related information under the European Banking Authority's comprehensive implementing technical standards.

They will have to already do so by early 2023, referencing data from the end of 2022. The information requested from banks includes qualitative and quantitative information on environmental, social and governance risks, as well as indicators such as alignment metrics and the green asset ratio – thus significantly raising the bar in terms of C&E risk reporting.

In the same vein, sustainability reporting obligations under the European Commission's Corporate Sustainability Reporting Directive will shortly apply to large corporations, including banks under our direct supervision.

Main findings of the ECB report on banks' progress towards transparently disclosing their C&E risk profile

The ECB is also well aware of the importance of transparent disclosures. We published our first stocktake of banks' C&E disclosures back in November 2020.

We did so precisely to give banks the time and the incentive to improve the quality of their own disclosures in this field. Back then, virtually none of the institutions in the scope of the assessment met our expectations as set out in the ECB Guide on climate-related and environmental risks, which we published at the same time.

The second stocktake, published today, shows that the quality of banks' disclosures has improved since then, especially in the areas of risk management, governance and business models.

However, this improvement has been only marginal: as of 2021, seven in ten banks disclosed information about C&E risk management and governance – compared to five in ten in 2020 -, while only four in ten shared relevant information about the incorporation of C&E risks into their strategic considerations – up from three in ten in 2020. And, all in all, none of the 115 banks directly supervised by the ECB fully meets our supervisory expectations for disclosures.

There is very little justification for this lack of substantial progress, particularly considering the vast amount and quality of climate-related data, tools and information shared by different international and European organisations and institutions in recent years.

The sheer speed at which regulation and metrics are developing in this field should leave no room for any doubt: addressing climate-related and environmental risks, and publishing good-quality disclosures, is not optional. Banks can and must do much better to improve the quality of their disclosures, and they need to do it quickly.

However, we see a considerable disconnect between banks' perception of the importance of C&E risks as communicated to us, the supervisor, and what banks choose to publicly disclose.

Banks are trying to compensate for the poor quality of their disclosures by issuing a great volume of information around green topics.

We end up with a lot of white noise and no real substance on what both markets and supervisors really want to know: how exposed is a bank to C&E risks and what is it doing to manage that exposure? It is of course relevant for banks to publicise their efforts to, for example, reduce the electricity consumption of their branches.

However, it would be much more significant if they were to announce how they are steering their activities towards risk management practices that are aligned with a carbon-neutral economy. Looking at the world through "green-coloured glasses" is not quite the same as a sound management of all material C&E risks.

We also observe a lack of concrete detail in how banks substantiate their climate-related and environmental metrics and targets. For example, when reporting on their commitment to align with the Paris Agreement, only around one in five institutions disclose the methodologies, definitions and criteria for all of the figures, metrics and targets reported as material.

More than one-third of institutions do not disclose these aspects at all. In light of the increasing importance of such commitments, interested parties will increasingly seek information on these alignment metrics – and banks' disclosures must become meaningful in this regard.

Best practices

Like many other institutions and agencies, the ECB is committed to sharing the best practices we have found across the industry. Not only do they serve as inspiration for banks who need to catch up, they also show that the ECB's expectations can, in fact, be met.

For example, one of the banks under our direct supervision published its own climate strategy – which aims at achieving net zero emissions for its lending portfolio by 2050 or sooner – in tandem with a number of (interim) targets and related metrics, as well as the progress made in meeting them. For each of these targets and metrics, the bank discloses the sectors covered, the underlying methodology and the scenarios used to draw up benchmarks.

For the methodologies and scenarios, it reports on the options it chose, the data sources it used and the changes it made with respect to the previous disclosure.

Another bank endeavoured to align its portfolios with science-based transition pathways, including technology pathways originating from the International Energy Agency's "Net Zero by 2050" report.

The bank disclosed dashboards that displayed the performance of its loan books in various transition sectors, such as power generation, oil and gas, automotive, steel, cement and real estate, against a science-based transition pathway. It also disclosed the precise indicators used, the underlying methodologies and the reference scenarios for each indicator.

For each of the indicators, the bank then disclosed its current and projected performance against the pathway and set associated targets.

Importantly, many of the banks raising the bar in C&E disclosures are small and medium-sized – showing that remarkable progress is achievable by all.

Supervisory follow-up

Let me now outline the next steps that the ECB plans to take to follow up on the results of our assessment of banks' C&E disclosures.

We have sent individual feedback letters to all banks under our direct supervision, setting out the key gaps in their disclosures and conveying our explicit expectation that they will take decisive action to address these gaps. In doing so, banks will ultimately ensure that their risk profile is transparently and comprehensively reflected in the information they disclose to the public. Addressing such gaps will also mean banks are well prepared to meet impending technical requirements.

As I mentioned, the consequences of non-compliance with minimum transparency standards are only going to increase for banks, as legal and reputational risks are starting to materialise for banks which fail to step up the quality of their disclosures.

More and more, clients, investors and other market participants want meaningful, comprehensive information on the climate-related actions of their banks. That way, they can make conscious, informed decisions about where their money goes.

Moreover, failing to disclose exposure to risks, including C&E risks, constitutes a breach of the Capital Requirements Regulation.
As such, we stand ready to use the full array of supervisory tools at our disposal to ensure banks' C&E disclosures are up to our standards, and ultimately that eligible banks are prepared for the new regulatory requirements.

