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Contributing Editors: **Peter Ch. Hsu & Daniel Flühmann**

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Andorra

Miguel Cases Nabau & Laura Nieto Silvente
Cases & Lacambra

Introduction

The Principality of Andorra ("**Andorra**") is a microstate situated in the southwest of Europe, embedded in the eastern side of the Pyrenees, bordered by Spain and France. Andorra has a unique institutional system headed by two co-princes, the Bishop of Urgell and the President of the French Republic. In 1993, the Constitution was approved by referendum, which allowed Andorra to achieve international recognition and become a member of the United Nations and the Council of Europe. In this sense, Andorra, which is structured into seven administrative regions known as "parishes", established itself as a parliamentary democracy with a Head of Government elected by the General Council, its Parliament and, as mentioned above, with the co-princes as its Head of State.

Andorra has historically based its significant economic prosperity on a competitive model based on tourism, trade, construction and its capacity as a financial hub.

The 2008 financial crisis, which affected the bordering states, was the starting point of a transition from a rather closed tax haven to a competitive, open and low-taxation jurisdiction. The change in the economic model has been accompanied by a new regulatory environment in line with international standards, the liberalisation of foreign investment and human capital and competitiveness.

Therefore, Andorra has opted for a standardisation of the level playing field with other European countries and the recommendations of the Organisation for Economic Co-operation and Development ("**OECD**"), but modulating certain distinctive features in order to enable Andorra to be more competitive in the services it offers, particularly in trade and tourism, and also to enable the country to become one of the most attractive jurisdictions in Europe with respect to the development of investment projects and business initiatives worldwide.

Andorra's new economic model, based on the liberalisation of foreign investment, provides a host of international strategic opportunities at both corporate and individual level, which is complemented by a competitive tax framework and an exceptional living standard.

Andorra has a very strong financial industry, with a local financial system that makes it one of the most relevant financial investment hubs, comparable to Luxembourg or Switzerland. The Andorran financial sector is the backbone of the Andorran economy, its core being the banking sector. To the extent that Andorra has a significant banking sector that operates in close connection with EU member countries, relevant EU banking and financial legislation is in force, such as legislation concerning the prevention of money laundering, terrorist financing and fraud, statistical reporting requirements, and investor protection, among others.

In June 2011, Andorra signed a Monetary Agreement with the European Union. The Monetary Agreement not only recognises the euro as the official currency of Andorra, but

also the right to issue euro coins and the obligation to grant legal tender status to euro banknotes and coins issued by the Eurosystem. The Monetary Agreement represents the cornerstone of the legal changes envisaged for the next 10 years, as it requires Andorra to adopt within certain timeframes a substantial part of all EU financial legislation.

Furthermore, in September 2013, the International Organization of Securities Commissions ("**IOSCO**") protocol for a multilateral agreement on consultations was signed.

To this extent, the Andorran legal system has changed since the Monetary Agreement came into effect on 1 April 2012, as it allowed reciprocal cooperation, assistance and exchange of information at an international level with the regulatory and supervisory authorities of global markets.

Negotiations between Andorra and the European Union for reaching an Association Agreement started in April 2014. At the time of this chapter being drafted, it continues to be negotiated, with some key areas being discussed.

The normal functioning of the Andorran economy needs the Andorran banking sector to be prepared for future challenges, including the supervisory authority and other bodies involved in investment and financing activities in the Andorran jurisdiction. This is a critical point to transform a potential threat into an opportunity to adapt its services and processes to international standards.

Accordingly, Andorran banking entities are continuously monitoring the most up-to-date, significant developments in banking regulation, such as good practice requirements defined by the Basel Committee, and the challenges of ensuring financial and insurance products, corporate governance, among others, with the clear purpose of positioning themselves within the global markets.

The progressive convergence of the Andorran and EU legal framework by means of the Monetary Agreement – which foresees the implementation of the second Markets in Financial Instruments Directive ("**MiFID II**") and the Markets in Financial Instruments Regulation ("**MiFIR**") – will be a tectonic shift from the previous framework in regulatory terms, and will impose increasing regulatory and adaptation costs on Andorran financial entities. On top of that, Andorran financial entities will also be obliged to concentrate significant resources on technological innovation and digital transformation.

In addition to this, the Andorran Government is actively promoting the use of innovative and disruptive technologies. To this extent, the Andorran Government announced in July 2020 the so-called "Horitzó 23", a plan adapted to the new scenario that emerged from the health crisis caused by SARS-CoV-2, known as COVID-19, in order to promote "making Andorra a resilient, sustainable and global country".

In this emerging scenario, Andorran banking entities, predominantly digital, may benefit in terms of collaboration agreements entered into with FinTech entities, the new players, in order to reduce costs and provide more sophisticated services to end investors.

To illustrate this, the following pieces of legislation have been approved or are under Andorran Parliamentary discussion: a draft bill on digital economy and entrepreneurship, which introduces crowdfunding platforms as regulated activities in Andorra; Law 37/2021 of 16 December amending Law 14/2017, which introduces cryptocurrency exchange platforms and custodians as obliged entities; a draft bill introducing Regulation 648/2012 on over-the-counter derivatives, central counterparties and trade repositories ("**EMIR**"); and Law 24/2022 of 30 June on digital representation of assets and cryptography and distributed ledger/blockchain technology.

