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Banking Regulation 2022

Andorra: Law & Practice
and
Andorra: Trends & Developments

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ANDORRA

Law and Practice

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1. LEGISLATIVE FRAMEWORK

1.1 Key Laws and Regulations

The financial industry of the Principality of Andorra (Andorra) has historically been a key contributor to the domestic economy. In turn, the banking sector is the cornerstone of the Andorran financial system, which represents roughly 20% of the Andorran Gross Domestic Product and almost 5% of Andorra's wage earners (according to the most recent data published by the Andorran Banking Association).

Due to the country's proximity to neighbouring European countries, along with the signature of the Monetary Agreement in 2011 between Andorra and the EU, the Andorran legal framework is aligned with EU legal initiatives in terms of banking regulation – namely solvency, capital requirements, supervision, investor protection and anti-money laundering and terrorist financing.

The most relevant Andorran regulations governing the banking sector are as follows:

- Law 35/2010 on the legal regime for authorising the creation of new operating entities within the Andorran financial system, dated 3 June 2010;
- Law 7/2013 on the legal regime of the entities operating within the Andorran financial system and other provisions regulating the exercise of financial activities in the Principality of Andorra, dated 9 May 2013;
- Law 8/2013 on the organisational requirements and the operational conditions of entities operating within the financial system, investor protection, market abuse and contractual netting arrangements, dated 9 May 2013;
- Law 10/2008 regulating Andorran collective investment undertakings, dated 12 June 2008;
- Law 10/2013 of the Andorran Financial Authority (AFA), dated 23 May 2013;
- Law 7/2021 of 29 April, regulating the Restructuring and Resolution of Banking Entities and Investment Entities;
- the Memorandum of Understanding (MoU) signed between Andorra and Spain on 4 April 2011;
- Law 20/2018 of 13 September, regulating the Andorran Guarantee Deposit Fund and Andorran Investment Guarantee System (FAGADI Law);
- Law regulating the disciplinary regime of the financial system, dated 27 November 1997 (Disciplinary Law);
- Law 35/2018, on solvency, liquidity and prudential supervision of banking entities and investment firms, dated 20 December 2018;
- Decree approving the accounting framework for entities and collective investment undertakings created under Andorran law operating in the Andorran financial system, dated 22 December 2016;
- Law 14/2017, on the prevention and fight against money or securities laundering and terrorism financing, dated 22 June 2017 (AML Law);
- Regulation for the development of Law 14/2017, 22 June, on the prevention and fight against money or securities laundering and terrorism financing, dated 6 June 2019 (AML Regulation);
- Law 20/2014, regulating electronic contracting and operators which develop their economic activity in a digital space, dated 16 October 2014;
- Law 13/2013, which regulates effective competition and consumer protection, dated 13 June 2013;

- Decree regulating the cessation of payments and insolvency, dated 4 October 1969 (Insolvency Law);
- Law 9/2005, which regulates the Andorran Criminal Code, dated 21 February 2005;
- Law 15/2003 on the protection of personal data, dated 18 December 2003 – note that Regulation (EU) No 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data (GDPR) could have an impact on the transfer of personal data carried out from Andorra due to its extraterritorial scope of application;
- Law 10/2012 on Foreign Investments, dated 21 June 2012 (Law on Foreign Investments);
- Law 19/2016, on International Automatic Exchange of Information in Tax Matters, dated 30 November 2016 (Tax Information Exchange Law); and
- Law 8/2018 on payment and electronic money services, dated 17 May.

The Andorran regulatory and supervisory authorities for the banking sector are as follows.