The ECB in addition publishes a yearly report on banks' Pillar 3 disclosures, where we also have the option to publicly list those banks which repeatedly fail to disclose their C&E risks.

In view of the poor results shown by our stocktake, and to assess the extent to which the banks address individual feedback, C&E risk disclosures will continue to feature prominently in the ECB's supervision.

We will assess banks' C&E disclosures again at the end of 2022 and we expect to see major progress by then.

Conclusion

Let me conclude. Stricter disclosure regulation is on the way, and time is running out for banks to get ready. Five years have passed since the Task Force on Climate-related Financial Disclosures published its recommendations. There are also many initiatives, some of them open source, to support banks' efforts.

Many companies have improved their disclosures and now provide information that can feed into banks' own disclosure indicators. And for those banks that have systematically fallen behind the ECB's – and the market's – expectations there is only one way forward. It is time for banks to be transparent and comprehensive with their C&E disclosures, so we that by bringing them to light, we can progress from an inconvenient truth towards a desirable outcome – for us and for all future generations.

Let me end where I started: the first step in coming to grips with any inconvenient truth is full disclosure.

From open banking to open finance

Denis Beau, First Deputy Governor of the Bank of France, at the France Payments Forum "The Europe of banking and financial services" – Paris

Technological innovations, changes in demand, the arrival of new players: the changes underway in the financial sector are providing a strong impetus to relax the conditions of access to the market, in order to foster competition and thus encourage the development of new, more efficient and less costly services.

In Europe, in the field of payments, this relaxation has already occurred. The EMD, the PSD1 and finally the PSD2 directives have all resulted in the emergence of more agile players, particularly in terms of data exploitation.

The pressure to open up data now extends to insurance and savings: after open banking, we now speak of open finance. This pressure calls for further adapting the regulatory framework. But what should our guiding principles be?

In the payments sector, the main objective of the directives I mentioned was to reconcile openness and security. While this challenge remains relevant for the transition from open banking to open finance, with digitalisation and the development of the platform economy, we have seen two other challenges emerge: reconciling innovation and integration on the one hand and competition and sovereignty on the other.

How do we at the Banque de France and the ACPR, given our role and experience as a supervisor, plan to address these new challenges? This is what I would like to briefly discuss with you today, after a quick recap of the regulatory framework for open banking and the lessons that can be drawn from it to guide the development of open finance.

Part I: Openness and security

A- As regards the assessment of and lessons learned from the regulatory framework for open banking, I would like to start by recalling:

1- The key principles that governed the sharing of payment data: on the one hand, the creation of appropriate statuses and, on the other, the strengthening of security requirements for access.

The creation of the payment service or electronic money service provider status has fostered the emergence of an open banking ecosystem. The

introduction of an agent status has also contributed to this process, by creating a gradual – proportionate – regulatory framework: it thus allows emerging players to test the suitability of their services with the market under the aegis of a licensed institution, before applying for a license themselves, if necessary.

2 – These developments have led to the rapid growth of Fintechs, drawing on their competitive advantages: speed, agility and responsiveness to customer needs. The increase in the number of licences and authorisations issued by the ACPR illustrates this success: more than half of the 62 electronic money institutions and payment institutions currently in operation were licensed after 2018; the number of agents registered with the ACPR has risen by more than 40% in one year, with almost 3,300 decisions to register agents in 2021.

3- However, the framework established for open banking has its limitations.

First, in terms of the openness of the market: the new service providers remain dependent on traditional institutions, in particular for the opening of a segregated account, which raises questions given the difficulties that many Fintechs encounter in practice in accessing accounts.

In technical terms too. While the use of APIs makes account access more secure, these interfaces must also ensure that new entrants are able to provide their services at a level of quality that is consistent with their business model, as I will discuss later.

B- As part of our supervisory duties, I can draw two lessons from these observations for the development of open finance regulations: one concerns the statuses that are necessary for the opening of the market, and the other concerns the technical means to ensure proper security.

1- While the creation of new statuses would appear to promote the emergence of new business models, we must nevertheless seek to limit unnecessary sources of complexity and, more fundamentally, the risks of regulatory arbitrage. Here are two examples to illustrate my point.

The first concerns the electronic money and payment service activities and the associated risks, which are now very similar. And yet, there are still differences in their prudential and anti-money laundering frameworks.

There are also differences between the competent authorities when it comes to assign innovative payment solutions to regulatory categories.

My second example concerns the draft European MiCA regulation on crypto-asset markets. This draft regulation distinguishes between two kinds

of stablecoins: those intended as investment instruments and backed by baskets of assets, Asset-Referenced Tokens (ART), and tokens for payments, Electronic Money Tokens (EMT), whose requirements are similar to those for electronic money.

This distinction requires vigilance in two respects: first, if they are not subject to the same rules, ARTs should not be able to be used for payment purposes; second, care should be taken to ensure that the regulatory requirements are clearly formulated in order to avoid multiple layers of redundant regulation.

2- The second lesson concerns the technical means to be implemented to reconcile openness and security, and in particular the use of APIs.

Should there be an extension of sharing to other financial data, the PSD2 directive calls for a more explicit definition of shareable data, a clearer allocation of responsibilities for authentication, and the promotion of the use of standardised APIs.

Part II: Innovation and integration

A- Let me now turn to the new challenges posed by the development of open banking and its extension towards open finance. I will start with that of promoting innovation without undermining the integration of the European market.