Regulatory architecture: Overview of banking regulators and key regulations

Andorran banking regulators

Under the Andorran Constitution, the legislative initiative lies jointly with the General Council ("*Consell General*") and the Andorran Government. The General Council exercises legislative power in the Andorran jurisdiction and is composed of 28 general councillors, elected by universal suffrage for a period of four years. By law, the General Council can delegate the exercise of legislative function to the Andorran Government. In case of extreme urgency and necessity, the Government may submit to the General Council a draft articulated text for its approval as a law within 48 hours.

The Andorran Financial Authority ("**AFA**") is the regulatory and supervisory authority of the Andorran financial system; the AFA is granted powers to issue, among others, technical communications and recommendations in order to develop regulations and standards regarding the exercise of banking, financial and insurance activities. Furthermore, its constitutive law grants the AFA the ability to set the applicable fallback of international standards for interpretational and prudential supervision purposes.

As the authority of the Andorran financial system, its functions encompass: (i) promoting and ensuring the functioning of the Andorran financial system; (ii) ensuring the stability and safeguarding the reputation of the Andorran financial system; (iii) ensuring adequate protection of clients and investors; (iv) promoting the competitiveness of the Andorran financial system; and (v) reducing the systemic risk arising from the instability of the financial markets.

In addition, the AFA: (i) has the power to carry out all the actions that are necessary to ensure the correct development of its supervision and control functions to the entities that compose the Andorran financial system (and their consolidated groups); (ii) exercises disciplinary and sanctioning power over these entities; (iii) provides treasury and public debt management services; (iv) manages customer complaints that are submitted to the AFA; (v) is responsible for international relations with central banks and other supervisory authorities; and (vi) submits reports and opinions on financial legislation to the Andorran Government.

On 17 September 2013, the AFA was accepted as a new ordinary member of IOSCO.

There are other bodies involved in financial activities whose functions are not strictly regulatory, but their role is essential for the adequate functioning of the Andorran financial system.

The Andorran Financial Intelligence Unit ("**UIFAND**") is an independent body created to promote and coordinate measures to prevent money laundering and terrorist financing. This unit was created in 2000 under the law for international cooperation on criminal matters and the fight against money laundering arising from international crime, following recommendations of the European Council's MONEYVAL Committee and the 40 recommendations of the Financial Action Task Force ("**FATF**").

UIFAND has the following functions: (i) to manage and promote the activities of prevention and the fight against the use of the financial system for money laundering or terrorist financing; (ii) to issue technical communications; (iii) to request any information or documents to reporting subjects, including Andorran banking entities; (iv) to conduct on-site inspections; (v) to request and receive certificates from the competent judicial authorities for criminal records; (vi) to receive and analyse the statements and all written or oral communications from reporting subjects; (vii) to cooperate with other foreign organisations; (viii) to sanction minor administrative offences; (ix) to submit to the Public Prosecutor all appropriate cases where there are reasonable suspicions of having committed a criminal offence; and (x) to submit proposed regulations to the Andorran Government relating to the fight against money laundering and terrorist financing.

The State Agency for the Resolution of Banking Institutions ("**AREB**") is a public institution created by Law 8/2015 on urgent measures to introduce mechanisms for the recovery and resolution of banking institutions of 2 April. This law attributes to this agency the management of the processes for the winding-up and resolution of banking entities.

The Andorran Fund for the Resolution of Banking Institutions ("**FAREB**") was created for the purpose of financing the measures agreed by the AREB in the application of Law 8/2015. This institution, which does not have legal personality, is managed by the AREB.

The Andorran Data Protection Agency, created by the Andorran Data Protection Act 15/2003 of 18 December 2003, is a public institution that exercises independent authority over the treatment of personal information provided by individuals, private entities and Andorra's Public Administration in order to ensure respect for the fundamental rights of individuals in all automated or manual processes involving an exchange of information.

The Commerce and Consumer Unit ("**UCiC**") is responsible for the development, promotion and implementation of policies in order to improve the Andorran commercial sector as well as the rights and protection of consumers. The UCiC is composed of three specific institutions: the Registry of Commerce; the Commerce and Consumer Affairs Inspectorate; and the Consumer Affairs Service.

The Association of Andorran Banks ("**ABA**") was founded on 11 November 1960. The ABA is an association that represents the collective interests of all its members, the Andorran banking entities, while guaranteeing good banking practices. The ABA provides information for its members and the public in general, proposes appropriate recommendations and promotes cooperation among its members.

Lastly, as Andorran banking entities operate in international markets, the supervision and verification of the origin and destination of funds deposited in the Andorran banking entities are guaranteed by the International Monetary Fund ("**IMF**") and the European Council.

The key legislation or regulations applicable to banks in the Andorran jurisdiction

The Andorran banking system is based on a universal banking model, in which Andorran banking entities offer a complete range of banking services (retail and private banking), asset management, brokering, credit transactions, equity management and other financial services.

Andorran legislation strictly prohibits opaque structures, such as trusts or private foundations, to promote offshore investment structures, which prevent the identification of beneficiaries.

The Andorran legal framework is aligned with neighbouring EU countries and regulates banking and finance issues related to banking entities' regimes, solvency, capital requirements, supervision, anti-money laundering and terrorist financing, and investor protection.

