



## Banking Regulation 2010

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# Sweden

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## Regulatory framework

- 1 What are the principal governmental and regulatory policies that govern the banking sector?

Recent general governmental policy has been that financial institutions must not be specifically regulated, unless such specific regulation is needed. Since regulations could impede competition and reduce effectiveness in the financial system, the Swedish government has stated that it is crucial to confine regulations to areas where it is motivated by an interest that needs to be protected. As a consequence of the recent financial market turmoil, it is however, unclear whether this governmental policy will continue to govern the banking sector. The governmental policy will primarily depend on the actions decided at EU level.

The aim of the Swedish government with current banking regulation is to promote a stable and efficient financial system with a high level of consumer protection and thereby prevent, among other things, banking crises.

The primary areas within the banking sector where the Swedish government has been motivated to take measures are in relation to the payment system, supply of capital and the credit institutions' risk taking.

- 2 Please summarise the primary statutes and regulations that govern the banking industry.

The Swedish banking regulations are to a large extent based upon EC directives, which are implemented mainly through governmental statutes but also through regulations by the Swedish Financial Supervisory Authority (FSA).

The main statute is the Banking and Finance Business Act 2004 (the Banking Act), which lays down fundamental rules regarding the business of credit institutions. The Banking Act contains rules on licence requirements, restrictions on banking activities, cross-border business and supervision, etc. In addition, the FSA has issued several regulations containing detailed rules under the Banking Act. The Banking Act also applies in part to banking business conducted by foreign banking enterprises in Sweden.

Swedish savings banks and membership banks are further regulated by the Savings Banks Act and the Membership Banks Act, respectively.

Other significant statutes and regulations are to be found in the Capital Adequacy and Large Exposures Act implementing Basel II, the Deposit Guarantee Act, the Securities Market Act implementing MiFID, the Act on Measures Against Money Laundering and Financing of Terrorism implementing the third money laundering directive, the Consumer Credit Act, the Foreign Branches Act, the Special Supervision of Financial Conglomerates Act and in relevant regulations that have been issued under the respective act by the FSA.

- 3 Which regulatory authorities are primarily responsible for overseeing banks?

The regulatory authority primarily responsible for overseeing credit institutions is the FSA. The object of the FSA is to promote stability and efficiency in the financial system as well as to ensure effective consumer protection. More specifically, the FSA is responsible for granting licences and supervising credit institutions and other financial institutions. Furthermore, the FSA issues binding regulations as well as non-binding guidelines for credit institutions and other financial institutions, inter alia, with regard to capital adequacy under the Basel II rules, accounting, governance structures risk control and procedures for the prevention of money laundering and terrorism financing. In relation to the Swedish Financial Stabilisation Plan (further described under question 7), the National Debt Office is responsible for administering the Guarantee Programme, the stabilisation fund and potential capital injections to credit institutions. The National Debt Office is also responsible for administering the deposit guarantee scheme. The FSA has also been given the task to monitor the situation in order to check that the benefits arising from the stabilisation programme are also passed on to households and businesses.

In addition, the Central Bank is responsible for monetary policy and aims to maintain price stability and promote a safe and efficient payment system. The Central Bank carries out studies of risks and efficiency regarding the payment system and the use of various instruments of payment, such as cash, card payments and giro transfers. The Central Bank is, however, not a supervisory authority.

- 4 Describe the extent to which deposits are insured by the government.

To implement the regime under the EC Deposit Guarantee Schemes Directive 94/19/EEC, Sweden introduced a deposit-guarantee programme to protect depositors from bankruptcy of a credit institution in Sweden. This was accomplished when the Deposit Guarantee Act entered into force in 1996.

In order to protect Swedish savers, the Swedish government has on two occasions decided to increase the deposit guarantee. On 29 October 2008 the Swedish parliament approved an increase of the guaranteed amount effective from 6 October 2008 under the Swedish deposit guarantee from 250,000 Swedish kronor to 500,000 Swedish kronor. As of 30 June 2009 the guaranteed amount is up to 500,000 Swedish kronor or the higher amount in Swedish kronor corresponding to €50,000. The guaranteed amount can never be lower than 500,000 Swedish kronor, but can be higher depending on the exchange rate of euro to Swedish kronor. Under the state-provided guarantee, the Swedish government will compensate customers for money that they have deposited with banks and certain other institutions if the institution fails. The new guarantee scheme covers all kinds of deposits in accounts, regardless of whether the account is fixed-term or flexible. The guarantee applies both to Swedish credit institutions and to subsidiaries of foreign credit institutions established in Sweden. The programme is financed by the credit

institutions as well as by other financial institutions that have a licence to accept deposits. The yearly fees depend on the amount of deposits, and the relation between a financial institution's capital adequacy ratio and the capital adequacy ratios of other financial institutions. It should be noted that a state commission has proposed a number of changes to the deposit guarantee in order to better protect Swedish depositors and to improve financial stability and, in addition, to implement the amendments of EC Deposit Guarantee Schemes Directive 94/19/EEC presented in October 2008 by the European Commission. It is proposed that the recommended amendments to the Deposit Guarantee Act come into effect on 1 January 2011.