1- In the area of payments, we face a number of challenges, not least that of exchanges between financial intermediaries

The development of the tokenisation of financial assets could lead to a proliferation of new infrastructures that would no longer be interoperable with each other, leading to a risk of market and liquidity fragmentation.

2- This trade-off between innovation and fragmentation risk is also reflected in the settlement asset itself used in payment chains.

If we take the example of stablecoins, their use for the settlement of tokenised financial assets could undermine the stability and efficiency of settlement transactions for new assets by fragmenting the field of settlement assets.

B- To reduce this risk of fragmentation, we have two levers.

1- The first is cooperation between private players to support the efforts of the public authorities to establish a regulatory framework that is clear, proportionate and flexible enough to take account of rapid changes in the market and innovation.

In this respect, there are certainly lessons to be learned from the framework developed for open banking. For example, the deployment of the APIs I mentioned earlier proved to be more complex than expected due to heterogeneous applications, late developments and the lack of an underlying business model.

In this light, two key principles could guide us. On the one hand, institutional players can act as a catalyst for private initiatives on standardisation.

I am referring in particular to the mandate given to the European Payments Council (EPC) for the creation of a dedicated open finance scheme, the SEPA Payment Account Access Scheme (SPAA).

On the other hand, the debate on open finance should also be an opportunity to push for an improvement in the quality of APIs – i.e. premium APIs – by openly addressing the issue of financial compensation for data providers.

2- The second lever is in the hands of central banks, in the form of new services to financial intermediaries.

This is the aim of the Banque de France's experimentation programme with new technologies. These experiments show, in particular, that a wholesale Central Bank Digital Currency (CBDC) would make it possible not only to maintain but also to promote central bank money as the safest and most liquid settlement asset, while adapting it to changes in demand and thus avoiding the fragmentation of settlement assets.

With this improved security, wholesale settlement through distributed ledger could be optimised in terms of efficiency, cost and traceability, including for cross-border payments, by ensuring interoperability between several CBDCs in different jurisdictions.

Part III: Competition and sovereignty

To conclude, I would like to say a few words about the growing challenges related to competition and sovereignty.

A- In this regard, open finance is a development that must be addressed with caution: while it promises to open up the financial market to new players, it could paradoxically increase its concentration, and compromise our strategic autonomy.

1- Indeed, with the platformisation of the digital economy, companies today aim to rapidly increase their market share in a specific segment and then extend the range of their services in order to build a captive customer base.

Open finance could accelerate this trend, which can already be seen in the payments market, by allowing the exchange and cross-referencing of an ever-increasing volume of data.

This may ultimately prove detrimental to competition. This challenge is particularly acute with the development of BigTechs in the financial services markets, which already have significant market power in the areas of cloud computing, mobile payments or digital identification.

2- Open finance also poses challenges in terms of sovereignty to which we must be attentive.

They primarily occur at the individual level. The increasing volume of data in circulation and its cross-referencing is a considerable challenge for the protection of personal data. Cross-border data flows also complicate the enforcement of regulations and make it more difficult for authorities to act.

Secondly, at the industrial level. Mastering artificial intelligence technologies is now contingent on the quantity and quality of accessible data. It is therefore essential that access to data should not be monopolised by non-European players alone.

Lastly, at the State level, because the concentration of data infrastructures raises concerns about their resilience in the event of an attack. Given the geopolitical risks, these aspects should not be underestimated.

The deployment of tokenised settlement assets across borders would also pose a risk to our monetary sovereignty, if it resulted in the use of stablecoins backed by foreign currencies or CBDCs.

B- To reconcile competition and sovereignty, a "retail" central bank digital currency is obviously a potentially important lever.

1- This was the main aim of the investigation phase launched by the Eurosystem in July last year.

Issuing a retail CBDC, nevertheless, raises a number of operational challenges. In particular because financial intermediaries, including banks, play a key role in the security and financial stability of our monetary and financial system.

Introducing a CBDC must therefore neither result in the conversion of a significant proportion of bank deposits into assets held in CBDCs – in

normal times as well as in times of stress – nor compete with banks in their day-to-day relations with their customers.

These issues need to be addressed by design in the architecture and functionality of a digital euro, for example by introducing holding limits or by promoting an intermediated model.

This is why it is essential that the financial intermediaries, along with the other stakeholders, be properly involved in the investigation phase that we are conducting: an expert advisory group has already been set up at European level, and this consultation will be extended to all stakeholders in the coming months, in particular via the European and French market bodies at our disposal.

2- But other levers will be needed to reconcile competition and sovereignty.

First and foremost, the regulatory lever. Against this backdrop, we welcome two European texts that are currently being finalised

(i) the Digital Operational Resilience Act (DORA), which aims, among other things, to bring critical service providers under the supervision of financial regulators;

(ii) and the Digital Market Act (DMA), which is intended to ensure that service providers have equal access to the hardware and software components of electronic devices.

These competition and sovereignty concerns should also be taken into account in the revision of PSD2.

Secondly, the industrial lever. While our market is and must remain open, it is nonetheless essential to encourage innovation by European players. This is why, in the area of payments, the Banque de France actively supports the EPI2 initiative for a modern European solution.

In conclusion, we can see that the changes taking place in the financial sector offer the prospect of even more accessible, efficient and innovative financial services, while at the same time raising new challenges for both market participants and public authorities.

I am convinced that the only way to meet these challenges is through a multi-faceted approach, with cooperation between public and private players.

