

The AFM Agenda in 2014

With the budget for 2014

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This is an informal translation only. In case of any conflict between this translation and the original text, the latter shall prevail.



The Netherlands Authority for the Financial Markets (AFM)

The AFM promotes fairness and transparency within financial markets. We are the independent supervisory authority for the savings, lending, investment and insurance markets. We promote the fair and conscientious provision of financial services to consumers and private investors, as well as professional and semi-professional parties. We supervise the fair and efficient operation of the capital markets. Our aim is to improve consumers' and companies' confidence in the financial markets, both in the Netherlands and abroad. In performing this task, the AFM contributes to the stability of the financial system, the economy and the reputation and prosperity of the Netherlands.

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Foreword

This is the AFM Agenda for 2014, which gives a general description of our plans. The Agenda also includes an analysis of relevant developments and our budget for 2014.

The environment in which the AFM operates is constantly changing. Against this dynamic background, the AFM has to update its mission, objectives and core values on a regular basis. In our opinion, the new mission and objectives more clearly represent what the AFM stands for. For example, we have further defined our role in the various areas of our supervision, as well as more clearly describing how we contribute to financial stability.

Our appeal in May 2013 for input on which to base our supervision in 2014 was favourably received by the market. We received various questions, comments and suggestions that we were able to use in the formulation of our plans. We also consulted with various market parties, interest groups and our fellow supervisors. The responses and consultations have been extremely useful, and have offered us items of attention for our supervision in 2014.

The Agenda was offered for consultation on 10 September. The responses have assisted us in the further elaboration of our plans. The AFM continues to conduct a dialogue with the parties concerned.

Questions or comments with respect to this Agenda are most welcome. There are various ways to contact us, including by e-mail via focus@afm.nl. Your knowledge, experience and insights will contribute to the formation of the AFM's vision. We look forward to your response!

Theodor Kockelkoren
Acting Chairman

1 Our mission, strategy and risks

This section begins with a description of our mission, strategic objectives and core values, which we have updated and amended this year. We then turn to the targets we have set for ourselves in 2014. Section 1.5, the risk statement, outlines the principal risks standing between us and the achievement of our strategic and thematic goals. The section concludes with a general account of the estimated costs of achieving these goals, and developments in this area.

1.1 Mission

The AFM promotes fairness and transparency within financial markets. We are the independent supervisory authority for the savings, lending, investment and insurance markets. We promote the fair and conscientious provision of financial services to consumers and private investors, as well as professional and semi-professional parties. We supervise the fair and efficient operation of the capital markets. Our aim is to improve consumers' and companies' confidence in the financial markets, both in the Netherlands and abroad. In performing this task, the AFM contributes to the stability of the financial system, the economy and the reputation and prosperity of the Netherlands.

1.2 Strategic objectives

The AFM's mission statement implies three strategic objectives:

1. The AFM promotes the fair and conscientious provision of financial services

Consumers, private investors and professional and semi-professional parties must be able to rely on the fair and conscientious provision of financial services. We supervise financial institutions in the fields of savings, loans, investment and insurance. Our supervision focuses on financial products, financial services and ethical business conduct of financial institutions. The AFM helps to promote an environment in which consumers, private investors and professional and semi-professional parties are in a position to make well-considered decisions regarding their financial position on the basis of comprehensible information and appropriate service provision.

2. The AFM promotes the fair and efficient operation of the capital markets

Investors, as well as other parties active in the capital markets, must be able to have confidence that the capital markets operate fairly and efficiently. Our supervision is designed to ensure that companies operating in the capital markets provide timely and reliable information, and that auditors who have to assess the reliability of the financial reporting perform this task correctly. We establish whether the financial reporting is prepared in accordance with the correct standards. The AFM contributes to an environment in which investors can make fair and informed decisions.

3. The AFM contributes to the stability of the financial system

Together with DNB, the AFM creates the preconditions for a financial system with manageable and transparent risks. The AFM supervises the orderly operation and stability of the financial infrastructure. Our supervision focuses on the behaviour of market parties that could undermine financial stability and on the transparency of systemic risks.

1.3 Core values

The AFM applies five core values in the conduct of its supervision:

Vigorous

As the enforcer of legislation and regulation, the AFM takes vigorous action. We apply both a formal and an informal approach in our supervision of compliance with legislation. Our methods, activities and supervisory tools are designed to influence behaviour effectively.