**5** Which legal and regulatory limitations apply to transactions between a bank and its affiliates? What constitutes an 'affiliate' for this purpose?

One of the general principles regarding the business of a credit institution is that its operations shall be organised in such a manner that the institution's structure, connections to other undertakings, and financial position may be assessed. In addition, the FSA has certain powers where a credit institution has close links with any person which prevents effective supervision of the credit institution. One example of such powers is that the FSA may order the holder of shares, which results in the close links, to divest such portion so that no close link continues to exist.

If a credit institution becomes aware of close links with another party, the credit institution must report it to the FSA as soon as possible. As a general rule a credit institution and another party are deemed to have close links if one of the parties involved, directly or indirectly through subsidiaries, owns at least 20 per cent of the shares or can utilise at least 20 per cent of all votes in the other company.

The Banking Act also contains rules on provision of services to persons with a conflict of interest. A credit institution may not agree to provide services on other conditions than those normally applied by the institution or enter into other agreements on conditions that are not commercially justified or to the benefit of certain affiliates, including members of the board of directors of the credit institution, delegates in leading positions who alone or in conjunction with another may decide in credit matters that otherwise are to be decided by the board of directors, and other employees who hold a leading position at the credit institution. It further includes shareholders (other than the state) with a holding corresponding to at least 3 per cent of the capital of the credit institution.

**6** What are the principal regulatory challenges facing the banking industry?

The FSA has declared that the recent financial market turmoil has revealed many of the underlying structural weaknesses of the current regulatory and supervisory arrangements in the EU, especially in relation to supervision and crisis management. In the view of the FSA and the Central Bank, the de Larosière report constitutes a comprehensive and pragmatic proposal to address these weaknesses. One of the regulatory challenges identified by the FSA and the Central Bank, based on the de Larosière report, is to harmonise a set of core rules in the EU, without unjustified national discretions and options. According to the FSA and the Central Bank, there is a need for the European Commission to speedily equip the EU financial sector with a consistent set of core rules. Without a single rule book, supervision of cross-border institutions will not succeed. Their proposal to the Commission is to present a roadmap for regulatory convergence, including definitions of, for example, capital, large exposures, supervisory powers, early interventions, etc.

In a response to the Commission Communication 'An EU framework for Cross-Border Crisis Management in the Banking Sector', the Swedish Ministry of Finance, Central Bank, the FSA and the Swedish National Debt Office has stated that the Swedish

authorities place a high priority on developing the EU framework for cross-border crisis management. In developing an EU framework for cross-border crisis management the priorities are to:

- ensure that authorities in all member states have a minimum set of supervisory tools to intervene early when a bank begins to face problems and if such intervention is not appropriate or sufficient to restore the bank's health, a minimum set of powers to safely resolve a systemic bank failure through winding-up or restructuring;
- ensure that the powers of supervisors and resolution authorities in all member states can be applied in a timely and robust manner proportionate to the severity of the situation, which may require carve-outs in EU as well as national company and insolvency legislation;
- ensure that banks can operate efficiently cross border as credit institutions or as banking groups without discriminating between legal forms;
- facilitate the exchange of information, cooperation and coordination between authorities across borders in both normal times and in times of crisis; and
- develop arrangements for burden-sharing.

**7** How has regulation changed in response to the recent crisis in the banking industry?

The Swedish government and the responsible regulatory authorities (including the FSA, the National Debt Office and the Central Bank) have taken several measures to maintain financial stability so as to limit the repercussions in the Swedish economy.

First (as described under question 4), the Swedish government has widened the deposit guarantee scheme. Secondly, the Swedish government has introduced a Swedish plan for financial stability (Swedish Financial Stabilisation Plan), which is intended to enhance the stability of Sweden's financial system and to address the negative impact of the global financial crisis on the Swedish economy including systematic illiquidity and high borrowing costs. Under the Swedish Financial Stabilisation Plan, the Swedish government is authorised to take a number of measures in support of the financial system, including issuing guarantees and making capital injections to credit institutions. In accordance with the EC Treaty (post Lisbon, the Treaty on the Functioning of the European Union (TFEU)), the Swedish Financial Stabilisation Plan was notified by Sweden to the European Commission pursuant to article 87(3) of the EC Treaty (now article 107(3) TFEU) as state aid (as defined in article 87(1) of the EC Treaty (now article 107(1) TFEU)). On 29 October 2008 the European Commission found the notified measures to be compatible with the Common market and accordingly decided not to raise objections. The Swedish National Debt Office, which is already responsible for administering Sweden's national deposit guarantee, is responsible for administering the Swedish Financial Stabilisation Plan.