That is why the Banque de France is fully committed to promoting innovation within a framework of trust: first, at the level of the regulatory

framework and as a supervisor, then by facilitating private initiatives and mobilising the market, and lastly, as a driver and player in innovation.

Deploying Pseudonymisation Techniques

The case of the Health Sector

As the healthcare domain is attempting to make the most of the evolving technical landscape and adapt the provision of services to fulfil the growing needs of patients in a timely manner, additional cybersecurity and data protection challenges come into play.

The integration of new technologies in already complex IT infrastructures opens up new challenges regarding data protection and cybersecurity.

This is due to the growing need to exchange and share the health related information of individuals among different stakeholders.

It is therefore essential for the entities processing personal data, on the one hand, to collect and further process only data that are necessary for their purposes and, on the other hand, to employ proper organisational and technical measures for the protection of such personal data.

Pseudonymisation is increasingly becoming a key security technique for providing a means that can facilitate personal data processing, while offering strong safeguards for the protection of personal data and thereby safeguarding the rights and freedoms of individuals.

Complementing previous work by ENISA that is relevant, this report demonstrates how pseudonymisation can be deployed in practice to further promote the protection of health data during processing.

Obviously, there is not a single solution on how and when to apply it; in fact different solutions might provide equally good results in specific scenarios, depending on the requirements in terms of protection, utility, scalability, etc.

Pseudonymisation can be a ‘simple’ option to adopt but it can also be comprised of a very complex process, both at technical as well as at organisational levels.

For this reason, defining the goals and objectives of pseudonymisation in each particular case and processing operation is really important.

This report highlights the added value of pseudonymisation in the healthcare sector and demonstrates its applicability through simple but specific use cases.

Complementing relevant ENISA publications in this area, it shows how such techniques can increase the level of protection for personal data being processed in the healthcare domain and will eventually promote and raise awareness on the usability and deployment of such technical measures.

Introduction

Recent decades have witnessed an accelerating pace in the development and adoption of new technologies.

This rapid technological change has also affected the healthcare sector which is going through the digitalisation process and has continuously been adopting new technologies to improve patient care, offer new services focusing on patient-at-home care and even preventive schemes.

The integration of new technologies into already complex IT infrastructures opens up new challenges regarding data protection and cybersecurity as there is an increasing need to exchange and share the health related information of individuals among different stakeholders, in some cases across countries, in order to provide better health services.

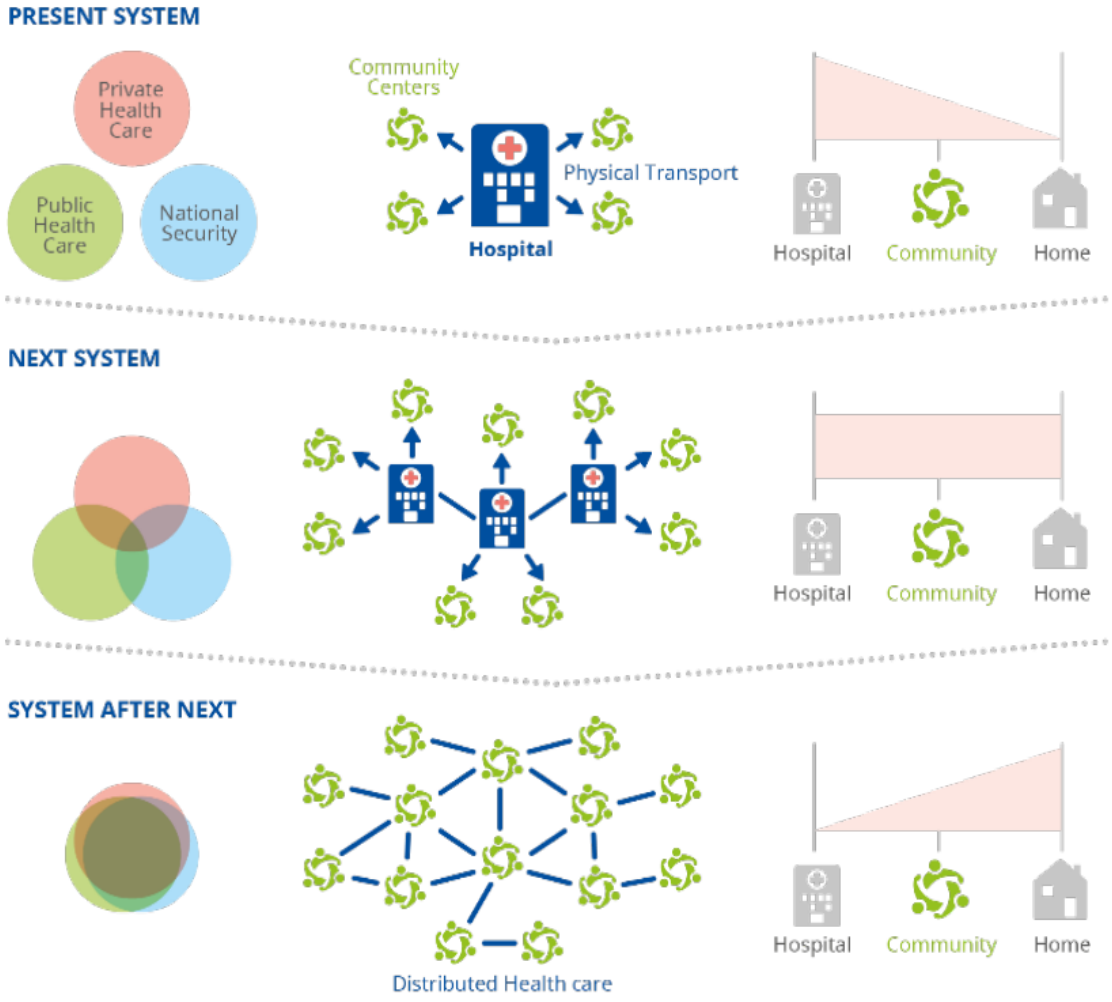
It is therefore essential for the entities processing personal data to collect and further process only data that are necessary for their purposes and, in addition, to employ proper organisational and technical measures for the protection of such data.