- The AFA is the regulatory and supervisory authority of the Andorran financial system, and its powers include issuing technical communications and recommendations in order to develop regulations and standards regarding the exercise of banking, financial and insurance activities. The AFA may also adopt the applicable fall-back of international standards for interpretational and prudential supervision purposes. On 17 September 2013, the AFA was accepted as a new ordinary member of the International Organization of Securities Commissions (IOSCO).
- The Andorran Financial Intelligence Unit (UIFAND) is an independent body created to promote and co-ordinate measures to prevent money laundering and terrorist financing. It follows the recommendations of the European Council's Committee of Experts on the Evaluation of Anti-Money Laundering Measures and the Financing of Terrorism (MONEYVAL) and the 40 recommendations from the Financial Action Task Force (FATF).
- The State Agency for the Resolution of Banking Institutions (AREB) is a public institution and is responsible for managing the processes for the winding-up and resolution of banking and investment entities. In turn, the Andorran Fund for the Resolution of Banking Institutions (FAREB) was created for the purpose of financing the measures adopted by the AREB.
- The Andorran Data Protection Agency (APDA), created by Law 15/2003, is a public and independent institution responsible for overseeing compliance with the treatment of personal information provided by individuals, private entities and Andorra's public administration.
- Although not a regulatory authority, the Association of Andorran Banks (ABA) represents the collective interests of all Andorran banking entities. The activity carried out by the ABA is relevant for the banking sector, to the extent that it provides information for its members and the public in general, proposes appropriate recommendations and promotes co-operation among its members.

Lastly, it is also relevant to point out the self-regulation activity carried out historically by banking entities. Likewise, those Andorran banking entities that are, in turn, parent companies of consolidated groups also apply international standards on a self-regulation basis.

2. AUTHORISATION

2.1 Licences and Application Process

Prior authorisation from the AFA is required in order to provide banking activities in Andorra.

Pursuant to Law 7/2013, Andorran banking entities are authorised to render the following financial services:

- deposit-taking, which includes taking deposits and other repayable funds (it must only be rendered by Andorran banking entities);
- granting loans and credits, including consumer credit, mortgage, factoring, with or without recourse, and forfaiting;
- financial leasing and non-financial renting with the option to buy or not;
- the granting of guarantees;
- payment transactions;
- the issuance of means of payment, including credit cards, traveller's checks and bank cheques;
- transactions for own account or on behalf of clients (on money market instruments, exchange markets, foreign exchange and securities);
- the issuance of securities and the provision of related services;
- intermediation in interbank markets;
- commercial reporting; and
- the hiring of security boxes.

Banking entities are also authorised to render the following investment and ancillary services:

- the reception and transmission of orders in relation to one or more financial instruments;
- the execution of clients' orders;
- trading for own account;
- discretionary portfolio management;
- providing investment advice;
- the underwriting of either the issuance or placement of financial instruments;
- the placement of financial instruments on the basis of a firm commitment or otherwise;
- the management of multilateral trading facilities;
- the custody and safekeeping of financial instruments on behalf of clients;
- the granting of credit or loans to an investor to enable him or her to carry out a transaction in one or more financial instruments;
- advising companies on capital structure, strategy and related issues, and providing advice and services on mergers and acquisitions of companies;
- foreign exchange services related to the provision of investment services;
- investment research; and
- services related to underwriting the issue or placing of financial instruments.

The authorisation process for setting up a banking entity in Andorra is governed by Law 35/2010. The submission form must be addressed to the AFA, along with the following documentation:

- the specific features of the banking entity's activity (ie, draft by-laws, the basic programme of activities, a specific statement on the foreseeable activities related to the promotion of the economy at a country level and a specific statement on the prospective provision of activities related to the sponsorship and patronage of educational and cultural activities in Andorra);
- the identification of the shareholders (if they are legal persons, information on the governing bodies must be provided, along with the annual financial statements and audit reports for the last three years, an affidavit on the contributions made by the shareholders to comply with the requirements established by the legislation on anti-money laundering and terrorism financing, the curriculum vitae of shareholders and the members of the governing bodies, and a code of conduct);

- the banking entity's structural, technical and economic forecast (ie, a description of the technical means, organisational and human resources, a detailed description of the activities that are intended to be undertaken within Andorra and those that are to be outsourced abroad, a generic description of the measures that are planned to be implemented to ensure adequate internal control of the procedures, the location of the premises and forecasts regarding the establishment of subsidiaries, branches and offices, the recruitment forecasts for staff during the first three years, indicating qualification levels, balance sheets and P&L for the first three years); and
- evidence of having constituted a deposit of EUR3 million to the AFA. Note that this amount shall be returned to the applicant within 20 working days of the rejection of the application or, if authorised, within 20 working days from the start of the business activity.