In addition to certain specific authorisations and programmes established under the Swedish Financial Stabilisation Plan itself, such as those described below under 'Compulsory Purchase of Shares' and 'The Stabilisation Fund and stabilisation charges', three specific ordinances have been issued by the Swedish government under this plan: a Guarantee Programme, a 2008 Capital Injection Scheme, and a 2009 Capital Injection Scheme, each of which is described below.

#### **The Guarantee Programme**

The Swedish Financial Stabilisation Plan and the ordinance on government guarantees to banks and others provides for the establishment of a guarantee programme (Guarantee Programme). The Guarantee Programme provides banks and major mortgage institutions based in Sweden, as well as certain credit market companies incorporated in Sweden, an opportunity, in exchange for a fee, to contract with the government, represented by the Swedish National Debt Office, for guarantees covering part of their borrowings. The

purpose of the Guarantee Programme is to facilitate borrowings by banks and certain credit market companies and reduce their borrowing costs during the prevailing global financial crisis. In order to obtain a guarantee the applicant must meet certain requirements regarding the composition and size of its capital base.

The guarantee may be applied for in relation to bonds, commercial paper and other debt securities, provided, inter alia, the debt securities have a maturity exceeding 90 days but not five years and are not subordinated. Complex and structured products are not included in the Guarantee Programme. An application under the Guarantee Programme can be made up to and including 30 June 2010, which deadline may be extended if the Swedish government considers this necessary. The maximum amount to be covered under the Guarantee Programme is 1,500 billion Swedish kronor, of which at most 500 billion Swedish kronor may relate to covered bonds having a maturity of between three and five years.

The Guarantee Programme is funded by charges to be paid by the institutions for each loan guaranteed. In order to participate in the Guarantee Programme, an institution must first enter into a guarantee agreement with the Swedish National Debt Office. The institution can then choose to apply for a guarantee for one or more loans. However, the total guaranteed amount for each institution under the Guarantee Programme may not at any time exceed the greater amount of the total amount of maturing debt securities issued by the institution and 20 per cent of the institution's deposits from the public as of 1 September 2008.

The charge for debt securities covered by the Guarantee Programme having a maturity not exceeding one year is 0.5 per cent of the amount guaranteed and the same charge is applied to all institutions. For debt securities with maturities longer than one year, the charge is determined on the basis of the market price for credit default swaps under normal market conditions for each institution plus a margin. The assessment of what may be deemed to comprise 'normal market conditions' shall be based on the conditions prevailing during the period from and including 1 January 2007 up to and including 31 August 2008.

Under the guarantee agreement with the Swedish National Debt Office, the institution must make a number of undertakings, inter alia, undertake not to use or refer to the guarantees issued under the Guarantee Programme in the marketing of credits and accept certain restrictions with respect to wage increases, bonus payments, increases in board remuneration and restrictions with respect to bank executives' severance packages during the guarantee period.

#### **The 2008 Capital Injection Scheme**

In October 2008, the Swedish government put in place measures under the Swedish Financial Stabilisation Plan for making capital injections, under certain circumstances, primarily in exchange for preference shares with strong voting rights (2008 Capital Injection Scheme). The Swedish National Debt Office may under the Swedish Financial Stabilisation Plan and the ordinance concerning government support to credit institutions intervene with capital injections should a financial institution encounter such grave financial difficulties that there is a risk of serious disruption to the Swedish financial system. An institution may obtain support when it is considered that its business is sustainable in the long-term or to facilitate the reconstruction or winding down of an institution that is not considered to be profitable in the long-term. The conditions for the support must be designed so that the institution receiving support and its owners must, in the first instance, bear its losses. The support must be provided on a commercial basis and must not distort competition. Examples of possible interventions are liquidity support, support in connection with acquisitions and capital reinforcement. Furthermore, in order to receive capital under this scheme, the relevant credit institution would have to enter into an agreement with the

Swedish National Debt Office providing for a number of undertakings including:

- not to use or refer to the state support in its marketing of credits;
- to accept certain restrictions with respect to wage increases, bonus payments, increases in board remuneration and restrictions with respect to bank executive's severance packages during the duration of the agreement; and
- not to undergo a significant expansion of operations which would not have taken place if the credit institution had not benefited from governmental support.

#### **Compulsory purchase of shares**

Under the Swedish Financial Stabilisation Plan, the Swedish state has the right to compulsory purchase the shares of a credit institution from its shareholders, including the shares of the issuer, provided it is considered to be of material importance from the perspective of the public and provided:

- the institution or its shareholders have not accepted an agreement proposed by the Swedish National Debt Office which has not been considered unreasonable by an appeal board;
- the institution or its shareholders have not fulfilled an obligation under an agreement under the Swedish Financial Stabilisation Plan which is of material importance; or
- the institution's capital base is below one-fourth of the required capital, calculated as set out in the Swedish act on capital adequacy and large exposures.