Since the Monetary Agreement was signed between Andorra and the European Union in 2011, Andorra has implemented several European regulations on banking and financial issues. The most important European regulations already transposed to Andorran legislation are the following:

- Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investment in transferable securities.
- Directive 2009/14/EC of the European Parliament and of the Council of 11 March 2009 amending Directive 94/19/EC on deposit guarantee schemes as regards the coverage level and the payout delay.
- Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on financial collateral arrangements.

- Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments and Directive 2006/73/EC of 10 August 2006 implementing Directive 2004/39/EC of the European Parliament and of the Council as regards organisational requirements and operating conditions for investment firms and defined terms for the purposes of that Directive ("**MiFID I**").
- Directive (EU) 2015/849 of the European Parliament and of the Council of 20 May 2015 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing ("**Fourth Money Laundering Directive**").
- Regulation (EU) 2015/847 of the European Parliament and of the Council of 20 May 2015 on information accompanying transfers of funds.
- Directive 2007/64/EC of the European Parliament and of the Council of 13 November 2007 on payment services in the internal market and Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market.
- Directive 2009/110/EC of the European Parliament and of the Council of 16 September 2009 on the taking-up, pursuit and prudential supervision of the business of electronic money institutions.
- Directive 2014/49/EU of the European Parliament and of the Council of 16 April 2014 on deposit guarantee schemes.
- Directive 97/9/EC of the European Parliament and of the Council of 3 March 1997 on investor compensation schemes.
- Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms ("**BRRD**").
- Regulation (EU) 596/2014 of the European Parliament and of the Council of 16 April 2014 on market abuse.
- 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 ("**CRD IV**").
- Regulation (EU) 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) 648/2012 ("**CRR**").
- Directive (EU) 2018/843 of the European Parliament and of the Council of 30 May 2018 amending Directive (EU) 2015/849 on the prevention of the use of the financial system for the purposes of money laundering or terrorist financing ("**AML 5**").

Regime for banking entities

Law 35/2010 on the legal regime for authorising the creation of new operating entities within the Andorran financial system, dated 3 June 2010. This law regulates the legal regime for authorising the creation of new Andorran operating entities.

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. This law sets out the legal regime of entities operating within the financial system and regulates financial activities within Andorra.

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, which was amended by Law 17/2019 of 9 May and fully transposes MiFID I within Andorra. This law establishes: the organisational requirements and operating conditions for the exercise of the activities of

entities operating within the financial system; the minimum requirements to be followed by these entities to safeguard investor protection; the obligations, prohibitions and the penalties system for market abuse; and the regulatory framework of the contractual netting agreements.

In accordance with the aforementioned legislation, the composition of the Andorran financial system is as follows:

- The financial activities regulated and exercised by the entities operating within the Andorran financial system, which are: (i) banking entities; (ii) financial investment entities (financial investment companies, financial investment agencies, asset management companies, financial consultants); (iii) management companies of collective investment undertakings; (iv) non-banking financial institutions, in specialised credit; (v) payment entities ("*entitats de pagament*"); and (vi) electronic money institutions ("*entitats de diner electrònic*").
- Financial agents ("*agents financers*") acting on behalf of any of the entities listed above and Andorran insurance or reinsurance entities ("*entitats asseguradores i reasseguradores*") that are also operating entities in the Andorran financial system.
- The Andorran financial markets.
- Other activities related to the entities operating within the financial system and the Andorran financial markets, including professional associations in the financial sector.

Law 10/2008 regulating Andorran collective investment undertakings, dated 12 June. This law includes the constitution of investment undertakings in Andorra, and regulates their functioning and distribution. Depending on the type of investor, purpose of the vehicle and advertising involved, we can find fully regulated collective investment vehicles to closed alternative investment funds.

Supervision

Law 10/2013 of the Andorran National Institute of Finance, dated 23 May 2013. This law regulates the nature and legal status of the AFA, its objectives, functions, competences and responsibilities, as well as its organisation, the obligation to secrecy and international cooperation. Law 10/2013 was modified in 2018, in order to change the denomination from "INAF" to "AFA". This regulatory body has supervised the Andorran insurance and reinsurance sector since 2018.

Law 7/2021 on recovery and resolution of banking and investment entities, dated 29 April 2021. This piece of legislation is based on the provisions within BRRD. In addition, this law regulates the nature and legal status of the AREB as the competent authority and the FAREB, with the aim of financing the measures agreed by the AREB.

The Memorandum of Understanding ("**MoU**") was signed between Andorra and Spain on 4 April 2011. The MoU: (i) constitutes an agreement for consolidated cooperation in the supervisory framework between the AFA and the Bank of Spain ("*Banco de España*"); (ii) establishes the terms of the protocol for the relationship and collaboration between both authorities; and (iii) enables the supervisory authority of the country of origin to request information of consolidated risks of banking groups from the relevant authority of the country where the entity has subsidiaries.

Financial system

Law 20/2018 of 13 September, regulating the Andorran Guarantee Deposit Fund and Andorran Investment Guarantee System. This law adapts Andorran legislation to the requirements of the European Union and establishes a regime designed to protect the robustness and capital adequacy of the Andorran financial system in relation to the depositors. The maximum amount covered is €100,000 per depositor and €100,000 per investor for each entity (based on an *ex post* guarantee system).