Upon submitting this documentation, the AFA has a maximum of six months to notify its decision.

According to the Technical Communication 1/19 issued by the AFA, the submission fee for setting up a banking entity in Andorra is EUR30,995, and the annual supervision fee shall vary according to the banking entity's balance sheet, with a maximum fee of EUR211,470.

3. CONTROL

3.1 Requirements for Acquiring or Increasing Control over a Bank

Changes in the shareholding of a banking entity are subject to the prior authorisation and later registration by the AFA when such changes imply the following:

- that any of the shareholders obtains or acquires a qualified participation;
- regardless of the relevant participation, that any of the shareholders obtains representation on the management body of the entity;
- that any of the shareholders increases the qualified participation to the extent that the percentage of voting rights or share capital is equal to or greater than 20%, 30% or 50%; or
- by virtue of the acquisition, that the entity may be controlled or become a subsidiary.

Qualified shareholding (*participació qualificada*) means any participation that, directly or indirectly, represents 10% or more of the share capital or voting rights of the banking entity. A shareholding is also deemed to be qualified if, without reaching the aforementioned percentage, it allows significant influence to be exercised over the entity. It is presumed that a natural or legal person can exercise a significant influence when, among other things, it has the power to appoint or remove a member of the board of directors.

There are no specific restrictions on foreign ownership applicable to banking entities.

4. SUPERVISION

4.1 Corporate Governance Requirements

Pursuant to Law 8/2013, banking entities must have robust corporate governance arrangements, which include the following:

- a clear organisational structure with well-defined, transparent and consistent lines of responsibility;
- effective processes to identify, manage, monitor and report the risks they are or might be exposed to;

- adequate internal control mechanisms, including sound administration and accounting procedures; and
- remuneration policies and practices that are consistent with and promote sound and effective risk management.

Notwithstanding this, the aforementioned arrangements, processes and mechanisms shall be comprehensive and proportionate to the nature, scale and complexity of the risks inherent in the business model and the entity's activities.

Accordingly, the board of directors of Andorran banking entities is obliged to define its risk appetite and approve the relevant risk management policies and periodically monitor its compliance, and to adopt adequate internal policies and procedures.

As far as organisational requirements are concerned, Andorran banking entities must implement a compliance function, a risk-management function and an internal audit department.

The compliance function is in charge of the supervision, monitoring and verification of the effective compliance with legal provisions and professional standards by employees and financial agents, in order to protect clients and minimise compliance risk. Moreover, in order to guarantee that the compliance function works appropriately, the entities must ensure that they have adequate authority and both technical and human resources, and must appoint a person to be in charge of the compliance function, in addition to avoiding participating economically in the services or activities which they are controlling.

The risk-management function carries out the following activities:

- advising senior management on the management risk policies and the determination of the level of risk tolerance;
- introducing, applying and maintaining management risk procedures; and
- monitoring the measures adopted to reduce or mitigate risk exposure.

The internal audit function is entitled to prepare, on an annual basis, a report establishing its opinion regarding the efficiency and design of the internal control and the risk management systems of the entity. This report is addressed to the management body for its review. A copy of this report must also be addressed to the AFA within the first semester following the closing of the exercise.

Law 8/2013 also establishes as a general principle that banking entities shall take all necessary measures in order to detect and prevent any conflict of interest that may arise during the performance of activities by any employee, director or assistant, which may cause any prejudice to clients.

Additionally, according to the proportionality principle, banking entities may have the following committees:

- audit committee;
- risk committee;
- appointments committee; and
- remuneration committee.

The committees must be composed of members who do not perform executive functions, and the chairpersons must be independent directors.