#### **The stabilisation fund and stabilisation charges**

The Swedish Financial Stabilisation Plan provides for the establishment of the stabilisation fund in the initial amount of 15 billion Swedish kronor to finance any support measures taken by the Swedish government. The objective is that the stabilisation fund shall comprise an amount equal to an average of 2.5 per cent of Sweden's GDP within 15 years. Apart from the stability charges, guarantee charges under the Guarantee Programme, deposit guarantee charges and recoveries from support measures provided under the Swedish Financial Stabilisation Plan will be transferred to the stabilisation fund.

To strengthen the stabilisation fund, an obligatory stability charge has been introduced by the Swedish government. The stabilisation charges are set at 0.036 per cent of certain parts of the institution's obligations, which is the basis for calculating the stabilisation charge, according to an approved balance sheet. An average of the value of the funding guaranteed by the state under the Guarantee Programme is deducted from the amount forming the basis for calculation of the stabilisation charge. The charge is payable at half the full rate in 2009 and 2010, after which it is raised to the full rate from 2011 onwards. The stability charge is mandatory for all credit institutions and other institutions that are covered by the Swedish Financial Stabilisation Plan. The stabilisation charge for each institution is calculated and decided annually by the Swedish National Debt Office.

#### **The 2009 Capital Injection Scheme**

On 17 February 2009 the Swedish government's ordinance on capital contributions to solvent banks and others, the 'capital injection scheme' (2009 Capital Injection Scheme), came into force. Under the 2009 Capital Injection Scheme, the Swedish National Debt Office may, after obtaining government approval, provide capital injections to institutions covered by the Guarantee Programme. The total limit for this 2009 Capital Injection Scheme is 50 billion Swedish kronor. The capital provided to a particular institution may not result in an increase of the capital adequacy ratio (determined pursuant to the Swedish law on capital adequacy and large exposures) of more than 2 per cent. The injection of capital can be provided in the form of share capital or hybrid capital that may be included in the core capital pursuant to the Swedish law on capital adequacy and large exposures. Capital can be provided through either state participation

in a market transaction, whereby the state acquires a maximum of 70 per cent of the shares or the hybrid debt instruments and the remainder is acquired by other investors; or state participation in a directed issue, whereby the state acquires shares or hybrid debt instruments in the forms of convertibles on terms decided by the Swedish National Debt Office.

In a market transaction, the Swedish National Debt Office participates on the same terms as private investors. In the case of a directed issue, where the state acquires more than 70 per cent, the Swedish National Debt Office will set the price based on a model reflecting the risk of the issuing institution and the returns on similar financial instruments under normal market conditions. The returns must always at least equal the level calculated on the basis of a model provided by the ECB.

Under this scheme, the Swedish National Debt Office will also enter into an agreement with the recipient providing for a number of undertakings, *inter alia*, to not use or refer to the state support in its marketing of credits and to accept certain restrictions with respect to wage increases, bonus payments, increases in board remuneration and restrictions with respect to bank executives' severance packages during 2010 and 2011.

The 2009 Capital Injection Scheme will apply until 17 August 2010 with the possibility for the Swedish government to extend this period if it is necessary.

**8** In what ways do you anticipate the legal and regulatory policy changing over the next few years?

The legal and regulatory policy will likely change due to the recent financial market turmoil and the work at the EU level based on the de Larosière report. As described under question 6, the FSA has declared that the proposals made in the de Larosière report are well in line with the view of the FSA. The FSA has stated that it expects continued regulatory development at the EU level. It should also be noted that the focus of the FSA during the past year has, as a consequence of the recent financial market turmoil, been focused on crisis management rather than review of the regulatory framework. However, the FSA has continued its work to reduce the number of rules and regulations for businesses generally in Sweden with the aim of reducing the administrative burden for such business. It is unclear whether this work will continue.

In addition, depending on how the financial market turmoil develops, it is possible that the Swedish government will propose further changes of the regulatory framework in order to safeguard financial stability.

### Supervision

**9** How are banks supervised by their regulatory authorities? How often do these examinations occur and how extensive are they?

Credit institutions are supervised by the FSA. The supervision includes compliance with statutes, regulations, by-laws, internal instructions of the credit institution, among others. The FSA furthermore supervises the ownership and management of a credit institution.

Credit institutions operating in Sweden are obliged to provide the FSA with such information about their business and related matters as the FSA may require. The FSA is furthermore given the authority by law to perform on-the-spot investigations of credit institutions. The FSA's supervision of credit institutions is subject to the rules provided in the Publicity and Secrecy Act. Thus, the outcome of such investigations may not be disclosed to the public.

