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London banking law firm Crefovi published this interview in the special Banking supplement of the International Financial Law Review (IFLR) in 2003 (IFLR banking yearbook).

This article summarises the state of banking and finance regulations that apply to financial services companies and banks in France, in 2003.

What legislation governs authorisation and regulation of banking activities in France? What has been the most significant regulatory issue in your jurisdiction?

Banking transactions, defined by Article L 311-1 of the French Monetary and Financial Code (the Code) comprise the receipt of funds from the public, credit operations and making available to customers or managing means of payment. Pursuant to Article L 511-5 of the Code, only credit institutions shall perform banking transactions in France on a regular basis. Article L 611-1 of the Code provides that the professional body named Committee of Banking and Financial Regulations (CRBF) is entitled to issue new regulations applicable to all credit institutions.

Investment services, defined by Article L 321-1 of the Code, comprise reception and transmission of orders on behalf of investors, execution of orders on behalf of investors, dealing for one's own account, portfolio management, firm-commitment underwriting or standby underwriting, placing. Pursuant to Article 531-10 of the Code, only investment firms and credit institutions authorized to carry out investment services (so-called investment service providers) shall provide investment services in France on a regular basis. Pursuant to Article L 622-7 of the Code, the general regulations of the Conseil des Marchés Financiers (CMF) apply to all investment service providers, including credit institutions authorized to provide investment services as related services. Moreover, pursuant to Article L 621-6 of the Code, the rulings of the Commission des Opérations de Bourse (Cob) also apply to investment service providers.

The most recent significant regulatory issue in France has been the draft bill on financial security (Draft Bill), discussed before the Parliament since March 2003. The main interests of the Draft Bill consist of the merger plans between the Cob and the CMF, in order to create a new entity named Autorité des Marchés Financiers (AMF) or Financial Markets Authority. The AMF is directed by a group (Collcge) that largely represents the market. This Draft Bill also provides specific rules on solicitation regarding banking and financial transactions.

What are the key activities for which authorisation is required?

The conduct of banking activity or the provision of investment services on French territory (as defined above) are subject to a prior authorization from the Credit Institutions and Investment Firms Committee (Cecei), an organization responsible for granting business authorization to credit institutions and investment firms in France.

As far as the provision of investment services (except portfolio management) is concerned, the Cecei shall give a copy of the application file to the Conseil des Marchés Financiers. As far as portfolio management activities are concerned, the Cecei shall give a copy of the application file to the Cob, the regulatory authority responsible for authorization and supervision of both French and foreign collective investment schemes in France. However, if this latter activity is to be carried out on an exclusive basis, the Cob will be the only supervisory authority.

What sanctions are available to the regulators in France when taking action against regulated bodies?

The sanction of financial offences in France is complex: these violations being both criminal offences and

breaches of administrative rules, they can lead to both prosecution in front of a criminal court and administrative as well as disciplinary proceedings in front of the Banking Commission or the Cob, or the CMF. Three types of sanctions can therefore be taken against a regulated entity. The only limit to this plurality of criminal and administrative sanctions is the application of the principle of proportionality.

Pursuant to Article L 613-21 of the Code, credit institutions may be sanctioned by the Banking Commission if they have breached a law or regulation relating to their activities, or failed to comply with a recommendation, instruction or notice. The sanctions are either a reprimand, the banning from the list of authorized credit institutions through a withdrawal of the banking licence granted in the past, a fine or the limitation of distributions of dividends.
Pursuant to Article L 621-15 of the Code and to repress anti-competitive behavior on the financial markets, the Cob can either fine for a maximum amount of €1.5 million ($1.75 million) or when some profits have been realized, give a pecuniary sanction that cannot be more than 10 times the amount of those profits, any person who has unfairly influenced the functioning of the market. The decision of sanction may also be published on certain newspapers and publications selected by the Cob. Pursuant to Article L 532-10 of the Code, the Cob may also sanction portfolio management companies by withdrawing their licence.

The CMF also holds some disciplinary powers on regulated credit institutions and investment firms (Article L 622-15 and seq of the Code). The CMF may either pronounce a warning, a reprimand, a fine with a maximum amount of €1.5 million (or, when some profits have been realized, a pecuniary sanction that cannot be more than 10 times the amount of those profits), or prohibit temporarily or permanently the provision of investment services by the concerned entity. The CMF can also withdraw the licence of a credit institution or investment firm.

Along with these administrative and disciplinary sanctions, a criminal court can also sanction a regulated entity for breaching market transparency (that is, insider trading, communication of privileged information, market manipulation and so on) pursuant to Article L 465-1 and seq of the Code. The regulated body can be sentenced by the court to a fine equal to five times the amount of the fine that would have been given to a natural person. Also, the entity can be either wound-up, banned from exercising certain activities (which have been the cause of the infraction) for a limited period of time, put under legal surveillance, or excluded from the public markets for a limited period or indefinitely, pursuant to Article 131-39 of the French Penal Code. The decision of the criminal court can be published in the media.

