

Banking Regulation

First Edition

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Argentina

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Introduction

By the end of the 20th century, the Argentine banking system started to suffer one of the biggest crises in its history, which ended with its full collapse at the end of 2001. That traumatic experience helped society to realise how much influence the financial system has in all economic and social fields of the country, but also provided evidence of existing weaknesses and the necessity for better regulation of the sector.

After the big crisis, the Argentine banking system was subjected to greater surveillance and became much more conservative, thus heavily reducing its exposure to systemic risk. Proof of that is the strength that the sector showed while the world financial crisis of 2008-2009 was (and currently is) affecting the banking systems of many developed countries.

However, even though more than ten years have passed since the big local collapse, Argentine society has not recovered its confidence in banks at all. This is evidenced in the very low volume of deposits maintained in the financial system and in the relatively low “bankerization” of Argentine society compared with other neighbouring countries. This prevents the financial system becoming the engine of the local economy.

In that sense, the Argentine banking system has still a big challenge ahead, and regulation can play a subtle part (but not the whole) in achieving the expected goals.

Regulatory architecture: overview of banking regulators and key regulations

The head of the Argentine banking regulatory sector is the Argentine Central Bank, which is an autonomous body within the National Government. As that implies, the Argentine Central Bank has (or should have) the highest degree of independence from the Executive Branch, notwithstanding in recent years that political influence over the bank has gradually increased.

The Argentine Central Bank was created, and its powers are set forth, by its Organic Chart (Law No. 24,144). Pursuant to the Organic Chart, the main functions of the Argentine Central Bank comprise the following: (i) to regulate the Argentine financial system and enforce the financial entities’ regulations; (ii) to regulate the quantity of currency and level of interest rates in the market, in order to orientate credit; (iii) to act as agent of the country with international financial organisms; (iv) to collect and manage reserves in foreign assets; (v) to help the smooth functioning of the capital market; (vi) to enforce the foreign exchange policy; (vii) to regulate payment systems; and (viii) to protect the rights of users of financial services and antitrust principles.

It is worth mentioning that every time the macro-political view of the National Government changes, the Organic Chart of the Argentine Central Bank suffers amendments in order to adapt to the new political context. Very recently (in 2012), the Organic Chart was amended by the National Congress. Such amendment included within the main functions of the Argentine Central Bank the promotion of employment and economic development with social equality, thus extending the scope of the National Government to dip into federal reserves in order to finance repayment of external debt, and other occasional needs.

As was mentioned above, one of the main functions of the Argentine Central Bank is to regulate the Argentine financial system and enforce the financial entities' regulations. In that sense, the Argentine Central Bank is the enforcement authority of the Argentine Financial Entities' Act (Law No. 21,526), which regulates financial intermediation, sets forth the types of financial entities that can operate within the local market, establishes the requirements for banks to obtain authorisations, and regulates insolvency measures for financial crises. In recent years, certain drafts have been filed with the National Congress in order to amend the Financial Entities' Act, so as to declare the financial activity of banks as a public service, to orientate credit to social development, and to restrict influence of foreign banks in the country. However, those drafts have not been strongly pushed by the National Government so far, and it cannot be ascertained whether they are going to be discussed in the short term or not.

One of the other main functions of the Argentine Central Bank that was mentioned above, which is one that is being exercised with full power these days, is the enforcement of foreign exchange policies. The Argentine Central Bank is the enforcement authority of the local foreign exchange market, which is globally regulated by the Money Exchange Houses Act (Law No. 18,924) and by Decree No. 616/2005, the latter being the one that reinstated huge limits to the inflow and outflow of foreign exchange. Currently, any foreign exchange transaction within the local market has to be registered with the Argentine Central Bank, and has to comply with its restrictions.

The framework of the local financial legal system is complemented by dispositions that the Argentine Central Bank issues day by day in the form of Communications, by means of which it regulates every aspect of the financial system (including the creation, merger and transformation of financial entities, the foreign exchange market, currency and interest rates, accountancy requirements, liquidity and solvency ratios, governance, payment systems, reporting duties, etc.).

Other key regulations, which are not exclusive to the financial system but which have relevant impact in the sector, include the Capital Market Act (recently enacted Law No. 26,831), the Anti-Money Laundering Act (Law No. 25,246), the Credit Cards Act (Law No. 25,065), the Data Protection Act (Law No. 25,326), Antitrust Act (Law No. 25,156) and Consumer Defense Act (Law No. 24,240). Even though all these specific regimes have their own enforcement authorities, the Argentine Central Bank has legal competence in order to regulate the effect of those regimes within the banking system, and to coordinate their enforcement with the relevant authorities.