The FSA may investigate a credit institution whenever it finds it necessary. However, the FSA's supervision of branches of foreign credit institutions domiciled within the EEA is limited, as a consequence of the principle of home country supervision.

The FSA classifies all companies under its supervision into a

number of categories. Depending on the category and risks involved in the business, the intensity and extent of the supervision by the FSA will vary. For instance, the four largest banking groups on the Swedish market all have the highest level of priority in terms of supervision.

**10** How do the regulatory authorities enforce banking laws and regulations?

The FSA has the authority to intervene if a credit institution neglects its obligations under the Banking Act and other relevant laws and regulations. There are several interventions available. The FSA may issue an order to take action within a specified period, a prohibition to carry out decisions or make an observation.

If the breach is material, the credit institution's licence shall be revoked, or a warning shall be issued if it is deemed sufficient.

If a credit institution has been notified about an observation or warning, the FSA may decide that the institution is to pay a penal charge between 5,000 and 50 million Swedish kronor. However, the penal charge may not exceed 10 per cent of the credit institution's turnover for the previous financial year. The FSA may also impose a conditional fine when issuing an order to take action within a specified period.

The FSA may also convene a meeting of the board of directors of a credit institution and may also request that an extraordinary shareholders' meeting is convened. If the board of directors has not complied with such a request, the FSA may publish a notice to convene the extraordinary meeting. Representatives of the FSA may attend general meetings and at board meetings which the authority has convened and also participate in deliberations.

Moreover, if any entity conducts banking activities without being licensed to do so, the FSA shall order the entity to cease such activities. The FSA may decide how the business is to be wound up.

**11** What are the most common enforcement issues and how have they been addressed by the regulators and the banks?

In 2009, the FSA issued sanctions towards banks in one case. Deficiencies in internal control was one of the grounds upon which the sanctions were issued. This is an area where the FSA in recent years has focused its supervision, mostly in relation to dimension of control functions and assessment of the internal processes of credit institutions.

The enforcement issue came up in June 2009 when the FSA issued sanctions towards the credit market company Finans AB Marginalen and a penal charge of 1.3 million Swedish kronor. The reasons for the sanctions towards the credit market company were, among others, that the credit market company was not fulfilling the requirements regarding management of credits, risk management in relation to credits, deficiencies in the internal control and violation of rules regarding large exposures.

Our recent experience is that the FSA is more likely to address enforcement issues by formal proceedings than informal contacts with the credit institutions. However, if this is a shift in policy by the FSA, it is still to be seen. We would still expect that most enforcement issues are addressed by the FSA and the credit institutions on an informal basis – and if the issue is not resolved formal proceedings may be initiated by the FSA.

**12** How has bank supervision changed in response to the recent crisis?

The bank supervision has not changed materially in response to the recent crisis. However, a change is that the FSA requests more extensive reporting from the credit institutions regarding, for example, exposure towards certain foreign markets and exposure towards large clients. The FSA has also continuously investigated the Swedish credit institutions' ability to handle the financial market turmoil in the Baltic countries. In addition, the FSA has continuously

investigated the Swedish mortgage market and bank lending in terms of ability of borrowers to repay their loans even if interest rates should rise significantly and the loan-to-value ratio rules are applied by banks. The FSA believes that the rising loan-to-value ratios are a cause for concern from a consumer protection standpoint. Even modest price falls on the housing market would mean that the mortgages of a number of households would exceed the market value of the property. It cannot be excluded that the FSA may issue guidelines for Swedish banks during 2010 in respect of the loan-to-value ratio, which may have a significant effect on the Swedish housing market.

The results of the reports have been used by the FSA to inform the Swedish government and the general public about the current situation in the Swedish financial system.

### Capital requirements

- 13** Describe the legal and regulatory capital adequacy requirements for banks.

The Capital Requirements Directive (which comprises the directives 2006/48/EC and 2006/49/EC) is based upon the Basel II framework and imposes new requirements relating to risk and capital management. The directive was implemented into Swedish law through the Capital Adequacy and Large Exposures Act, which entered into force in February 2007.

The rules aim at ensuring that financial institutions hold sufficient capital reserves in relation to the risk that the credit institution is exposed to. Furthermore, the new regime gives financial institutions increased possibilities to decide how to estimate the capital risks.

Due to the wealth of details provided in the Basel II framework and in the Capital Requirements Directive, the Swedish government decided not to stipulate all the rules in the Capital Adequacy and Large Exposures Act, but to commission the FSA to issue regulations for the application of the rules. The most important regulations are laid down in the FSA's regulations and general guidelines regarding capital adequacy and large exposures.

If a bank is part of a 'financial conglomerate', that is, basically a group consisting of both a bank and an insurance company, special rules apply according to the Special Supervision of Financial Conglomerates Act.

- 14** How are the capital adequacy guidelines enforced?

The FSA supervises the application and intervenes in case of breach of the capital adequacy requirements. The form of the supervision or intervention is the same as in question 9.