Law 8/2013 also provides for the possibility of combining the audit and risk committees and

the appointments and remuneration committees, according to the proportionality principle and upon the AFA's authorisation.

Additionally, banking entities must develop adequate procedures to the extent that employees can notify possible infringements internally (ie, whistle-blowing channels). These procedures must guarantee the confidentiality of both the reporting person and the offender.

Technical Communication 163/05, issued by the AFA, highlights some rules on ethics and professional behaviour applicable to Andorran banking entities – namely the prohibition on carrying out own-account operations under identical or better conditions than those of clients to the latter's detriment, and on providing incentives and compensation to clients with relevant influence on the entity.

The Andorran Banking Association published a Code of Conducts in 2017 that reflects the minimum professional standards and recommendations for the banking sector.

4.2 Registration and Oversight of Senior Management

Law 7/2013 sets a limit on the number of directorships that may be held by a member of the management body in a banking entity, taking into account individual circumstances and the nature, scale and complexity of the entity's activities.

In this vein, banking entities may not hold more than one of the following combinations of directorships at the same time:

- one executive directorship with two non-executive directorships; and
- four non-executive directorships.

Moreover, the board members must be persons of recognised commercial and professional honour, and must also possess adequate knowledge and experience in order to exercise their duties.

The requirements of honour, adequate knowledge and experience must also be met by the managing directors, and by those responsible for internal control functions (ie, those in charge of the compliance function, the risk-management function and the internal audit department, as stated in **4.1 Corporate Governance Requirements**).

Prior authorisation by the AFA and subsequent registration is required for every appointment and replacement of directors and those responsible for the internal control functions.

Likewise, banking entities must periodically assess, at least once a year, the continued suitability of their board of directors and of each of its members, as well as of the relevant committees.

4.3 Remuneration Requirements

Remuneration requirements applicable to Andorran banking entities are aligned with European provisions and the guidelines on sound remuneration policies issued by the European Banking Authority (EBA) and the European Securities and Markets Authority (ESMA).

Pursuant to Law 8/2013, banking entities at the group level, parent companies and subsidiaries, including subsidiaries established in third countries (with the exception of foreign subsidiaries located in jurisdictions considered by the AFA to be equivalent for regulatory and supervisory purposes), are obliged to comply with the remuneration requirements set forth in the applicable laws, regulations and technical communications issued by the AFA.

The principles that are applicable to remuneration policies are as follows:

- the remuneration policy should be compatible with a prudent risk management and long-term business strategy;
- the remuneration policy must be compatible with the business strategy and long-term interests of the banking entity, including measures to avoid conflicts of interest;
- the board of directors must adopt and periodically monitor the general principles of the remuneration policy;
- an internal and independent assessment of the implementation of the policy must be carried out at least once a year;
- staff performing control functions must be independent and must have the necessary authority and be remunerated irrespective of the results of the business departments they monitor;
- the remuneration of the general management or those responsible for the risk management and compliance functions should be directly supervised by the remuneration committee or, if this committee is not created, by the board of directors; and
- a clear distinction should be made between fixed and variable remuneration criteria.

In this line, Law 8/2013 also establishes the following ratios between the fixed and variable components of total remuneration:

- the variable component shall not exceed 100% of the fixed component of the total remuneration for each individual; and
- financial entities may allow shareholders to approve a higher maximum level of the ratio between the fixed and variable components of remuneration, provided that the overall level of the variable component does not exceed 200% of the fixed component of the total remuneration for each individual.

Andorran banking entities must follow the inspiring principles when implementing the remuneration policy, including salaries and discretionary retirement benefits for categories of staff including senior management, employees who take risks, those who exercise internal control functions, and any employee who receives a lump-sum payment that includes them in the same scale of remuneration as senior management and other risk-taking employees.

Law 8/2013 also establishes that infringements of these provisions may be sanctioned according to the Disciplinary Law.

5. AML/KYC

5.1 AML and CFT Requirements

Andorra is totally committed to complying with international standards on anti-money laundering and terrorism financing through the implementation of the Fourth Anti-Money Laundering Directive and the FATF's recommendations.