Does the regulatory regime for banking business in your jurisdiction include regulatory conduct of business rules governing the obligations of a bank to its customers?

Pursuant to Article L 613-1 of the Code, the Banking Commission controls the compliance of credit institutions with conduct of business rules. Those rules are not defined in any text, but result from recommendations of the French Association of credit institutions or from master agreements.

Article L 533-4 of the Code implements into French law Article 11 of the Investment Service Directive of May 10 1993, relating to conduct of business rules for investment service providers. Notably, this article from the Code provides that investment service providers shall "check the financial situation of their clients, as well as their experience in investment matters and their objectives as far as the requested investment services are concerned". Conduct of business rules for investment service providers are issued by the Conseil des Marchés Financiers (Title III of its General Regulations) and apply to all investment service providers except those offering portfolio management services on behalf of a third party. Portfolio management companies shall comply with Cob Ruling number 96-03 relating to conduct of business rules applicable to portfolio management services on behalf of a third party.

Moreover, Article L 562-2 of the Code provides that all credit institutions and investment firms must be vigilant and declare to Tracfin, the organization in charge of anti-money laundering controls, any sum written in their books that could emanate from drug trafficking or criminal activities, any transaction that could be linked to such traffic or activities and any transaction in which the principal's or beneficiary's identity is unclear.

SUPERVISORY REQUIREMENTS

Does the regulatory regime for banking business in your jurisdiction include regulatory capital requirements? If so, are these based on the Basel Accord and are there significant variations from the core Basel recommendations?

The French regulatory regime includes several capital requirements, for example, the definition of own funds of French credit institutions as provided by Regulation number 90-02 of the CRBF dated February 23 1990, the solvency ratio defined by Regulation number 91-05 of the CRBF dated February 15 1991 or the large exposures ratio as described in Regulation number 93-05 of the CRBF dated December 21 1993. Both credit institutions and investment firms must comply with those prudential rules, as provided by Articles L 533-1 and L 533-2 of the Code.

These French regulations on capital requirements derive either from harmonized rules adopted by the EU through directives and regulations inspired by the Basel Committee's capital measurement and capital standards of July 1988, or from French prudential rulings that aim to set higher and stricter standards on capital requirements. French capital requirements always comply with the minimum standards to be achieved, defined by the Basel Accord of 1988. For example, the Instruction number 96-01 of the Banking Commission dated March 8 1996, on prudential surveillance of market risks and the reporting of the international solvency ratio complies with the common minimum frame set up by Basel I.

What effect will Basel II have on banking transactions in your jurisdiction? Are

financial institutions already taking account of its effect?

The new Basel reform, which sets up a model of internal control that checks that own funds of banks relate to credit risks and operational risks through the Mc Donough ratio, favours the transfer of risks outside the banking system (for example, it favours securitization outside the banking system which is detrimental to interbanking securitization) and may constitute a substantial advantage for banks that finance retail customers. In effect, while the default probabilities are equivalent to those of institutional customers, the requirements in own funds are significantly lower for retail customers than for companies, sometimes by as much as half. French retail customers being, in average, less indebted than other retail customers from certain other developed countries and particularly than American retail customers, French bankers think that it is essentially American banks which could take a competitive advantage from the Basel reform. The same applies for revolving credit, which is the favourite way to obtain consumer credit in the US and which is treated in a very favourable way in the Basel II agreement, while it represents 7.4% of the American GDP and only 1% of Euroland's GDP.

Does the regime in your jurisdiction include rules and operational and organisational requirements relating to internal controls and operational risk?

Pursuant to Regulation number 2001-01 of the CRBF dated June 26 2001, credit institutions and investment firms (not including those providing portfolio management services) shall have an adequate internal control system and operational risk's measures. When the Cecei examines an application for licensing one of the above-mentioned entities, it checks whether the investment firm or credit institution is efficiently organized, notably as far as internal control and protection against operational risk are concerned.

Pursuant to Article 10 of Cob Ruling number 96-02 dated December 24 1966, investment firms that have portfolio management activities must also set up an internal control procedure. The Cob checks whether the management company has an efficient internal control system before giving a licence to provide portfolio management services in France.

Do you believe that Sarbanes-Oxley will have a material impact in your jurisdiction?

The Sarbanes-Oxley Act of January 23 2002 (the Act) should not have any direct impact in France. However, the French regulators share the same priorities with the American regulators, and the Cob has therefore published in August 2002 a professional guide to the attention of managers of listed companies. This vade-mecum reminds managers of their professional obligations and ethics (for example, personal obligations to declare the transactions undergone by managers on the securities of their company and obligations to keep shares under the registered securities form or in deposit), while running the company.

The Draft Bill is also being influenced by the Act, since the Parliament has inserted some new provisions on research analysts and their ability to manage conflicts of interests, and since the Draft Bill also provides for new rules setting up auditor's independence (for example, splitting up auditing and advising activities).

Does the regime in your jurisdiction include a requirement for controllers and major

shareholders of regulated banking institutions to be approved by the supervisory authorities?