Pseudonymisation is one well-known measure that can significantly contribute to this end.

Broadly speaking, pseudonymisation aims at protecting personal data by hiding the identities of individuals in a dataset, e.g. by replacing one or more personal identifiers with the so-called pseudonyms (and appropriately protecting the link between the pseudonyms and the initial identifiers).

This process is not at all new in the design of information systems but gained special attention after the adoption of the General Data Protection Regulation (GDPR), where pseudonymisation is explicitly referred as a technique which can both promote data protection by design (Article 25 GDPR), as well as the security of personal data processing (Article 32 GDPR).

Figure 1: Digital transformation induced shift of value in healthcare [3]



1.1 DIGITAL TRANSFORMATION OF THE HEALTH SECTOR

Health data has always been a valuable source of knowledge in healthcare.

The healthcare domain has historically generated vast amounts of data, both for the treatment of patients and for research and further analysis.

Such processing was mostly performed in paper form but over the last few decades, the accessibility and amount of digitized data has increased massively.

More recently an abundance of new sources of health data occurred as a result of the widespread use of electronic health records, health applications and wearable devices.

Furthermore, advances in computational power have enabled the development of novel data analytics and machine learning techniques that improve diagnostics, treatment and administration in healthcare.

The result is a change in assumptions that is increasingly moving the patient away from hospitalization towards a distributed healthcare system provided by a blend of public and private operators while staying closer to home, as depicted in Figure 1.

To read more:
https://www.enisa.europa.eu/publications/deploying-pseudonymisation-techniques

Variation in the Inflation Experiences of Households

Governor Lael Brainard, at the Spring 2022 Institute Research Conference, Opportunity and Inclusive Growth Institute, Federal Reserve Bank of Minneapolis, Minneapolis, Minnesota

It is a pleasure to join you to discuss differences in how households at different income levels experience inflation. I look forward to hearing from the panelists, who are doing important and interesting research on this topic.

By law, the Federal Reserve is assigned the responsibility to pursue price stability and maximum employment. The Federal Open Market Committee (the Committee) has long recognized the connection between stable, low inflation and maximum employment.

Forty years ago, Paul Volcker noted that the dual mandate isn't an either-or proposition and that runaway inflation "would be the greatest threat to the continuing growth of the economy... and ultimately, to employment."

Maximum employment and stable, low inflation benefit all Americans, but are particularly important for low- and moderate-income families.

The combination of good job opportunities and stable, low inflation provides purchasing power to fill up gas tanks and grocery carts and pay housing and medical costs, leaving room to build emergency cushions and invest in education; retirement; and, for some, small businesses.

Indeed, the Employment Act of 1946 called on the federal government to promote "maximum employment, production, and purchasing power."

While national data do not directly disaggregate the differential effects of inflation by household income groups, a variety of evidence suggests that lower-income households disproportionately feel the burden of high inflation.

Lower-income families expend a greater share of their income on necessities; have smaller financial cushions; and may have less ability to switch to lower-priced alternatives.

Arthur Burns noted in the late 1960s that "there can be little doubt that poor people...are the chief sufferers of inflation."

Today, inflation is very high, particularly for food and gasoline. All Americans are confronting higher prices, but the burden is particularly great for households with more limited resources.

That is why getting inflation down is our most important task, while sustaining a recovery that includes everyone. This is vital to sustaining the purchasing power of American families.

Whose Cost of Living?

In assessing inflation faced by American consumers, economists and policymakers generally rely on the change in the consumer price index (CPI) or the change in the price index for personal consumption expenditures (PCE).

Since January 2012, the Committee's price-stability goal has been specified as a longer-run goal of 2 percent in terms of annual PCE inflation.

Both CPI and PCE inflation metrics are assembled from a collection of underlying elementary price indexes for narrow subsets of goods and services.

The price changes each month for the goods and services in these subsets are combined into measures of overall inflation by calculating a weighted average of all these subindexes, where the weights are based on average aggregate consumer expenditures in each category.

Using a national average of consumer expenditures to weight the categories has intuitive appeal. This measure is particularly useful, for example, in adjusting measures of overall expenditure for changes in prices to determine how much real growth has occurred between two periods.

However, using a national average of expenditures to weight the categories has limitations when it comes to representing the true cost of living experienced by different types of households.

U.S. Households Have Different Inflation Experiences

Each household in the United States has a particular consumption bundle whose prices and quantities combine to make up that household's cost of living.

If we could start with each individual household's cost of living and aggregate across households by giving equal weight to each household, it would create an economy-wide cost-of-living index.

The change in such a cost-of-living index would represent the average inflation experienced by U.S. households.