Recent regulatory themes and key regulatory developments

Notwithstanding that the legal core of the local financial system (Law No. 21,526 and Law No. 18,924) was established some time ago in the Seventies, the modern issues in the sector began to be regulated in the Nineties and the beginning of the 21st century.

The most recent regulations in the area can be identified in the fields of the foreign exchange market, anti-money laundering, governance of financial institutions, financial consumer protection, minimum capital requirements, public offerings, data protection and class actions.

As we mentioned above, in 2012 the National Congress passed Law No. 26,739, which amended the Organic Chart of the Argentine Central Bank. Such amendment added within the main functions of the Argentine Central Bank the promotion of employment and economic development with social equality, thus extending the ability of the National Government to dip into federal reserves in order to finance repayment of external debt and other occasional financial needs. This amendment also focused on the idea that the Argentine Central Bank should act in accordance with the guidelines of national politics, and protect financial consumers.

As was also mentioned, in the year 2005 the National Government (Decree No. 616/2005) decided to reinstate restrictions on the local foreign exchange market, which was wholly deregulated in the Nineties. Those restrictions mainly establish that any local foreign exchange transaction has to be registered with the Argentine Central Bank, and comply with the local foreign exchange market regulations issued by the Argentine Central Bank. At first, restrictions were imposed in the inflow of monies to the country (in order to discourage speculative investments), by means of subjecting 30% of any foreign investment and financing (except in certain specific cases – i.e. direct investments, imports

financings, etc.) to a mandatory non-remuneratory deposit for a one-year period (called “*encaje*”). Apart from that, repatriation of foreign funds was required in certain cases (export of goods and services) and payments abroad were restricted, limited and regulated, depending on whether an import was involved, an investment, or a transfer of dividends to foreign shareholders. All these restrictions still exist nowadays and, since 2005, they have been broadly extended by the Argentine Central Bank day by day. It is important to say that local banks are responsible for monitoring compliance with these regulations by their clients.

The anti-money-laundering field is also one that has been developing since the beginning of the new century (with the enactment of Law No. 25,246). In recent years, as a consequence of major international pressure exercised by the Financial Action Task Force (FATF-GAFI) over the National Government, the original Act was amended, and many new regulations have been enshrined by the Argentine Financial Information Unit (the relevant enforcement authority) and by the Argentine Central Bank in order to comply with international standards, mainly in terms of the “know your customer” and internal politics requirements. In Argentina, banks have been the first obliged persons to be reached by these regulations, so anti-money laundering practice is well-known and established in the financial sector.

At the beginning of 2013 the National Congress enacted the new Capital Market Act (Law No. 26,831), thus modifying the public offerings regime that had existed since the middle of the 20th century. Although this new legislation goes beyond the banking sector, it affects certain activities in which banks operate on a daily basis, such as intermediation in securities, underwriting, secrecy rules, among others.

Another legal field that began to be developed since the beginning of the new century, is data protection. Upon the enactment of the Data Protection Act (Law No. 25,326), the processing of personal data is now regulated, and certain conditions are imposed on the transfer, use or disclosure of personal information of clients. These regulations (which are mainly set forth by the National Directory for Personal Data Protection) specifically affect banks in connection with the reporting of financial information to the Argentine Central Bank and credit bureaux, notwithstanding the general secrecy obligation that banks have over deposits, pursuant to section 39 of Law No. 21,526.

As was explained at the beginning of this section, recent regulations have been also issued in the fields of governance of financial institutions, minimum capital requirements, financial consumer protection and class actions. Those regulations will be explained in the following sections.

Bank governance and internal controls

Directors and top managers of banks in Argentina must be appointed and exercise their functions in accordance with specific dispositions of the Argentine Central Bank, which evaluates their capacity, experience, reputation and ability in the financial field, and must approve their designation for it to be effective.

Apart from that, recently, by means of Communication “A” 5201 (as amended), the Argentine Central Bank set forth certain guidelines for the corporate governance of banks. These guidelines constitute a mix of mandatory rules and soft-law recommendations that are seen by the Argentine Central Bank as good practice.

Pursuant to this Communication, banks must adopt and approve an internal corporate governance code regarding the management of the risks of the activity, taking into consideration the guidelines that the Argentine Central Bank mentions as good practice.