In this vein, both the European provisions and the FATF's recommendations are intended to serve as the backbone of the Andorran system for the prevention of money laundering and terrorism financing.

In turn, the UIFAND is entitled to draw up and publish annual reports and statistics to assess the effectiveness of the Andorran system for the prevention of money laundering and terrorism financing. Additionally, Andorra is periodically subject to the assessments of the Council of Europe, carried out by MONEYVAL.

Banking entities must comply with the following obligations:

- prior to the commencement of the business relationship, the entity must solicit the infor-

mation regarding both the client (and the beneficial owner) and the transaction in order to identify them;
- the banking entity must report to the UIFAND any suspicious transaction that could involve money laundering or terrorism financing;
- information about the identity of the issuer of the suspicious reporting must be kept confidential;
- simplified and enhanced due diligence measures must be applied according to the risk profile of the client, the business relationship, the product or the transaction;
- a clients' admission policy must be drawn up;
- documentation must be kept for at least ten years;
- adequate procedures must be adopted through which to detect unusual or suspicious transactions, with the possibility of submitting a suspicious transaction report to the UIFAND;
- AML-CFT training programmes addressed to employees must be drawn up; and
- an independent external audit must be conducted to verify compliance with AML-CFT provisions, with a copy of the report sent to the UIFAND.

6. DEPOSITOR PROTECTION

6.1 Depositor Protection Regime

FAGADI Law regulates the guarantee system for deposits aligned with Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes. It also states that FAGADI administers the scheme, as well as the relevant limits.

The key regulatory features of the deposit guarantee system are as follows:

- if the insolvency of an Andorran banking entity should occur, the clients' deposits would be repaid up to EUR100,000, and additional coverages are foreseen in exceptional cases that guarantee – up to a limit of EUR300,000 – deposits from real estate transactions of a residential and private nature, payments received by the depositor on a one-off basis and linked to marriage, divorce, retirement, dismissal, disability or death, and those that are based on the payment of insurance benefits or compensation for damages and are the result of a crime or a legal error, provided that these balances have been paid to the covered accounts during the three previous months;
- the FAGADI's ex ante resources must reach 0.8% of guaranteed deposits by 30 June 2024, through the bank's annual contributions;
- the FAGADI will receive the available finance through contributions that its members carry out at least once a year;
- if the FAGADI's available financial resources are not sufficient to reimburse depositors in cases of coverage, the FAGADI board of directors may solicit extraordinary contributions from member entities – these contributions may not exceed 0.5% of their guaranteed deposits per calendar year; and
- the FAGADI board of directors, with prior consent from the AFA, may request higher contributions in exceptional circumstances that in no case imply exceeding the maximum limit of coverage established by the FAGADI Law.

7. BANK SECRECY

7.1 Bank Secrecy Requirements

The Andorran Criminal Law regulates the breach of professional secrecy, whereby a professional discloses or reveals the secrets of an individual,

as a criminal offence punishable by imprisonment of three months to three years and disqualification from the position for up to six years.

Bank secrecy is no longer applicable within Andorra due to the adoption of the international requirements on the exchange of information on tax purposes recommended by the OECD.

Thereupon, three types of exchange of information on tax purposes are regulated in Andorra:

- the exchange of information on request;
- the automatic exchange of information; and
- the spontaneous exchange of information.

8. PRUDENTIAL REGIME

8.1 Capital, Liquidity and Related Risk Control Requirements

Law 35/2018 is aligned with both (i) Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC and (ii) Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012. It requires banking entities to have minimum internal capital that is adequate in quantity, quality and distribution, having regard to the risks to which they are or may be exposed. Accordingly, Andorran banking entities must develop strategies and processes for assessing and maintaining the adequacy of their internal capital.

The amount of capital maintained by banking entities is subdivided as follows:

- Common Equity Tier 1 capital, intended to ensure business continuity;
- Additional Tier 1 capital; and
- Tier 2 capital, intended to cover losses in the event of a liquidation scenario.