Pursuant to Article L 511-10 of the Code, credit institutions must prove that the quality of their shareholders reaches high standards, in order to obtain a banking licence from the Cecei. This regulatory entity checks whether the shareholders who bring in the capital, can sustain the development and solidity of the credit institutions.

Pursuant to Regulation number 96-16 of December 20 1996 relating to modifications of the situation of credit institutions and investment firms other than portfolio management companies (the authorized entities), any person or group of persons acting together should obtain the authorization from the Cecei before the realization of any transaction of acquisition, extension or cession of shares, directly or indirectly, in authorized entities, when this transaction has one of the following effects. It leads the person or group either to obtain or lose the effective power of control on the firm's management or obtain or lose one-third, one-fifth or one-tenth of the voting rights. Moreover, any transaction that allows one person or a group of persons to obtain one- twentieth of the voting rights must be immediately notified to the Cecei.As far as the statutory auditors of credit institutions and investment firms are concerned, Article L 511-38 of the Code provides that two auditors are designated after the consent of the Banking Commission. Whenever required, the Banking Commission can also designate an additional statutory auditor.

Internal controllers do not have to be approved by the French supervisory authorities, but, pursuant to Regulation number 97-02 of February 21 1997 relating to internal control of credit institutions and investment firms, the regulated entities must select a person responsible for the coherence and efficiency of internal control, and inform either the Banking Commission, or the Cob or the Conseil des Marchés Financiers of their choice.

INVESTOR PROTECTION

Have there been any recent significant changes to insolvency legislation in your jurisdiction, or are any such changes proposed? Have they made or will they make the regime more or less borrower friendly?

EU Regulation number 1346/2000 of May 29 2000 has entered into force in France on May 31 2002. This new set of rules simplifies the treatment of transnational insolvencies within the EU and is applicable to all type of bankruptcies, either for legal entities or natural persons, with the exclusion of bankruptcies of insurance companies, credit institutions and investment firms that offer services implying holding funds

and securities of a third party. The most important aspect of this new Regulation is the fact that it sets up the principle of immediate recognition of decisions relating to insolvency procedures. Previously, it was necessary to use the exequatur procedure in order to have an insolvency court recognized in France. Now, the only reason for which a member state could refuse to recognize an insolvency proceeding started by another member state, would be to prove that the effects of such proceeding breach its public order. This new Regulation seriously decreases the possibilities to refuse the recognition of any foreign decision.

Since Regulation number 1346/2000 entered into force in May 2002, French regulators are looking to change the insolvency regime, in order to include in this framework the bankruptcy of natural persons for their non-professional debts, which does not exists at a national scale in France. In effect, while the bankruptcy of natural persons for their professional debts is possible (for example traders or craftsmen), civil insolvency is not allowed at present by French national law. As a consequence, a draft bill on the treatment of natural persons with excessive debts should be submitted to the French Senate in June 2003. The new procedure is inspired by the civil insolvency regime already existing in Alsace and Moselle, two French departments.

Does your jurisdiction operate a deposit protection or guarantee scheme protecting retail depositors from loss in the event of the insolvency of an authorised bank?

Pursuant to Article L 312-4 and Article L 511-43 of the Code and to several regulations from the CRBF relating to the guaranty of deposits and any other reimbursable funds held by credit institutions having their head office either in France or Monaco, French credit institutions must register with the guaranty fund for deposits, a legal entity managed by an executive board controlled by a supervisory board. Financed by the contributions of the registered institutions, the fund is aimed at indemnifying the depositors in case of unavailability of their deposits or other reimbursable funds. The Banking Commission decides when and to whom to give these indemnities: funds of UCITS, credit institutions and investment firms cannot receive any indemnification. The indemnity granted by the guaranty fund for deposits may not be higher than €70,000 by depositor.

Pursuant to Article L 322-1 and seq and to Article L 533-13 of the Code, investment service providers having an activity of securities' custody must register to a securities guaranty fund, aimed at protecting investors against risks linked to custody of financial instruments. Managed by the above-mentioned guaranty funds for deposits, the securities guaranty fund is run in a similar way.

Does your jurisdiction have an ombudsman scheme, arbitration scheme or similar scheme for the resolution of disputes between a bank and its retail customers other than through formal legal proceedings?

Law number 2001-1168 of December 11 2001 relating to urgent economical and financial reforms (the Murcef Law) had provided for an ombudsman scheme to solve disputes between a credit institution and its retail customers. This banking mediation was envisaged in the Murcef Law as either an alternative or a prerequisite to legal proceedings. The new arbitration scheme has been revised and completed by the

Charter of February 2003 on agreements on deposit accounts, signed by every credit institution in France.

Every French credit institution should now choose an ombudsman who is supervised by the Central Committee of Mediation. If the bank doesn’t appoint a mediator, the French Banking

Federation shall provide an ombudsman to the retail customer who files a claim. The mission of this mediator is to recommend a solution to both parties (the bank and the retail customer) and therefore answer to the query of the retail customer who has solicited him within two months. The recommended solution does not have to be followed by both parties who could prefer going to court. The mediator also reports its activity to the governor of the Bank of France annually.

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