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Information on governance in the context of dividend arbitrage schemes, including cum-ex and cum-cum schemes

Introduction and Background

1. On 28 November 2018, the EU Parliament adopted a resolution that included a request to ESMA and the EBA to conduct an inquiry into dividend arbitrage trading schemes such as cum-ex or cum-cum, in order to assess potential threats to the integrity of financial markets and to national budgets; to establish the nature and magnitude of actors in these schemes; to assess whether there were breaches of either national or Union law; to assess the actions taken by financial supervisors in Member States; and to make appropriate recommendations for reform and for action to the competent authorities concerned.
2. Under such schemes investors are aiming at reducing the income taxes to be paid in different ways. In some cases this includes selling and buying shares at a time so that due to the technicalities of the tax schemes and tax refund system the involved parties would not pay income tax or that the tax due would be reduced. In some jurisdictions, both parties receive a certificate about the tax paid at the source, which can be filed for a tax refund, while only one party or no party at all paid the tax. The submission of such wrong tax to receive a refund statements is viewed as tax fraud.
3. Following discussions at the EBA’s Board of Supervisors, preliminary views were sought from AMLC on whether members had identified any cum-ex or cum-cum schemes in their jurisdiction and on whether they had taken, or were thinking of taking, any supervisory action in relation to these schemes. At the time, in December 2018, only few competent authorities were aware of such schemes and some expressed divergent views of the extent to which such schemes were relevant from a supervisory point of view.
4. In May 2019, the AMLC was approached to take stock of the current situation and to understand whether double tax refunds were treated as a tax crime, as handling the proceeds from tax crime might amount to money-laundering by banks. Competent authorities were asked to respond to a questionnaire, which explored the legal status of cum-ex schemes; supervisory measures; coordination between public authorities; a potential role for the EBA; and findings on cum-cum schemes.
5. The AMLC considered that the role of banks in such tax schemes is also relevant for the assessment of the appropriateness of institutions governance arrangements and that “the risk posed by cum-ex schemes is the risk that an institution's internal governance and internal control framework are not sufficiently adequate and effective to manage the risk that the institution, or someone acting on its behalf, commits or facilitates tax crimes”.
6. To allow the EBA to have a deeper understanding of the current situation and prudential concerns, it has now been decided to further inform the analysis by a questionnaire, focusing mainly on governance arrangements that cover the named tax fraud risks and the supervisory measures with regard to such governance aspects. Under Article 74 of Directive 2013/36/EU (CRD) banks must have robust governance arrangements in place. Such arrangements should also ensure that banks are not contributing to the conduct of tax fraud. Failing to have such arrangements in place can trigger operational and compliance risks. Article 85 CRD requires institutions to implement policies and processes to evaluate and manage the exposure to operational risk, which includes internal and external fraud and most relevant in this context the risk of losses caused by circumvention of laws by a third party[[1]](#footnote-2). Shortcomings in the management of such risks would be relevant also for the supervisory assessment of their internal governance arrangements and potentially the suitability of their members of the management body and key function holders if they failed to put appropriate policies and processes in place.
7. In addition to the information requested below, the EBA may use aggregated and anonymised information from the responses received in the context of other reports, including in its response to the European Parliament. Disclosure of information relating to individual competent authorities (e.g. examples of supervisory measures taken) will be discussed with those competent authorities in advance and in due course.
8. Please provide your responses to the questionnaire by **12 August 2019, cob** to governance@eba.europa.eu. In order to answer to the questionnaire it is recommended that the responsible governance experts, i.e. members of the SGGR in liaison with the persons who lead the work under the AMLC or other experts who were involved in the supervisory review of cum-ex schemes as needed.
9. Based on the received information, the prudential concerns and supervisory practices in regard to dividend arbitrage schemes will be analysed. Subsequently, it needs to be seen, if the EBA should issue an opinion to the European Commission on the need for regulatory actions in order to set out clear requirements and responsibilities for preventing such schemes and providing clear expectations regarding the different roles of tax authorities and institutions in this context.

Questionnaire dividend arbitrage schemes

1. Are you aware of any criminal/administrative investigation being carried out by the judiciary or other public authority in your jurisdiction in relation to dividend arbitrage trading schemes, including cum-ex or cum-cum? If so, please describe the main substance and results of the investigations?

The financial commission and the commission of the external affairs of the French parliament lower house (national assembly) have created a common information mission related to tax cross border schemes, the main objective of which is to analyse the texts and the methods of the tax authority to fight cross border schemes and to identify the eventual gaps.