Thus, credit institutions are supervised by the FSA in accordance with the Banking Act. There are, however, regulations in relation to supervision according to the Capital Adequacy and Large Exposures Act. For example, there are specific regulations regarding financial groups and financial holding companies.

The capital adequacy guidelines are primarily enforced by the requirement on credit institutions to regularly report its own funds and its capital requirements to the FSA.

- 15** What happens in the event that a bank becomes undercapitalised?

As described under question 7, the Swedish government has introduced several measures to maintain financial stability so as to limit the repercussions in the Swedish economy due to the recent financial turmoil. One of these measures is the possibility for credit institutions to participate in the Guarantee Programme that is administered by the National Debt Office. The Swedish government guarantees new borrowings for credit institutions that participate in the programme in exchange for a guarantee fee. The guarantee means that the Swedish government will step in if the credit institution itself is unable to pay.

In addition, the Swedish government has also introduced

capital injection schemes, which are further described in question 7. In addition, if a credit institution becomes undercapitalised and breaches provisions regarding capital requirements in the Capital Adequacy and Large Exposures Act, the FSA may take action according to the Banking Act. For further information about enforcement, see question 11.

- 16** What are the legal and regulatory processes in the event that a bank becomes insolvent?

In order to create stability and confidence in the Swedish financial markets, the Swedish government in October 2008 proposed new legislation that makes it possible for the Swedish government to provide emergency support to a credit institution if it is facing solvency problems that means it is at risk of failure. The purpose is to avoid an institution suspending payments or failing, thus threatening the entire financial system. If the Swedish government provides aid to a credit institution with serious problems, the primary requirement will be state ownership of preference shares. To safeguard taxpayers' interests, the Swedish government may also impose various restrictions on the institution. Besides this special regulation, the same regulations apply to credit institutions as to other companies. General insolvency regulations are primarily to be found in the Insolvency Act. Furthermore, the insolvency process for limited liability companies is regulated in the Companies Act.

If a credit institution has been placed into insolvent liquidation, the FSA shall appoint a general representative. The general representative shall participate in the management of the estate as a trustee together with the trustees appointed pursuant to the Insolvency Act.

- 17** Have capital adequacy guidelines changed, or are they expected to change in the near future?

The FSA are currently working on new regulations regarding liquidity risks. The first regulation, regarding management of liquidity risks for credit institutions and investment firms, is expected to enter into force at the end of 2010. The proposal is in large aspects based upon the Basel committee's recommendations from autumn 2008 (Principles for Sound Liquidity Risk Management and Supervision) and amendments to the EU's capital adequacy directive (2009/11/EC) (especially appendix V). The FSA is also working on new regulations regarding reporting of liquidity risks which are based on the Basel committee's recommendations (International Framework for Liquidity Risk Measurement, standards and monitoring).

### Ownership restrictions and implications

- 18** Describe the legal and regulatory limitations regarding the types of entities and individuals that may own a controlling interest in a bank. What constitutes 'control' for this purpose?

Under Swedish law there are no general limitations regarding the type of entity or individual that may own a controlling interest in a credit institution. The assessment of suitability as described in question 22 should, however, be noted when it comes to owners of a controlling interest.

- 19** Are there any restrictions on foreign ownership of banks?

No, there are no specific restrictions on foreign ownership of credit institutions under Swedish law.

- 20** What are the legal and regulatory implications for entities that control banks?

Previously, a credit institution was only allowed to be a subsidiary company to entities conducting financial business and being under

## Update and trends

### Financial Supervisory Authority introduces new regulations on variable compensation

On 1 January 2010 the FSA introduced new regulations and guidelines on variable compensation. The new regulations and guidelines apply, in principle, to all financial firms that fall under the authority's supervision. With regard to employees whose actions can have a material impact on the firm's risk exposure, companies must apply the regulations and the guidelines to all decisions regarding remuneration for the period before 1 January 2010.

According to the regulations and guidelines, firms must have a remuneration policy that is consistent with good risk management and does not encourage short-term profit and excessive risk-taking. The remuneration policy shall encompass all employees. The new regulation and guidelines provide guidance on how performance should be measured and how risks should be managed when applying variable compensation. The remuneration policy should be subject to regular reviews to ensure that it develops in conjunction with changes to the firm's situation. The firm should base a decision on the design of the remuneration policy on an analysis of how the policy affects the risks to which the firm is exposed and how these risks are managed.

When the firm determines if remuneration shall consist of cash or shares, share-linked instruments or other financial instruments, or a combination of these, the firm should endeavour to encourage long-term value creation and apply a sound risk horizon. In addition, guaranteed variable remuneration should constitute an exception and only be allowed in conjunction with new employment, and then limited to the first year.

The regulations and guidelines clarify the board of directors' responsibility for the firm's remuneration policy and stipulate which information regarding remuneration should be disclosed in conjunction with the annual report.