Law regulating the disciplinary regime of the financial system, dated 27 November 1997. This law establishes the disciplinary regime applicable to the entities that compose the Andorran financial system in order to guarantee its stability and solvency.

Law 35/2018 on solvency, liquidity and prudential supervision of banking entities and investment firms, dated 20 December 2018 ("**Capital Adequacy and Solvency Law**"), which implements CRR and CRD IV provisions on prudential, solvency and liquidity requirements. Both pieces of regulation establish the capital adequacy ratio at a minimum of 10%, and the liquidity ratio at a minimum of 100%.

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.

Insurance sector

Law 12/2017 on regulation and supervision of insurances and reinsurances in the Principality of Andorra, dated 22 June 2017 ("**Insurance Law**"). This law establishes the applicable regulation for the Andorran insurance and reinsurance market, with the aim of creating a modern, comprehensive and efficient regulatory framework in order to align its regulatory system with the changes produced in the European regulatory environment, and guarantees challenges to come for the Andorran financial system. Under the Insurance Law, supervision over the Andorran insurance and reinsurance market, jointly with the banking and financial investment sector, will be conducted by the AFA, which emerges as a macroprudential supervisory authority.

International cooperation on criminal issues and anti-money laundering/terrorist financing provisions

Law 14/2017 on the prevention and fight against money or securities laundering and terrorism financing, dated 22 June 2017 ("**AML Law**"). This law establishes procedures to identify customers, adequate procedures and controls to detect suspicious operations arising from organised crime, the training of personnel in specific money laundering prevention programmes, and an external auditor to review the level of anti-money laundering compliance. This law implements the Fourth Money Laundering Directive provisions and the recommendations provided by the FATF to adapt the Andorran legal framework to the latest international standards in these areas. The regulation for development of the AML Law ("**AML Regulation**") was also passed and entered into force on 6 June 2019. Furthermore, Andorra has partially projected the AML 5 provisions.

Law 20/2014, regulating electronic contracting and operators that develop their economic activity in a digital space, dated 16 October 2014. This law: establishes the obligations of operators, the regime of liability of operators and, in particular, providers of brokerage of such services; establishes the regime of electronic commercial communications; and includes provisions regarding extrajudicial conflict resolution and the use of instruments of self-regulation, codes of conduct and guarantees. The aim of this law is to establish a basic legal framework for the development of economic activities in the digital space and electronic contracting, particularly electronic commercial communications, the process of formation and perfection of the contracts, and the conditions for its enforcement.

Law 13/2013, which regulates effective competition and consumer protection, dated 13 June 2013. This law aims to improve conditions for consumer protection and market efficiency, with the ultimate goal of having a system that provides an adequate legal instrument to protect consumers. The provisions regulate antitrust, unfair competition and consumer protection. In the area of antitrust, the objective is to get companies operating independently in the market. Regarding unfair competition, this law seeks to limit unfair and dishonest practices in industrial and commercial fields. In the area of consumer protection, this law intends to modernise the existing regulations in Andorra that will guarantee efficient access to goods and services for citizens.

Decree regulating the cessation of payments and insolvency, dated 4 October 1969, which is the insolvency provision of Andorra. This Decree regulates the premises for the declaration of insolvency, through an arrangement with creditors or the liquidation of the company.

Law 9/2005, which regulates the Andorran Criminal Code, dated 21 February 2005, includes the violation of professional secrecy as a criminal offence and is punished with imprisonment of between three months and three years.

Law 29/2021 on the protection of personal data, dated 28 October 2021, which is intended to guarantee and protect persona data. This law establishes not only general principles applicable to all processing of personal data but also specific requirements governing the collection and processing of data carried out by both public and private entities. Note that Regulation (EU) 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 impact on 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. The aim of this law is to liberalise foreign investment in Andorra. This law removes the previous requirement whereby a local partner had to be authorised prior to investing in any kind of business, corporation or assets located in Andorra. Currently, the only requirement is prior authorisation of the Andorran Government for foreign investments that exceed a 10% stake in a local company. This authorisation is given within 30 days of the application being submitted. There are three requirements to be fulfilled: (i) the partners' identity; (ii) the invested capital; and (iii) the business plan. Its impact on foreign banking entities that aim to set up in the Andorran jurisdiction is related to the fact that prior authorisation of the Andorran Government is needed for its constitution.

Law 19/2016 on international automatic exchange of information in tax matters, dated 30 November 2016 ("**Tax Information Exchange Law**") entered into force in Andorra on 1 January 2017, in order to implement internally the Common Reporting Standard ("**CRS**") approved by the OECD in July 2014 and, especially, the International Protocol executed on 12 February 2016 between the European Union and Andorra introducing the automatic exchange-of-tax-information standard between Andorra and the 27 member countries of the European Union.

The reporting parties under the Tax Information Exchange Law are Andorran financial entities, described by law as follows: (i) banking entities; (ii) investment financial entities; (iii) investment financial agencies; (iv) asset management firms; (v) collective investment management entities – the basic criteria for the exchange of tax information will be based on the tax residence of the owner(s) or person(s) who exercise(s) control over the legal person, or the owner(s) of the current account/deposit account/securities/life insurance "cash value" at the end of each calendar year; and (vi) insurance entities.