As far as the minimum capital requirements are concerned, the total amount of capital required to be held by banking entities must be at least 8% of their risk-weighted assets. The part corresponding to the highest quality capital – Common Equity Tier 1 capital – must represent 4.5% of the risk-weighted assets and 6% of the part corresponding to Tier 1 capital.

Law 35/2018 also introduces the obligation to cover 100% of the liquidity outflows net of liquidity inflows with high liquidity assets, within 30 days and in a stress scenario, such as a major withdrawal of deposits.

Other obligations include the inclusion of intraday operations in the supervision regime, the obligation to develop methodologies to manage the positions of financing, the distinction between pledged assets and unencumbered assets, and the adoption of liquidity recovery plans.

Regarding structural long-term liquidity ratios or stable funding, Andorran provisions require banking entities to cover their long-term liabilities (ie, longer than 12 months) through a variety of stable funding instruments, under both normal and stress conditions. On a quarterly basis and in a single currency, they must also report the elements that require stable financing to the AFA.

Law 35/2018 also includes the obligation to publish the so-called solvency report, which must include the following information:

- data on the financial situation and activity of the banking entity;
- market strategy;
- risk control;
- internal organisation and corporate governance; and
- compliance with the minimum equity requirements laid down in the solvency regulations.

Likewise, banking entities must have policies and processes in place for the identification, management and monitoring of the risk of excessive leverage.

These indicators include the leverage ratio, which is the amount of Tier 1 capital of the entity divided into the total exposure value of the entity, expressed as a percentage. To this extent, the obliged entity shall address the risk of excessive leverage in a precautionary manner by taking due account of potential increases in the risk of excessive leverage caused by reductions of the entity's own funds through expected or realised losses, depending on the applicable accounting rules. Additionally, entities must submit information on the leverage ratio to the AFA, which must monitor the levels of leverage in order to reduce the risk of excessive leverage.

In addition to other own fund requirements, banking entities must hold a capital conservation buffer and a countercyclical capital buffer to ensure that they accumulate a sufficient capital base, during periods of economic growth, to absorb losses in stressed periods. The countercyclical capital buffer should be built up when aggregate growth in credit and other asset classes with a significant impact on the risk profile of such banking entities is judged to be associated with a build-up of system-wide risk, and drawn down during stressed periods.

Note also that Andorran banking entities have implemented IFRS standards with the Decree approving the accounting framework for entities and collective investment undertakings created under Andorran law operating in the Andorran financial system, dated 22 December 2016, which requires entities operating in the Andorran financial system and Andorran collective investment undertakings to prepare their individual and consolidated annual accounts in accordance with the international financial reporting standards adopted by the European Union (IFRS-EU).

9. INSOLVENCY, RECOVERY AND RESOLUTION

9.1 Legal and Regulatory Framework

Law 7/2021 establishes a framework for the recovery and resolution of Andorran banking entities and is extended to investment firms and other financial institutions (with the exclusion of insurance companies); it also regulates the legal status of the resolution authority, the AREB.

This piece of law establishes that a banking entity is under a restructuring situation when it breaches or could breach the applicable liquidity and solvency regulations in the near future, but it is able to comply again with those regulations by its own means.

In such a situation, the bank must give notice to the AFA in order for it to adopt ex officio measures such as a formal requirement to the bank's management body to draft an action plan to redress the situation, the appointment of a special administrator, or the removal of one or more

members of the management body, among others.

If the banking entity cannot redress its stressed situation, the AREB shall assess whether it has to initiate its resolution process.

The resolution process of a banking entity requires the fulfilment of the following requirements:

- it is not financially viable;
- it is reasonably unexpected that it could be redressed by measures from private stakeholders; and
- there are reasons of public interest.

Law 7/2021 entitles the AREB to apply a set catalogue of resolution tools (*instruments de resolució*) and to intervene in a banking entity to ensure continuity in its critical financial and economic functions, while minimising the impact of the banking entity's failure on the Andorran economy and national financial system, and minimising the total resolution costs for taxpayers.