Diligence

A vigorous supervisor must of course act with diligence and care. We collect and analyse the facts. We enter into a dialogue with those concerned and consider all the interests carefully, including the interests of consumers, individual market parties and the sector in general. The action taken by the AFM is proportional.

Reference point

The AFM acts as a reference point for consumers, private investors and semi-professional and professional parties. We explain our principles and regulations and put these into context. We strive to be as predictable as possible. As an interlocutor for market parties, we state what is and what is not allowed, and we discuss possibilities and solutions. We conduct a dialogue with all interested parties.

Efficiency

In its supervision, the AFM looks for ways in which its actions can achieve the greatest possible effect on the market. We also strive to limit the financial and administrative burden for market parties as far as possible. Furthermore, we strive to use our resources as efficiently as possible. To do this, we have created an efficient, creative and flexible organisation and we work together with other supervisors and enforcement agencies in the Netherlands and across national borders.

Personal responsibility

We start with the personal responsibility of consumers and the sector. Our supervision is designed to suit the circumstances: the more we can rely on individual companies and a sector as a whole, the more our supervision can be at a distance. Companies are responsible for the quality of their products and services and by extension for confidence in the financial markets. Consumers must in turn critically assess products and services on the basis of comprehensible information, aided by appropriate service provision.

1.4 Targets for 2014

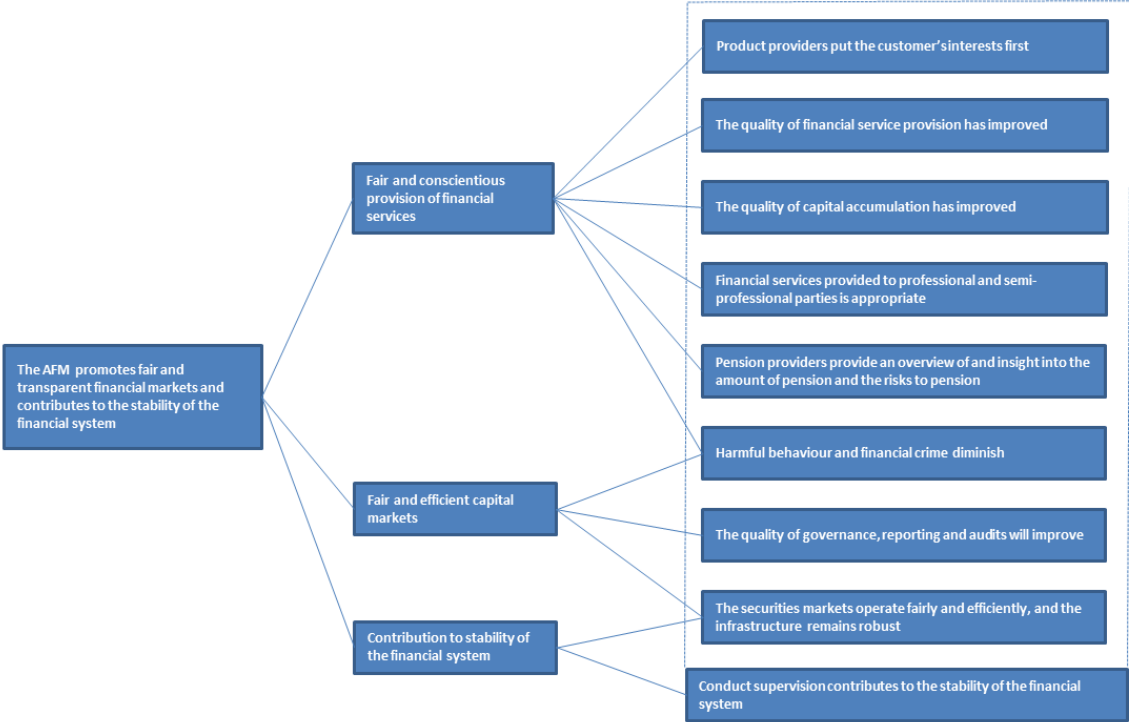
The AFM's supervision is risk-driven. This means that we set priorities so that our presence can be focused where the risks are the greatest. We anticipate new and future risks as far as possible. The AFM analyses market developments and risks in order to set the right priorities in our supervision.

The AFM sets and structures its priorities on the basis of themes. Each theme has its own focus area, with specific targets and is intended to achieve certain effects in the longer and the shorter term. The AFM's activities are determined by these targets and intended effects. New insights gained during the year may lead to a change in the priorities of the themes, either within a theme or between themes. This means that the AFM actually deploys its resources in accordance with the most important priorities.