The scope of the automatic exchange of tax information is limited by the OECD to financial matters and, therefore, does not affect non-financial assets (e.g. real estate, works of art or precious metals). Therefore, the tax residence must be audited by the compliance departments of the respective financial institutions obliged by the law on 31 December of each calendar year, in order to verify whether an account/person/entity (or controlling persons of entities) is subject to reporting.

The subjective scope of reporting will be as follows: (i) individuals; (ii) individuals controlling entities that are considered non-financial passive investment entities; and (iii) companies carrying out business activities (active entities). The law introduces particularities in relation to non-reportable accounts out of the general CRS/OECD standard (i.e. home-savings accounts and public debt accounts). Moreover, the Tax Information Exchange Law includes an open clause that allows the Andorran Government to exclude in the future other financial accounts that are not relevant according to the spirit of the law and the CRS. In terms of deadlines for the reporting, there are different dates in relation to the amount of the account (major or low-value accounts) and the kind of accountholders that must be reported.

In this regard, the dates are focused on the actual reporting of the financial information to the country of tax residence, but this does not necessarily mean that those are the dates as from when the information will be collected and reported ("cut-off date"): (i) Andorran financial entities had until 30 June 2018 to forward the information of pre-existing accounts owned by individuals of more than US$ 1 million (high-value accounts) to the Government (and the Government reported them for the first time to the tax-residence country in September/October 2018); (ii) Andorran financial entities had until 30 June 2019 to forward pre-existing accounts owned by individuals of less than US$ 1 million (low-value accounts) to the Government (the Government reported them for first time in September/October 2019); and (iii) information of pre-existing, non-financial passive entities, with a balance below US$ 250,000, had to be submitted to the Government before 30 June 2019.

As a consequence of the international cooperation of Andorra towards tax transparency, and particularly the adoption of the standards of the OECD and the execution of multiple International Tax Exchange Agreements, Andorra has been taken off the list of tax havens and blacklists of the OECD and the vast majority of the most relevant and developed jurisdictions.

The last modification of the Tax Information Exchange Law introduced the so-called "wider approach", on whose grounds reporting parties must request each new client to complete the CRS self-certification form.

On 11 June 2015, Andorra ratified the Hague Convention on Private International Law statute, becoming a full member of the Hague Convention.

Lastly, Act 13/2018, enacted on 31 May, created the Andorran Arbitral Tribunal.

The influence of supra-national regulatory regimes or bodies

Pursuant to article 3 of the Andorran Constitution, the universally recognised principles of public international law are incorporated into the Andorran jurisdiction, and the integration of international treaties and agreements shall require their publication in the Official Gazette of Andorra. They have an infra-constitutional and supra-legal status, which means that they are above Andorran laws but are at a lower level than the Constitution.

In addition, the Universal Declaration of Human Rights is also in force in Andorra. As mentioned above, the AFA, within the framework of its regulatory and supervisory activity, applies international standards.

Furthermore, it is worth noting the extraterritorial impact of the common rules within the European Union, including those enacted by non-community authorities and institutions such as EMIR, the US Foreign Account Tax Compliance Act and the GDPR, as indicated above.

Banking activity restrictions

Andorra is not a member of the European Union. Accordingly, the freedom of provision of financial and investment services granted by the European passport does not apply. All financial and investment activities directly carried out within the Andorran jurisdiction: (i) are subject to prior authorisation by the AFA; and (ii) can only be carried out directly by the locally authorised entities that compose the Andorran financial system. However, international firms and investment banks may provide, under very specific circumstances as explained below, wholesale cross-border financial services in the Andorran jurisdiction.

As there is no central bank in the Andorran jurisdiction, financial and investment services rendered by Andorran banking entities have mandatorily required the use of foreign correspondent banks for all kinds of assets. In October 2020, Andorra adhered to the IMF, mainly with the goal of gaining access to a lender of last resort.

Deposit-taking, which includes taking deposits and other repayable funds, is a regulated activity in the Andorran jurisdiction, and it must only be rendered by Andorran banking entities.

Technical communication 163/05, issued by the AFA regarding rules for ethics and behaviour for Andorran banking entities, establishes the prohibition of: (i) carrying out own-account operations under identical or better conditions than those of clients to the latter's detriment; and (ii) providing incentives and compensation to clients with relevant influence on the entity.

Changes to the regulatory architecture

The financial crisis in 2008 did not play a significant role in Andorra, as Andorran financial entities are characterised by their high solvency and liquidity ratios, due to prudent and conservative management that was not highly impacted by the global crisis. Accordingly, no changes were made to the regulatory regime for banks for this purpose.

To the extent that Andorra is a country in evolution and with a clear projection abroad, it has been rapidly and constantly adapting its legislative framework to international standards. Nowadays, Andorra is making a significant effort to bring its legislative framework in line with the European Union, particularly in relation to banking and finance legislation.

Since the Monetary Agreement was agreed by Andorra and the European Union, Andorra became engaged to implement and apply the European provisions set down in the annex to the Monetary Agreement. In fulfilment of this obligation, several European provisions have already been implemented into Andorran law, while others are to be integrated shortly.