<http://www2.assemblee-nationale.fr/15/commissions-permanentes/commission-des-affaires-etrangeres/missions-d-information/bilan-de-la-lutte-contre-les-montages-transfrontaliers/>

Besides, a complaint was lodged to the national financial prosecution service for aggravated laundering of tax fraud and aggravated fraud by 250 citizens led by a Member of Parliament (the MP ) : <https://ccbo-france.fr/>

1. Has your CA carried out or plans to carry out supervisory reviews/actions to detect tax related operational and compliance risks in the context of dividend arbitrage schemes (see also par 6 of the background) and the active/passive involvement of institutions? If so, can you describe it (onsite/offsite; through the SREP, the fit and proper assessment of members of the management body and key function holders, other processes; scope of institutions covered).

x Yes (Please describe below (box 2a) the named aspects)

☐ No

☐ Other (Please provide additional explanation)

Additional explanations

2a)

The ACPR was aware of dividend arbitrage schemes and the related on-going legal proceedings before the matter was released in the press. As part of the permanent control, 3 main financial institutions had already revealed their involvement, under a form or another, via branches or subsidiaries active in Germany, through supervision interviews.

The financial institutions involved had transmitted their internal audit report on the subject to the ACPR. Those audits were carried out in the wake of legal proceedings opened in Germany regarding operation dealt in the early 2010’s.

The internal investigations led by the financial institutions didn’t highlight that the cum-ex schemes were made for own account. However, several proceedings are still pending in Germany aiming at establishing the responsibility of the financial institutions involved.

In addition ACPR will continue to discuss the matter with the groups involved and follow up on the outcomes potential implication of the tax and/or criminal proceedings opened in Germany.

Finally it could be mentioned that in one case the Cumex issue have impact the 2018 SREP business model and operational risk risk assessment – carried out by the ECB in its role of prudential supervisor of the institution involved – due, in particular, to its potential significant financial implications (through additional taxes claims and/or legal penalties.

If you took supervisory actions, please explicitly explain below (2b) the **prudential grounds** which triggered the above supervisory actions together with the **legal basis** that your NCA has used to carry out such supervisory actions?

2b)

The ACPR has the power and duty to control the application of the *code monétaire et financier (CMF)* by financial institutions and any other provisions of which disregard would lead to a violation of the CMF: [article L 612-1 of the CMF](https://www.legifrance.gouv.fr/affichCodeArticle.do?cidTexte=LEGITEXT000006072026&idArticle=LEGIARTI000006659429&dateTexte=&categorieLien=cid). This grounds includes supervision of AML/CFT, internal control and prudential provisions.

Based on [article L 612-24 of the CMF](https://www.legifrance.gouv.fr/affichCodeArticle.do?idArticle=LEGIARTI000028636121&cidTexte=LEGITEXT000006072026&dateTexte=20140222), the ACPR can collect documents and interview persons as part of its duties.

1. In your reviews under point 2, did you identify specific weaknesses in institutions’ policies and procedures related to compliance with tax laws or related issues?

[ ]  No, institutions in general have appropriate policies in place

X No, institutions in general have appropriate policies in place, but we have observed the need of improvement on certain aspects

[ ]  Yes, institutions do not have, in general, appropriate policies in place and/or material weaknesses have been observed

[ ]  Other (please provide additional explanations)

Please provide additional explanations and main supervisory findings below, as applicable:

3a) Observed strong governance practices regarding dividend arbitrage schemes:

3 b) Observed weaknesses within institutions policies and procedures:

3 c) Weaknesses identified with regard to suitability of members of the management body and key function holders:

3d) Other observed issues:

Concerning one bank, according to the information available to the ACPR, the case highlighted some weaknesses in the internal control and risk management framework, in particular regarding:

 - the formalisation of procedures (no dedicated procedure about KYCs was in place at that time within the local entity),

- the observance of the applicable procedures by the staff

- the effectiveness of new product processes (given the atypical business model of the concerned customers, this should have been examined by a new product committee),

- the monitoring of transactions and the related investigations (given the volume and amount of the transactions, the bank could have performed in-depth analyses, notably as part of the transaction monitoring required by AML regulation).

The on-site inspection mentioned in answer to question 2 will be launched in Q419.

1. Please describe how you cooperated with other competent authorities in the cum-ex context. Did you:

[ ]  Coordinate action, for example joint visits or joint questionnaires (please explain, and include numbers where possible)

[x]  Exchange information, for example in relation to your findings of cross-border banks’ internal controls or risk management processes

[ ]  Issue raised in the context of supervisory colleges

[ ]  Other (Please provide additional explanation)

Additional explanations

The ACPR collaborates with the ECB and the German supervision authority (BundesBank and BAFIN) on the cases mentioned above.

There is no cooperation with the French tax authority on this topic.

1. Please refer also to the definition of operational risk loss event types in Article 324 of Regulation (EU) No. 575/2013 and the BCBS operational risk event types <https://www.bis.org/bcbs/qisoprisknote.pdf> . [↑](#footnote-ref-2)