Based on its strategic objectives and observed external developments (as described in section 2), the AFM has decided to continue its nine supervisory themes in 2014. According to our current understanding, these nine themes represent the most important problems and risks for supervision in 2014.

We have changed the title of four of these themes from those used last year. The new theme titles *'The quality of capital accumulation has improved'* and *'The financial services provided to professional and semi-professional parties is appropriate'* more accurately reflect the targets of the themes concerned. The new title of the theme *'Pension providers provide an overview of and insight into the amount of pension and the risks to pension'* is the result of our increased attention to pension scheme members. Transparency regarding the amount of and risks to pensions is important, however it is also important that scheme members can do something with this information. We will focus next year on the overview, information and action taken for scheme members with respect to the amount of their pensions, their purchasing power and the risks involved. Communication regarding risks also plays an important part in the transition to new pension agreements. The new title of the theme *'Harmful behaviour and financial crime diminish'* is the result of the change of activities that previously fell under the theme of *'The quality of financial service provision has improved'*. These activities concern harmful behaviour in the service provision chain that has the greatest relative effect on consumer confidence in the market and the level playing field for market parties.

Translation of mission into strategic objectives and themes for 2014



1.5 Risk statement

This risk statement describes the principal risks identified by the AFM as risks that it cannot fully prevent as a result of the limits to its influence. These risks are a threat to the proper functioning of the financial markets. To a certain extent they are not avoidable, or are associated with limitations to statutory powers and international cooperation.

The effects of the euro crisis are still with us. In the short term it is not certain whether the economic reforms will be sufficient to achieve a moderate recovery in 2014. Broad-based political support is important for the necessary economic reforms to be pushed through. This is true at national and European level. A possible renewed escalation of the European debt crisis also continues to be a threat to the stability of the European and Dutch financial system. The fragile economic situation means that the risks described below may continue, or increase.

1. The development of all-embracing international legislation and regulation is inherently complex

The international nature of the financial markets means that financial regulation and supervision has to be internationally coordinated. The financial crisis moreover exposed weaknesses in financial regulation. Policymakers around the world have announced measures in response to this. The AFM sees risks with regard to parts of European legislation and regulation which could lead to unintended consequences.

Pressure on quality of European regulation

The quality of European legislation and regulation is a point of particular interest. It is correlated to the huge quantity of regulation in development and the pressure to implement it quickly, the sector-based approach chosen for this and the differences of opinion between countries as to how to regulate markets. The risk is that important issues and terms in European regulation are sometimes not sufficiently well defined and/or demarcated. This could create inconsistencies in the implementation and interpretation of this legislation and regulation within Europe and in certain cases unintended conflicts between various European directives and/or regulations. For instance, this is a risk in the field of product development, and the area of remuneration policy. For example, the risk arises when limitations on the maximum of bonuses are avoided in ways that unintentionally cause new incentives for hazardous behaviour.

The amount of new European regulation that financial institutions have to comply with also entails a risk that they will adopt a checklist mentality. Smaller players are experiencing difficulty in meeting the stricter regulations and capital requirements. These unintended indirect effects of the new regulation could lead to increased market concentration.

Avoidance

Another unintended effect of European legislation and regulation is avoidance. One example of this is the proposal to introduce a European tax on financial transactions. If transaction tax is not harmonised, there is a risk that trading will move to jurisdictions where there is no transaction tax, to European countries that do not join or to the financial centres outside Europe. Moreover, the extra-territorial operation of new financial legislation and regulation in the United States, Europe and the Netherlands may not be sufficiently harmonised. This could have consequences for the competitive position of financial enterprises in the Netherlands, especially if the extra-territorial operation of European regulation is prevailed by the regulation in third countries. In those cases, enterprises situated in those third countries which operate across borders have a competitive advantage. They are bound by one set of rules, whereas parties situated in Europe are bound by two sets of rules when operating in third countries.