Upcoming law projects entering into force shortly include new regulations to provide even higher legal security to foreign investors, and new procedural regulations to provide greater guarantees for creditors and to simplify credit execution procedures.

Over the coming years, Andorra will have to implement provisions for the upcoming implementation of MiFID II. This tremendous shift in the Andorran regulatory landscape, transitioning from a reduced framework to an EU-level playing field, will most likely result in a burdensome process for Andorran financial entities, which face not only an impact on their customer base (e.g. loss of customers due to the entry into force of the CRS regime) but also a direct shock to their profit and loss accounts.

Recent regulatory themes and key regulatory developments

The principal regulatory developments in relation to banks in Andorra focus on the implementation of the commitments contained in the Monetary Agreement (CRR, CRD IV, the Second Payment Services Directive and the Single Euro Payments Area).

Furthermore, the Andorran Government is currently preparing with the AFA a draft of the financial code to combine all Andorran financial laws into a single regulatory body, while amending some aspects to align local financial regulation with the latest international standards.

Bank governance and internal controls

Banking governance key requirements

The number of directorships that may be held by a member of the management body at the same time shall take into account individual circumstances and the nature, scale and complexity of the institution's activities. Notwithstanding the foregoing, and in line with CRD IV, local banking regulation has laid down that banking entities may not hold more than one of the following combinations of directorships at the same time: (a) one executive directorship with two non-executive directorships; and (b) four non-executive directorships.

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

The provisions above also apply to the management companies of collective investment institutions and non-banking financial institutions, with the exception of the minimum number of board members, which in the following cases shall be at least three.

Furthermore, the AFA, as the authority of the Andorran financial system, is bound by specific corporate governance rules. In particular, the AFA, in the exercise of its functions and competences, shall, among others: (i) act in a transparent, autonomous and independent manner; (ii) consider international standards in all matters; (iii) strictly follow corporate governance rules; and (iv) use resources in an efficient way.

The board of directors is also obliged to create commissions that are considered necessary in order to either improve the performance of its powers or to reinforce transparency. In particular, Appointments and Remuneration, Internal Audit, and Risk Committees must be constituted.

Upon the entry into force of CRD IV, Andorra must implement requirements laid down thereof and the Basel Committee on Banking Supervision Guidelines, titled the "Corporate governance principles for banks".

Furthermore, Andorran remuneration policy provisions are in line with the remuneration principles set out in CRD IV and the European Banking Authority guidelines on sound remuneration. Financial entities shall set the appropriate ratios between the fixed and variable components of the total remuneration, whereby the following principles shall apply: (i) the variable component shall not exceed 100% of the fixed component of the total remuneration for each individual; and (ii) financial entities may allow shareholders or owners or members of the institution 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.

Internal controls

Financial entities are obliged to have a compliance function, a risk management function and an internal audit department. In any case, each of them shall act independently from the others.

Firstly, the compliance function is in charge of the supervision, monitoring and verification of the permanent and effective compliance of the legal obligations, ethics and conduct by the employers and financial agents, in order to protect clients and reduce the compliance risk, among others. Moreover, in order to guarantee that the compliance function works appropriately, the entities must ensure that: (i) it is provided with the adequate authority and technical and human resources; (ii) a person in charge of the compliance function has been designated; and (iii) those in charge of the referred function cannot participate in the election of either the controlling services or activities.

Secondly, regarding the risk management function, the law establishes that the entities of the financial system must carry out the following activities: (i) advise senior management relating to the risk management policies and the determination of the level of risk tolerance; (ii) introduce, apply and maintain risk management procedures allowing the identification, evaluation, management, and so on, of the risk management report resulting from the activities of the entity; and (iii) in general, supervise that the measures are suitable regarding the level of risk, and that the entity is complying with the requirements established in the regulations.

Finally, considering the nature, complexity and level of their activity, as well as the risks to which the activities are exposed, financial entities shall have a department that is in charge of the internal auditory function, in order to evaluate and supervise the efficiency of internal controls. When appropriate, the entity shall designate someone working therein in order to make sure that the level of independence is suitable regarding the circumstances of the entity. The internal audit function must prepare, on an annual basis, a report establishing its opinion regarding the efficiency and design of the internal control system and the risk management of the entity. This report is addressed to the directors of the entity for review. A copy of that report must also be addressed to the AFA within the first semester following the closing of the exercise.

Regarding the management policy of conflicts of interest, article 13 of Law 8/2013 establishes as a general principle that any entity operating within the financial system shall take all the necessary measures in order to detect and prevent any conflict of interest that may arise during the performance of the activities by any employer, director or assistant, and that may cause any prejudice to a client. Accordingly, the entities must adopt in writing both the policy and proceedings on the prevention and solution of the conflict of interest, considering the organisation, volume and complexity of the provided activities.

The areas or departments of the entity involving activities with securities or financial instruments shall remain separated in order to ensure that activities are pursued autonomously to prevent any conflict of interest, and to avoid undue transmission of privileged information. Activities relating to managing their own or third-party portfolios will be carried out in separate departments.