For employees whose actions can have a material impact on the risk exposure of the firm, at least 60 per cent of the variable remuneration should be deferred for at least three years. In certain circumstances, such as if the firm's position has been significantly weakened, companies may decide to cancel deferred payment, either in part or in whole.

The regulation and guidelines are based on the European Commission's Recommendation K(2009) 3159 governing remuneration policy in the financial services sector. With these regulations and guidelines, the authority has also implemented the global principles for sound remuneration systems which were adopted at the G20 meeting in September 2009.

### The Swedish EU presidency

When Sweden took over the EU presidency in July 2009 the economic and financial affairs of Europe were among the top priorities. The Swedish presidency's three top objectives were to manage the EU's efforts to combat the downturn, to strengthen the financial market supervision and regulation and to restore the long-term sustainability of public finances in the EU member states.

In brief, Sweden achieved, inter alia, the following during its six months of presidency:

- better and increased financial supervision in order to prevent the emergence of new crises through a joint European Systemic Risk Board, set up to monitor the stability of the financial

system. In addition, three new supervisory bodies were created: the European Banking Authority, the European Insurance and Occupational Pensions Authority, and the European Securities and Markets Authority;

- in order to end the inappropriate bonus culture, the member states agreed on new binding European rules governing compensation systems in banks and investment firms. The member states also agreed on new European rules on capital adequacy in order to decrease the possibilities to resell risks and make banks more resilient against losses in hard times;
- creation of a finance policy exit strategy on how to return to healthy public finances and the adoption of excessive deficit procedures in order to establish a process for the way forward; and
- creation of a financial market exit strategy containing clear principles for the phasing-out of support measures for the financial markets with the objective to give healthy banks encouragement to return to a competition market.

### The Payment Services Directive

The Payment Services Directive 2007/64/EC will be implemented into Swedish law during the spring of 2010. The Payment Services Directive aims to guarantee fair and open access to payment markets, increase consumer protection, provide for better protection of the payment market and the creation of a cross-border right of establishment.

The Payment Services Directive will comprise all firms offering payment services and provides a legal framework on how to perform the services as regards mandatory information to clients and conduct of business requirements for payments.

The Payment Services Directive affects firms which offer payment services and their clients. In order to offer payment services a licence from the FSA will be required. In connection with the implementation of the directive a whole new category of firms must apply for such licence. Firms in which the payments during a 12-month period are below €3 million may apply for an exemption from the requirement to have a licence.

### Ownership and management assessments

On 1 July 2009 amendments to regulations governing the ownership and management assessments, carried out by the FSA in applications to conduct financial operations and in acquisitions of shares in companies under FSA's supervision, were implemented.

Before a qualifying holding of shares is acquired, or a company commences licensed operations, an application for a licence shall be submitted to the FSA. Furthermore, the regulations also apply to an acquisition resulting in an increase of a qualified holding to or above 20, 30 or 50 per cent of the share capital or the number of votes of all shares or in the firm becoming a subsidiary.

According to the new regulations, the FSA will grant a licence for acquisition or financial operations if the acquirer is assessed to be suitable and the planned acquisition is financially sound. The assessment will be based on different criteria, of which some are equivalent to the current regulations while others are further developed or completely new. For example, the acquirer's good financial strength and possible connection to money laundering and financing of terrorism will be scrutinised.

the supervision of the FSA or an equivalent foreign authority. Other entities were only permitted to own credit institutions under extraordinary circumstances. This requirement was abolished in 1996 and today non-financial business entities may own a credit institution.

A controlling entity may be affected by the regulations in the Capital Adequacy and Large Exposures Act. The controlling entity and the credit institution might constitute a 'group of financial companies', which would trigger certain requirements that would have implications for the controlling entity. This could for instance mean that a person in the management of the controlling entity is required to have certain experience and also otherwise be suitable for the position.

**21** What are the legal and regulatory duties and responsibilities of an entity or individual that controls a bank?

Any changes in the management of a legal entity that holds a qualified holding in a credit institution must be announced to the FSA as soon as possible. As a result of the EC Directive on Acquisitions in the Financial Sector (2007/44/EC) Sweden has implemented amended legislation on ownership and management assessments of financial companies which entered into force on 1 July 2009. According to the new legislation, a holding is considered as qualified if it constitutes direct or indirect ownership of a company, represents 10 per cent or more of the equity or of all votes or otherwise makes possible a significant influence on the management of the company. The following is an example of what shall be taken into account in the assessment of whether a holding is to be considered as 'qualified':

- shares held by someone other than the acquirer but which grant the acquirer a voting right;

- deposit certificates; and
- shares on which the acquirer may vote by proxy.

The following shall not be included in the assessment:

- shares acquired for the purpose of clearing and liquidating transactions;
- shares held by deposit holders or market guarantors; and
- shares included in the trading stock of investment firms or credit institutions.