The main targets to which the corporate governance code must aim are: (i) to establish politics in order to comply with the corporate objectives of the bank; (ii) to guarantee that the activities of the bank comply with the necessary levels of security and solvency, in full compliance with applicable laws and regulations; (iii) to define the risks to be assumed by the bank; (iv) to protect the interests of the depositors of the bank; (v) to assume liabilities *vis-à-vis* the shareholders of the bank, but also with other third interested parties; and (vi) to effect the daily transactions of the bank.

In summary, the following guidelines are considered as good practice by the Argentine Central Bank

and should be covered in the corporate governance codes of banks:

- (i) the different responsibilities of the board of directors and managers in approving and conducting the business and politics of the bank should not be mixed up;
- (ii) directors should be the real and ultimate responsible persons for the actions taken by the bank, and should supervise the managers in their activity;
- (iii) the board of directors should have a relevant number of independent members (specifically in the audit committee);
- (iv) the bank should have different committees to advise the board of directors, depending on the relevance of the activities in which the bank is involved;
- (v) the board of directors and the managers should encourage and regard the opinions of internal auditors, and should request the monitoring of independent external auditors;
- (vi) the bank should avoid granting incentives to its personnel that could encourage the latter to take decisions beyond the acceptable risks of the activity;
- (vii) the bank should promote transparency at every level, and
- (viii) the bank should adopt risk management policies in accordance with applicable regulations; among others.

Pursuant to the same Communication, banks must implement adequate internal control procedures for monitoring compliance with corporate governance, compliance with applicable laws and regulations, and for reporting any deviation to the managers or the board of directors, as the case may be.

In connection with this internal control, the Argentine Central Bank has specified in 2010 (by means of Communication “A” 5042, as amended) certain minimum requirements that the internal control of financial entities must regard. The internal control should be focused on three different categories: (i) measuring the effectiveness and efficiency of transactions; (ii) testing the reliability of accounting information; and (iii) monitoring compliance with applicable laws and regulations.

For the Argentine Central Bank, all members of the financial entity are responsible for compliance with internal controls. However, such responsibility is specially assigned to the board of directors, the managers, the audit committee and the internal auditor.

Pursuant to the referred Communication, banks must have an audit committee composed of at least two members of the board of directors and by the internal auditor. The internal auditor must have functional independency, and its duties can be assigned to an independent professional.

The Argentine Central Bank, by means of the cited Communication, establishes the guidelines and methodology that the internal control should follow in the design, instrumentation, evaluation and reporting strategy.

Bank capital requirements

In accordance with section 32 of the Argentine Financial Entities Act (Law No. 21,526), banks must comply with the minimum capital requirements that the Argentine Central Bank may establish from time to time.

As from the year 2007, the Argentine Central Bank has been implementing policies in order to comply with the guidelines of Basel II and Basel III in terms of minimum capital requirements and risk management.

Recently, the Argentine Central Bank modified the minimum capital requirements. Currently, the minimum capital that banks must comply with is the higher between the basic exigency (Ar\$26m for categories 1 and 2) and the sum of other exigencies determined by credit risk, interest rate, market risk and operational risk. In case the bank acts as a custody or registry agent, exigencies are higher, depending on the volume of securities in custody and/or registry.

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

Up to the beginning of 2013, the Argentine Central Bank used to have a disposition (Communication “A” 4429) governing the relationship among banks and their customers, though it was mainly an

operational disposition and it did not focus strongly on the protection of customers. At the same time, in year 2005 the principal private chambers gathering banks in Argentina published a Code of Good Banking Practices, which constituted a form of self-regulation by the banks (without the intervention of the Argentine Central Bank), with doubtful efficacy in practice.

In that scenario, customers have exercised their rights (when controversy arose) within the frame of the general Consumer Defense Act (Law No. 24,240), rather than within specific banking regulations.

Recently, in January 2013, the Argentine Central Bank issued a new regulation for the protection of financial services' users (Communication "A" 5388), which grants broader rights to banking consumers and sets forth more detailed procedures for the management of consumer claims.

Apart from that, it is worth mentioning that in year 2009 the Supreme Court of Argentina ruled in the case "Halabi", which admitted the possibility of individuals to initiate class actions in order to defend their rights. Even though class actions are not still legislated for in Argentina, this court precedent opened the door for many new cases, in which financial entities are being currently involved.

Finally, as it was mentioned above, anti-money-laundering and data-protection dispositions have put additional requirements in the way in which banks deal day-by-day with their clients, mainly in terms of "know your customer" policies and in terms of handling and processing client information.

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