Outsourcing of functions

As contemplated in article 8 of Law 8/2013, the outsourcing of functions needs previous authorisation by the AFA, and the adoption by the financial entity of as many measures as appropriate in order to avoid increasing its operational risk. Under no circumstances may the outsourcing of a function result in an exclusion of liability by those financial entities operating within the Andorran financial sector.

Bank capital requirements

On 20 December 2018, the General Council approved the Capital Adequacy and Solvency Law implementing CRD IV and, on 6 March 2019, the regulation of the Capital Adequacy and Solvency Law, which implements CRR in the jurisdiction.

The Capital Adequacy and Solvency Law establishes the capital adequacy ratio at a minimum of 10%, and the liquidity ratio at a minimum of 100%.

Additionally, in order to fulfil the obligations, Andorran banking entities must maintain a reserve to fulfil the covered guarantees, and an amount equivalent to this reserve must be invested in secure and liquid assets that fulfil a series of requirements established by the law for this purpose.

The regulatory capital and liquidity requirements derive from the application of Basel III provisions.

Rules governing banks' relationships with their customers and other third parties

Banking and investment services rendered within the Andorran jurisdiction

Banking and investment activities are basically regulated by Law 7/2013 and Law 8/2013, which cover the organisational requirements and operating conditions of the operating entities in the Andorran financial system, investor protection, market abuse and financial securities agreements.

Under Andorran law, all banking and investment activities rendered inside the jurisdiction can only be carried out directly, with the limitations and conditions set forth in the laws, by the locally authorised entities that compose the Andorran financial system.

From a regulatory point of view, banking and investment activities in Andorra are subject to local licensing requirements, which apply to deposit-taking activities, lending activities, investment services and proprietary trading activities. While deposit-taking activities can only be performed by duly authorised banking entities, specialised credit institutions are allowed to carry out lending activities and investment services, and proprietary trading activities can be rendered by any investment financial entity.

Customers' protection provisions

Banks' dealings with third parties are expressly regulated in Law 8/2013, as are the rules for ethical behaviour in the Andorran financial system, which explicitly defines the duties to be complied with by entities integrated in the financial system. This regulation ensures a full and correct transposition of MiFID I, seeks to maintain and strengthen certain ethical and behavioural principles, and prohibits certain practices that are actively combatted internationally.

According to Andorran legislation, a retail investor/client is any individual or legal person other than a professional investor/client. A professional investor is a client who possesses the experience, knowledge and expertise to make its own investment decisions and to properly assess the risks incurred.

Additionally, general provisions on consumer protection established in Law 13/2013, which guide principles on the rights of consumption, basic rights of consumers, regulatory requirements common to all consumer relations, the offences and sanctions regime and administrative protection of the consumer, apply to banks' dealings with third parties.

According to Law 8/2013, financial entities must establish, implement and maintain effective and transparent procedures to allow a reasonable and swift treatment of claims

filed by customers or potential customers, and must keep a record of each complaint and the resolution measures adopted.

Additionally, any individual or legal person being a client of a bank or financial institution supervised by the AFA, and wanting to make a complaint related to any such supervised entities, may present a complaint to this authority. Before filing a complaint within the AFA, the client and/or claimant must have filed the related claim directly to the bank or financial institution.

If no reply is received from the entity within a reasonable time since the client complained, a complaint form may be filed before the AFA, which, as the financial system supervisor, will analyse the claim.

Reports issued by the AFA Claims Service are not binding in relation to contractual responsibilities between the client and the entity, which matter is reserved to the courts' jurisdiction.

If the analysis of the complaint put forward to the AFA reveals a prudential concern that goes beyond a single customer complaint, the AFA may implement specific controls under prudential supervision. Steps undertaken by the AFA in the framework of a prudential supervision cannot be shared with clients due to confidentiality.

In addition, the Andorran Government has created the UCiC, which is intended to ensure efficient and effective protection of consumer rights. This entity is intended to: (i) inform and guide consumers and entrepreneurs; (ii) receive and process complaints of consumers; (iii) disseminate actions to improve consumption; (iv) develop inspection and control functions in the field of consumption; and (v) establish agreements with organisations aiming to protect consumer rights.

Andorra also has the institution of the Citizen's Ombudsman, which defends and oversees the application of the rights and liberties included in the Constitution and compliance therewith, acting as a commissioner or delegate for the General Council. The Ombudsman receives and processes all complaints and claims relating to citizens' dealings with all public administrative entities in Andorra, responding with independence and impartiality.

Moreover, Andorra has an arbitration regime for commercial disputes, and its Arbitration Court will begin operating shortly. The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, and the referral by a court to arbitration, have been in force in Andorra since September 2015.

Compensation schemes

Regarding compensation schemes, the Andorran deposit guarantee system matches European standards. Act 20/2018 on banks' deposit guarantee systems fixes the maximum amount of coverage at €100,000 per depositor and €100,000 per investor for each entity.

The assessment of the various guarantee schemes applied to comparative reference systems (*ex ante* and *ex post*) and the particularities of the banking sector (high concentration level) have configured the system in this Act as a mechanism to guarantee *ex post* by paying the corresponding amounts secured in case of intervention or forced liquidation of the member organisations.

Cross-border provision of financial and investment services

As no Andorran law or provision establishes when such services are rendered inside or outside the Andorran jurisdiction, it has to be deduced by the analysis of the nexus between

the services rendered or the products provided and the relevant jurisdiction where the service is rendered in Andorra, or on a cross-border basis (i.e. where the agreement was made/accepted, where the product was marketed, where the accounts were located or where the payments were made).