Further, owners must refrain from taking certain actions that might harm the credit institution. Accordingly, the Banking Act provides that the FSA may decide that an owner may not represent more shares than an amount that corresponds to a holding that is not qualified if the owner works against, or there is reason to believe that he or she will work against the business of the credit institution being operated in a way compatible with laws and regulations regulating the activity of the institution, if the controlling owner materially neglects his or her responsibilities in business activities or in other financial affairs, or is guilty of serious criminal acts.

If a controlling entity and the credit institution constitute a group of financial companies according to the Capital Adequacy and Large Exposures Act, the controlling entity may become responsible for, among other things, that the whole group of financial companies complies with the capital adequacy requirements.

**22** What are the implications for a controlling entity or individual in the event that a bank becomes insolvent?

There are no specific regulations under Swedish law regarding an owner's responsibility in the event of insolvency of a credit institution. The rules in the Insolvency Act and the Companies Act will apply, for example, regarding any possible liability in damages.

Besides that, one implication could be that the controlling entity or the individual would not be considered suitable in any future owner assessment if that owner applies for approval to acquire shares in another credit institution or financial company (see question 25).

#### Changes in control

**23** Describe the regulatory approvals needed to acquire control of a bank. How is 'control' defined for this purpose?

The Banking Act contains certain restrictions regarding qualified holdings in credit institutions. A direct or indirect acquisition of shares in a credit institution that entails that the acquirer's total holding constitutes a qualified holding (see question 21) may only take place after prior consent has been obtained from the FSA. Such consent must, according to the new legislation regarding ownership assessment, also

be obtained if an acquirer's total possession through an acquisition exceeds 20, 30 or 50 per cent of the equity or of all votes.

**24** Are the regulatory authorities receptive to foreign acquirers? How is the regulatory process different for a foreign acquirer?

The regulatory process is the same for a foreign acquirer as for a Swedish acquirer. Consent may however, only be given after consultation with the competent home state authorities within the EEA if the Swedish credit institution will become a subsidiary to, or otherwise controlled by, a financial institution authorised in such home state following the acquisition. Consultation with the competent foreign authority is also required if the acquirer is the parent company to an entity or person in control of a financial institution authorised in a country within the EEA.

**25** What factors are considered by the relevant regulatory authorities in considering an acquisition of control of a bank?

The fundamental factors to be considered when deciding whether to approve an acquisition are laid down in the Banking Act. As a result of the Acquisition Directive there is a higher degree of harmonisation between the national rules on ownership assessment. The FSA takes several criteria into consideration when performing its ownership assessment in connection with an acquisition that results in a qualified holding (or an increase in a qualified holding) in a credit institution:

- permission will be granted only if the acquirer is deemed to be suitable to have a significant influence over the relevant company and the acquisition is deemed to be economically sound;
- the acquirer's reputation and capital strength (ie, its ability to finance the proposed acquisition and maintain a financially sound structure in the relevant entity) will be considered. Any doubts about the acquirer's integrity and competence, experience, general judgement and compliance with the law will be investigated;
- if the acquirer plans to replace management of the target company upon completion of the proposed transaction, the new management will be subject to management assessment in connection with the ownership assessment. Consequently, information relating to new personell must be submitted to the FSA;
- the FSA must consider whether the proposed transaction involves any risk relating to money-laundering activities. The rule aims to ensure that the money used to purchase shares is not derived from criminal activities and money-laundering activities will not be carried out within the target company after the transaction is completed; and
- the size of the acquirer's holding and the acquirer's impact on the target company after completion of the transaction must also be considered.

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**26** Describe the required filings for an acquisition of control of a bank.

An application for consent to acquire shares in a credit institution shall, according to the Banking Act, be filed with the FSA prior to the acquisition. According to the new legislation regarding ownership assessment, the ownership application must be made to the FSA in writing and the FSA will be required to confirm receipt of the application within two days. The FSA will perform an overall review of the application to ensure that all the requisite documents have been submitted and thus ensure that the application can be deemed complete. The applicant's option to file supplementary information remains.

If the acquirer is a legal entity that has been under the supervision of a foreign regulatory authority within the past year, this must be stated in the application to the FSA.

In addition to the above, merger control may apply under the Competition Act.

**27** What is the typical time frame for regulatory approval for both a domestic and a foreign acquirer?

Upon application, the FSA will, under the new rules, make a decision whether to give consent to an acquirer within 60 days. Should the FSA not render its decision within this time frame, the application will be deemed to have been approved. This time limit applies both to domestic and foreign acquirers. The handling of matters concerning an assessment of foreign acquirers may, due to the consultation of foreign authorities, take longer than an assessment of Swedish acquirers. This does not necessarily mean, however, that such matters concerning an assessment of foreign acquirers will be delayed.



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