The resolution measures established by Act 7/2021 encompass the sale of business tool, the bridge institution tool, the asset separation tool and the bail-in tool (ie, including the exercise of write-down and conversion powers).

The bail-in tool does not apply to claims insofar as they are secured, collateralised or otherwise guaranteed. Certain kinds of unsecured liability are excluded from the bail-in tool, as covered deposits.

The most relevant provisions of Law 7/2021 are as follows:

- the regulatory requirements cover:
  (a) the draw-up of recovery plans; and
  (b) the calculation of the MREL ratio, as an additional and complementary requirement to capital, liquidity and leverage ratios; and
- a separation of situations involving early temporary measures by the AFA from the resolution phase by the AREB (ie, to this extent the resolution phase is divided into the preventative phase and the execution phase).

In those cases in which the AFA detects any material deficiency in the recovery plans (preliminary phase) drawn up by the institutions, it may require the modification of the plan or the enforcement of the following measures (they are not numerus clausus):

- reduction of the risk profile (eg, liquidity);
- allowing the timely adoption of internal recapitalisation measures;
- reviewing the strategy and structure;
- modifying the funding strategy; or
- introducing changes in its corporate governance system. In any case, the AREB will also have to be informed.

As far as early intervention measures are concerned, Law 7/2021 establishes that the AFA may adopt other measures, which may include the segregation of assets to an asset management company.

Law 7/2021 also sets out the measures that the AREB, in co-ordination with the AFA, may adopt to overcome the obstacles identified in the resolution plans (assessment of the potential resolution of the institution), including:

- a review of funding mechanisms;
- limits on individual and aggregate risks;
- the divestment of specific assets;
- a limit or cessation of certain activities;
- setting up a parent financial holding company; and

- issuing eligible liabilities.

The powers of the AREB include the power to oblige institutions under resolution to adopt effective measures in relation to assets held in third countries, or even to halt the adoption of measures or revoke measures already adopted when they are not effective.

In respect of procedural issues, Law 7/2021 implements the following:

- the introduction of liability against the AREB and its representatives;
- the impossibility of exercising the social action of liability;
- the civil courts are subject to the resolutions handed down by the administrative courts;
- the inadmissibility of the interim suspension;
- the urgent and preferential procedure for the protection of rights and freedoms; and
- the appeal against the decisions and administrative acts issued in matters of amortisation or the conversion of instruments, as well as internal recapitalisation.

Regarding the winding-up regime, the most important aspects are as follows:

- the rules on the priority of claims and loss absorption have the character of special legislation in Andorra;
- the implementation of a new regime regarding the effects of early intervention and resolution processes and applications for a declaration of cessation of payments or insolvency; and
- amendment of the Insolvency Law to include a new regime applicable to entities, covering general privileged credits, ordinary preferential credits (the European standard uses the opposite sense and refers to ordinary non-preferential credits) and subordinated credits, with a clear alignment with EU Directive 2017/2339.

10. HORIZON SCANNING

10.1 Regulatory Developments

Andorran banking entities continuously monitor the most up-to-date, significant developments in banking regulation.

According to the Monetary Agreement, the implementation of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments (MiFID II) and Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories (EMIR) is planned by 2022.

Andorra is also currently negotiating the Association Agreement with the EU.

To this extent, Andorran banking entities face a twofold challenge:

- the regulatory challenge; and
- technological innovation and digital transformation.

As a consequence, the banking industry is facing a substantive transformation of its activity because of the need to renew the provision of its services in the interest of investors and society at large.

Cases & Lacambra is the leading business law firm in the Principality of Andorra. It has a marked international character and focuses on the client, aiming to offer the best comprehensive business law advice to local and international players. The firm has a solid, recognised and highly tested track record in both national and cross-border banking matters, and in the regulation of financial markets, corporate and debt transactions, special situations and asset recovery. It has also had a respected tax practice since 2016. The team is made up of highly qualified professionals, who have very marked methodologies and are orientated to satisfy the needs of the most demanding international institutional and private clients.