Instead, because the CPI and PCE indexes weight every dollar of expenditure equally, these indexes implicitly weight each household's cost of living proportionally to their total expenditure.

Since lower-income households represent a relatively smaller share of overall expenditure, the inflation associated with their consumption baskets is underrepresented in the official consumer price indexes.

It would be useful to have data about consumer inflation broken out by demographic groups, similar to labor market and personal-income data, in order to assess the differential effect of inflation across different groups of households.

U.S. statistical agencies do not collect the information needed to accurately assess inflation at a household level, and it would require a large change in the way these agencies go about their work to do so.

Nonetheless, recent research has begun to assess variation in the ways different households experience inflation.

Households at different income levels could experience differential inflation effects for several reasons: Consumption shares could differ systematically for low- and high-income households; the goods and services within each consumption category could differ; the ability to substitute for lower-priced alternatives of the same item could differ; and prices paid for the same good could differ systematically due to differences in access. I will briefly touch on these four reasons.

First, low- and moderate-income households could experience inflation that diverges from the average because their consumption baskets differ systematically from the average.

Lower-income households spend 77 percent of their income on necessities — more than double the 31 percent of income spent by higher-income households on these categories.

Several studies have found that the consumption baskets of lower-income households have experienced higher-than-average inflation rates over time. Research from the Bureau of Labor Statistics (BLS) has examined the effect of different consumption baskets by using the same elementary price indexes as used in the official CPI but assigning the weights of these components to reflect the consumption bundles of different types of households.

A 2021 working paper by BLS staff based on data from 2003 to 2018 found that a price index reflecting the consumption basket for households in the lowest-income quartile grew faster than the overall CPI, while a price index reflecting the consumption basket for households in the highest-income quartile grew more slowly than the overall CPI.

A 2015 BLS study found a similar result using data from 1982 to 2014.

Of course, the recent sharp increases in inflation may have affected the consumption bundles of lower-income households relative to the average differently than in previous cycles.

While these studies allow for differences in the weighting of price indexes across different income groups, they rely on the same elementary price indexes for subcategories of goods and services. As a result, they may miss additional sources of variation in the inflation rates experienced by households at different income levels.

This consideration brings us to the second point: Households with different levels of income may purchase significantly different items even within the same elementary index categories for goods and services.

To take an extreme example, caviar and canned tuna are both in the same elementary index. The demand and supply dynamics for those products are likely quite different, meaning that their relative price dynamics are poorly described by a single index.

Third, households at different income levels may have differing abilities to substitute for lower-priced alternatives within an elementary category.

Consider a price increase for a breakfast cereal that increases the prices of both the brand-name cereal and the corresponding lower-priced store-brand cereal but maintains a differential between them.

A household that had been purchasing brand-name cereal could save money by purchasing store-brand cereal instead, perhaps even eliminating any effect of the price increase on their actual spending while purchasing the same quantity of cereal in that narrow category.
However, a household that was already purchasing the store brand would have to either absorb the increase in cost or consume less within that category.

Finally, beyond the variation in inflation that comes from households buying different goods, research also shows that differences in inflation can result from households paying different prices for identical goods.

Using transaction-level data, researchers found that almost two-thirds of the variation in inflation across households comes from differences in prices paid for identical goods, with only about one-third coming from differences in the mix of goods within broad categories.

As a result of these differences, households with lower incomes, more household members, or older household heads experienced higher inflation on average.

Variations in the prices paid for identical goods could reflect differences in the ability of some households to stock up when prices are discounted or to buy in bulk and save—options only available to households with the means to buy in larger quantities, adequate capacity to store larger quantities, or the flexibility to delay purchases if there is an opportunity to save in the future.

In addition, evidence suggests that inflation could be lower for items purchased online rather than from brick-and-mortar stores, suggesting that households who do not have full access to online shopping options could face a higher cost of living.

One study of online transactions made between 2014 and 2017 found that online inflation averaged more than 1 percentage point per year lower than the equivalent CPI measure of the relevant product categories.

We are only beginning to understand the ways in which inflation experiences vary from household to household, how this variation correlates with income and demographic information, and how these divergent inflation experiences change over time.

This developing area of research will benefit from conferences like this one that help expand the frontier of our knowledge about the heterogeneity of experienced inflation.

Implications for the Outlook and Policy

High inflation places a burden on working families who are concerned about how far their paychecks will stretch as well as seniors living on fixed incomes. So now let me turn briefly to what we are seeing on inflation and the outlook for jobs and growth.

Headline PCE inflation for February came in at 6.4 percent on a 12-month basis. Food and energy account for an outsized one-fourth share of this high level of inflation and also constitute an outsized share of expenditure for lower-income Americans, who spend 26 percent of their income on food at home and transportation, compared with 9 percent for high-income Americans.

Core inflation is also elevated, and inflationary pressures have been broadening out. Housing contributed about one-tenth of total PCE inflation in February and is the single greatest category of expenditures by far for lower-income Americans, who spend 45 percent of their income on housing, compared to 18 percent for high-income Americans.

Durable goods inflation, particularly in autos, accounted for slightly more than one-fifth of total PCE inflation in February, representing a much greater contribution to inflation than was the case pre-pandemic.

High durable goods inflation reflects pandemic-related supply constraints as well as persistently elevated demand associated with the pandemic.

I will be carefully monitoring the extent to which demand rotates back to services and away from durable goods, where it has remained consistently above pre-pandemic levels, and the extent to which the services sector is able to absorb higher demand without generating undue inflationary pressure.