Notwithstanding the foregoing, these activities can be carried out without triggering any licensing requirements, with some limitations, on a cross-border basis to professional investors, under a genuine reverse solicitation scenario, as it is understood that these activities are rendered outside the jurisdiction.

Also, some activities, such as funds distribution, can be performed by foreign entities without triggering licensing requirements by means of indirect distribution through a cross-border execution transaction if they are entered into with a local banking entity on a principal-to-principal basis, and with no marketing activities performed by the foreign entity towards end-users based in Andorra.

In general, the marketing/commercialisation and/or sales promotion of financial services in the jurisdiction, which are carried out in a manner that is deemed to be active commercialisation ("*comercialització activa*"), will trigger local licensing requirements. In this sense, all active marketing activities conducted within the Andorran jurisdiction (by telephone, email, mail or in person), which include naming the services or products, may constitute marketing activities and therefore be subject to licensing requirements.

However, the circulation of generic information to potential investors (i.e. information that does not refer (directly or indirectly) to specific products), or initial contact to gauge interest that involves discreet one-to-one discussions with a limited number of investors, is unlikely to constitute a marketing activity.

Anti-money laundering provisions

Andorra follows the international standards of anti-money laundering and terrorist financing by means of the implementation of the Fourth Money Laundering Directive through the AML Law, complemented by the AML Regulation. At present, Andorra has transposed AML 5 provisions in Law 37/2021, which amends the AML Law accordingly.

The law recognises cryptocurrency exchange platforms and custodians as obliged entities.

Specifically, financial entities shall comply with the following obligations:

- Formal identification and beneficial owner identification: Prior to the commencement of the business relation, the entity shall request all the details regarding the client and transaction that were necessary in order to identify the client. Thus, the entity involved shall fill in an official form of UIFAND.
- Obligation to declare: The obliged persons shall declare to UIFAND any transaction, project or operation that could involve money laundering or terrorist financing.
- Suspicious transaction communication: The financial entities must communicate to UIFAND any transaction that might be susceptible or seems suspicious regarding money laundering. However, keeping the information confidential constitutes another obligation, as the information about the identity of the issuer of the suspicious declarations in any administrative or judicial proceedings with origin or relation of the declarations shall be treated as confidential.
- Due diligence measures: Simplified and enhanced due diligence measures may be applied regarding both the risk degree and, depending on the client profile, business relation, product or transaction. These issues need to be in conformity with the clients' admission

policy. The obliged persons must be able to demonstrate that the adopted measures are enough, taking into account the risk of money laundering or terrorist financing of the transaction. The risk degree must be in writing. However, simplified due diligence measures may be adopted in appropriate circumstances when there is a low degree of risk.

- Record-keeping: The financial entities must keep the documentation for a period of at least 10 years.

Andorra has established a very similar system to that of other Member States of the European Union, such as, for example, Spain and France. When comparing both systems, it is clear that many of the provisions and obligations are the same.

Miguel Cases Nabau
Tel: +376 728 001 / Email: miguel.cases@caseslacambra.com

Miguel Cases Nabau is the Managing Partner of Cases & Lacambra. He leads the Commercial & Corporate Law and Financial Services practices and is qualified to practise in both Spain and the Principality of Andorra, where he is Resident Partner. He has extensive experience advising credit institutions and investment services firms, being the legal counsel of several national and international financial institutions, public administrations and investment funds. His work includes banking contracts, structuring and negotiating financial derivatives and debt transactions. In the latter areas, he has participated in several of the most cutting-edge transactions in both Spain and Andorra in the past few years.

His practice includes regulation of the financial sector, where he is an expert on the legal framework and regulatory environment applicable to entities subject to prudential supervision, especially those rendering financial and investment services.

Laura Nieto Silvente
Tel: +376 728 001 / Email: laura.nieto@caseslacambra.com

Laura Nieto Silvente is a Partner of Cases & Lacambra and a member of the Markets & Financial Services practice at the firm's office in Andorra.

Laura specialises in banking and financial regulation and has an in-depth understanding of the asset management industry. She has broad experience advising credit institutions and investment services firms in the legal framework and regulatory environment applicable to entities subject to prudential supervision, especially in the provision of financial and investment services.

Her practice includes the pre-contracting, contracting and post-contracting of financial instruments and structured products, as well as global legal advice on netting market agreements and financial collateral arrangements (i.e., ISDA MA, GMRA, GMSLA). Laura's practice also includes cross-border transactions and funds distribution.

Throughout her career, she has undertaken projects relating to compliance with AML, market abuse (MAR), investor protection (MiFID), data protection and CRD IV-CRR regulations, including corporate governance and solvency and capital requirements.

Before joining Cases & Lacambra, Laura worked in the compliance departments of Crèdit Andorrà in the Principality of Andorra, and Caixa d'Enginyers and CatalunyaCaixa in Barcelona (Spain).

Cases & Lacambra

Manuel Cerqueda i Escaler 3–5, AD700 Escaldes-Engordany, Andorra
Tel: +376 728 001 / URL: www.caseslacambra.com

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