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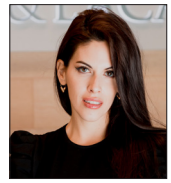

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CASES & LACAMBRA

Trends and Developments

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Challenges Facing the Andorran Banking Industry

The economic openness of the Principality of Andorra (Andorra) has unlocked unprecedented levels of growth and development within the last decades. Upon the signature of the Monetary Agreement with the EU, the Andorran legal framework has been exponentially enriched, but this has presented a challenge to the banking sector within a short period of time.

Along with existing regulations based on European standards and already implemented into local law according to the Monetary Agreement, the following regulatory tsunami scheduled for 2021 and 2022 is extremely burdensome for Andorran banking entities:

- Directive 2014/65 on markets in financial instruments (MiFID II);
- Directive 2018/843 on the prevention of the use of financial system for the purposes of money laundering or terrorist financing (AML 5); and
- Regulation 648/2012 on OTC derivatives, central counterparties and trade repositories (EMIR).

Two recent milestones are also noteworthy:

- the negotiation of the "Association Agreement" with the EU, with the current key area under discussion being the freedom of goods (the conclusion of the negotiations with the EU is expected in two years); and
- the accession to the International Monetary Fund in October 2020 in order to gain access to a lender of last resource, to the extent that there is no Central Bank in Andorra and banking entities have traditionally used foreign correspondents for all kinds of assets.

The regulatory pressure combined with the supervisory activity carried out by the Andorran Financial Authority (AFA), mainly as a result of the new IFRS accounting standard and both the capital and solvency requirements, may slow down the R&D initiatives of banking entities due to the economic and human costs associated.

Notwithstanding this, the Andorran government is actively promoting the use of innovative and disruptive technological tools (ie, digital identity, distributed ledger technologies and artificial intelligence), focusing mainly on digitalisation in both the public sphere and the private sector.

Likewise, Andorran public institutions are working on a large-scale transformation of the Andorran economy to attract new investments, predominantly orientated towards fashionable niche markets such as fintech, eSports and start-ups that develop distributed ledger technologies. In parallel, they are working to further develop new regulations on eSports (Act 8/2021, of 29 April), digital economy (draft bill under Parliamentary discussion) and blockchain/digital assets (draft bill under Parliamentary discussion).

In this emerging scenario, Andorran banking entities may benefit from these new business opportunities, in terms of collaboration agreements entered into with these new players and cost reduction strategies.

The COVID-19 outbreak has also triggered a considerable effort across the Andorran economy, notably for small and medium-sized enter-

prises. The exceptional measures adopted by the Andorran government (ie, financial support) and the proactive approach of the banking sector (ie, promoting telecommuting) are contributing to mitigate the negative impact of the pandemic on the economy and society at large.

Under this scenario of significant instability and high volatility in global capital markets, along with low interest rates, the core banking profitability is falling dramatically. An additional impact related to the health emergency is the increased credit risk of corporate and retail clients of banking entities (ie, those associated with forthcoming insolvency proceedings). Hence, banking entities are called to distinguish between these temporary situations (ie, management or reclassification) and other longer lasting impacts (ie, loan loss provisions) in order to continue financing the real economy.

However, the COVID-19 outbreak has also led to an acceleration of the digital transformation of the banking sector (ie, through partnerships and collaborations within the fintech industry), promoting the offering of an excellent customer experience.

Cases & Lacambra is the leading business law firm in the Principality of Andorra. It has a marked international character and focuses on the client, aiming to offer the best comprehensive business law advice to local and international players. The firm has a solid, recognised and highly tested track record in both national and cross-border banking matters, and in the regulation of financial markets, corporate and debt transactions, special situations and asset recovery. It has also had a respected tax practice since 2016. The team is made up of highly qualified professionals, who have very marked methodologies and are orientated to satisfy the needs of the most demanding international institutional and private clients.

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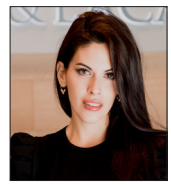

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