Russia's invasion of Ukraine is a human tragedy and a seismic geopolitical event. The global commodity supply shock associated with Russia's actions skews inflation risks to the upside and is expected to exacerbate high prices for gasoline and food as well as supply chain bottlenecks in goods sectors. The recent COVID lockdowns in China are also likely to extend bottlenecks.

These geopolitical events also pose downside risks to growth. That said, the U.S. economy entered this period of uncertainty with considerable momentum in demand and a strong labor market.

As of the March labor report, payroll employment has increased at a pace of 600,000 jobs per month over the past six months, and the unemployment rate has fallen by a percentage point over that period and is now close to its pre-pandemic level.

In contrast, until recently, the recovery in labor force participation was lagging far behind.

So it is particularly noteworthy to see that the pandemic constraints on labor supply are diminishing for the prime-age workforce: The prime-age participation rate jumped 0.7 percentage points for women in March, following a similar-sized jump for men in February.

An increase in labor supply associated with diminishing pandemic constraints combined with a moderation in demand associated with tightening financial conditions, slowing foreign growth, and a large decrease in fiscal support could be expected to reduce imbalances later in the year.

Against that backdrop, I will turn to policy. It is of paramount importance to get inflation down. Accordingly, the Committee will continue tightening monetary policy methodically through a series of interest rate increases and by starting to reduce the balance sheet at a rapid pace as soon as our May meeting.

Given that the recovery has been considerably stronger and faster than in the previous cycle, I expect the balance sheet to shrink considerably more rapidly than in the previous recovery, with significantly larger caps and a much shorter period to phase in the maximum caps compared with 2017–19.

The reduction in the balance sheet will contribute to monetary policy tightening over and above the expected increases in the policy rate reflected in market pricing and the Committee's Summary of Economic Projections.

I expect the combined effect of rate increases and balance sheet reduction to bring the stance of policy to a more neutral position later this year, with the full extent of additional tightening over time dependent on how the outlook for inflation and employment evolves.

Our communications have resulted in broad market expectations for an expeditious increase in the policy rate toward a neutral level and a more rapid reduction in the balance sheet compared with 2017–19.

Consistent with these expectations, we have already seen significant tightening in market financing conditions at longer maturities, which tend to be most relevant for household and business decisionmaking.

For instance, 30-year mortgage rates have increased more than 100 basis points in just a few months and are now at levels last seen in late 2018. Looking forward, at every meeting, we will have the opportunity to calibrate the appropriate pace of firming through the policy rate to reflect what the incoming data tell us about the outlook and the balance of risks. For today, every indicator of longer-term inflation expectations lies within the range of historical values consistent with our 2 percent target.

On the other side, I am attentive to signals from the yield curve at different horizons and from other data that might suggest increased downside risks to activity. Currently, inflation is much too high and is subject to upside risks.

The Committee is prepared to take stronger action if indicators of inflation and inflation expectations indicate that such action is warranted.

We are committed to bringing inflation back down to its 2 percent target, recognizing that stable low inflation is vital to maintaining a strong economy and a labor market that works for everyone.

Fake WhatsApp 'voice message' emails are spreading malware

National Cyber Security Centre

A phishing campaign which impersonates WhatsApp's voice message feature has been spreading information-stealing malware.

The attack starts with an email claiming to be a notification from WhatsApp of a new private voice message. The email contains a creation date and clip duration for the supposed message, and a 'Play' button.

The identity 'Whatsapp Notifier' masks a real email address belonging to a Russian road safety organisation. As the address and organisation are real, the messages aren't flagged as spam or blocked by email security tools. Armorblox, who discovered the scam, believe the Russian organisation is playing a role without realising.

The 'Play' button will take the email recipient to a website which then asks them to click 'Allow' in an allow/block prompt to 'confirm you are not a robot'. Once 'allow' is clicked, the browser will prompt to install software that turns out to be information-stealing malware.

While there are numerous 'tells' that this is a scam, these attacks rely on people missing the signs – perhaps because they are waiting for urgent or exciting news that could well be delivered by a voice message.

The NCSC has published guidance on how to spot and report scams, including those delivered by email and messaging. You may visit: https://www.ncsc.gov.uk/collection/phishing-scams

GUIDANCE

Phishing: Spot and report scam emails, texts, websites and calls

How to recognise and report emails, texts, websites, adverts or phone calls that you think are trying to scam you.

Our top tips for staying secure online will help you keep your devices and information secure even if you do click on a scam, and you can also learn how to recover a hacked account.

As of March 2022 the NCSC has received over:

11m reported scams

Which has resulted to:

78k scams being removed across 144,000 urls

Capability Assessment for StratCom:

Using the New Risk Perspective to Inform the Development of Effective Response Capability Assessments for Countering Information Influence Operations

There are no established models for assessing an organisation's capability to respond to *information influence operations (IIOs)*.

While great efforts have been made to improve our knowledge and understanding of IIOs and how to counter them, and measures have been taken to strengthen democratic processes and to decrease societal vulnerabilities, few efforts have been made to measure the impact of IIOs or to assess the efficacy of the countermeasures currently in place—the response capability—to mitigate those consequences.

When facing a potential threat, we don't want to just sit and wait for something bad to happen, experience the impact, and only then consider how best to respond.

It is much better to be proactive and seek to develop a response capability that can prevent losses or effectively mitigate the negative impact of an adverse event when it occurs.

To assess whether our response capability is sufficient we must be able to:

1) clearly identify the critical assets we wish to protect, and

2) accurately describe the response we have in place for when those assets are threatened.

Traditionally, 'risk' has been defined as 'a measure of the probability and severity of adverse effects', but recent advancements in risk research have prompted a shift in thinking.

The new perspective on risk management takes into account 'the effect of uncertainty on objectives'.

While these two orientations are largely compatible, incorporating what we know about uncertainties into estimates of response effectiveness rather

than relying on probability calculations results in more robust and flexible capability assessments.

Capability assessments have been a key activity within crisis and emergency management in the last decades.

The purpose of these assessments is to support proactive decision-making concerning resource allocation for response preparedness.

Traditional assessment models—the so-called indicator and index models — equate resources with capability; such assessments provide decision – makers with either a checklist of resources or a numerical representation that evaluates the resources available for a crisis response within a target range for acceptability.

While such models have proven utility in the business world, where production can be (more or less) planned, they are not well suited to crisis and emergency management where uncertainty plays a much larger role.

The new risk perspective addresses this dilemma, suggesting a way forward for an assessment model that takes uncertainties into account, identifies the most effective response tasks and, in the absence of actual feedback and the wisdom of hindsight, provides the best possible information for making decisions regarding investments in capability.

The first part of this report describes response capability assessment—what it is for, what goes into preparing one, and why incorporating the new risk perspective leads to more useful information.

The theoretical explanation will be illustrated with typical examples from the field of risk management concerning residential fires and the response capability of a local fire service.

The second part of the report offers suggestions on how these concepts and ideas might be adapted for responding to IIOs.

The report ends with concluding remarks and a glossary of terms.

To read more:
https://stratcomcoe.org/publications/capability-assessment-for-stratcom-using-the-new-risk-perspective-to-inform-the-development-of-effective-response-capability-assessments-for-countering-information-influence-operations/240

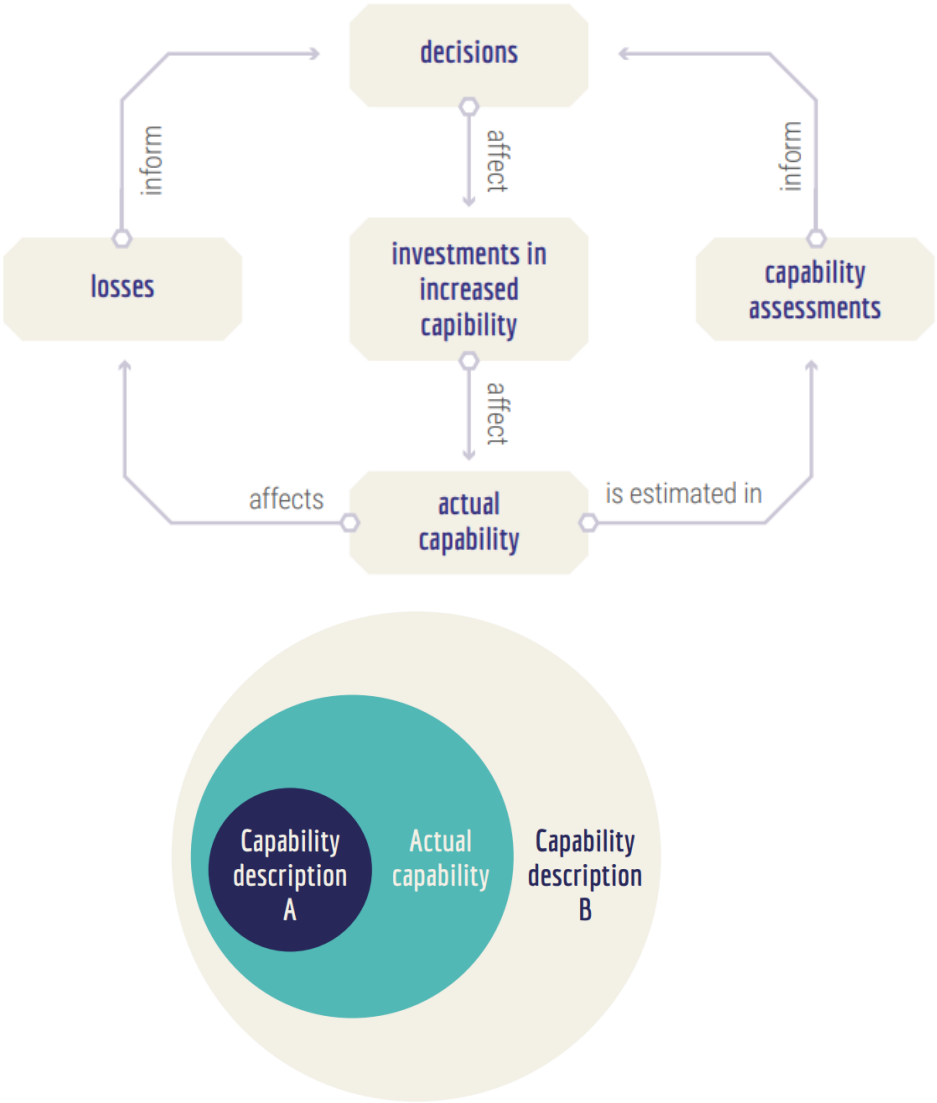


Figure 4. The difference between actual capability and possible descriptions of that capability

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