European cooperation

In view of the international nature of the financial markets and the supervision thereof, the effectiveness of the AFM partly depends on the regulation that is established at European level and on the supervision in other Member States. We therefore enthusiastically support international cooperation and further convergence in the area of supervision by the European Supervisory Authority (ESAs). Convergence of supervision has however received too little attention since the European System for Financial Supervision came into operation. This is partly due to the activities of the ESAs in the context of the single rule book, the harmonised European regulation. The other difficulty is that the network structure, which involves representation of all the participant countries, makes it difficult to take decisive action on politically controversial issues. The interests of Europe thus regularly conflict with national interests. The ESAs will have to demonstrate in the coming years that their current governance system, in which all the national supervisory agencies are represented, can effectively coordinate an approach to cross-border problems. The organisations of the individual ESAs will also continue to grow, in both effectiveness and capacity. The position and ambitions for European supervision in other Member States will therefore to some extent determine the extent to which the AFM will be effective in issues dealt with through the ESAs.

Attention paid to conduct supervision diminishes due to the banking union

At the end of June 2013, the European Finance Ministers reached agreement regarding rules for European supervision of banks, the so-called banking union. The banking union consists of a common European supervision mechanism, the Single Supervisory Mechanism (SSM). An important objective of the SSM is to prevent systemically important banks from ailing in the future. In the event that a bank gets itself into trouble, the European resolution mechanism and a European deposit guarantee system, should limit as much as possible the vicious circle between banks and governments. The banking union could thus be a positive development for the internal market.

The developments surrounding the banking union are largely outside the AFM's mandate, since they mainly relate to prudential supervision. The risk is therefore that conduct supervision within Europe will receive less attention because the focus will be mainly on the application of prudential supervision. The AFM and DNB will have to find a new mechanism for cooperation and exchange of information in cases where powers overlap and the ECB is the competent authority.

Dependence on technological means and expertise of foreign supervisory agencies

In order to continue to effectively supervise a complex and technologically advanced international market, supervisors, which usually follow the market, will have to keep up with the market as closely as possible. Additional investment in resources and expertise is still necessary. The capacity for accumulating and organising the necessary expertise however varies per country. This can for instance be seen in the protection of the integrity of the market and the prevention of market abuse. Improvement of adequate sharing and use of this expertise in an international context takes time. In mitigating these risks, the AFM depends on the resources and expertise of other foreign supervisory agencies.

2. Cybercrime is a threat to the financial system

Advanced information and communication technology are increasingly playing a central role in the financial system. Therefore cybercrime is a threat to the fair and efficient operation of the financial markets. The responsibility for the correct operation of IT systems during and after a cyber attack rests primarily with financial enterprises. Supervisors have only limited influence on the risk of cybercrime.

Until now, cyber attacks on the financial system have not been serious enough to cause a systemic shock. This does not mean that this can happen in the future. The volume, degree of sophistication and complexity of cyber

attacks increase. A serious cyber attack on a bank or stock exchange could have a drastic effect on the operation of such a link in the financial system and thus lead to a widespread reaction.

3. Settlement of the “woekerpolis” affair

A number of insurers have compensated customers for high charges, in response to the *woekerpolis* affair which concerned the sale of insurance policies with excessive charges. These insurers offer customers options to improve their financial situation. It is important that customers not only have the opportunity to improve their financial situation, but also do so as quickly as possible. Many consumers holding investment-linked insurance policies accumulate too little capital to pay off their mortgages or to complement their pension income.

We urge insurers and financial advisors to actively approach their customers to find a solution. This means that customers have an overview of their financial situation and their options and take steps with the insurer or their advisor to improve their situation. Most insurers and advisors have started doing this, but attention on providing customers with support remains necessary. We keep an eye on the progress and intervene when we find that progress is insufficient or if unjust barriers for customers are raised.

The *woekerpolis* affair also concerns risks which we do not have direct possibilities or powers to intervene. It primarily involves risks resulting from claims from customers. The claims and the publicity surrounding it could prevent the restoration of consumer confidence in life insurers. Moreover, a definitive solution to the *woekerpolis* affair is an important prerequisite for the sustainability of the sector.

4. Structured products not subject to product development supervision

The currently limited scope and the variations in international initiatives mean there is a real risk of supervision arbitrage and the evasive constructions associated with this. Therefore a public standard for the quality of products is needed for institutions and product groups that currently fall outside the scope of supervision. The Dutch government is however bound by the European regulatory framework. The Ministry of Finance is thus arguing for changes to PRIIPs and MiFID II so that the scope of product development supervision will be extended.

The AFM has authority to supervise product development since 1 January 2013. We consider the standard for the supervision of product development however too strict in scope, given the problems in the market. In general terms, the supervision covers insurers, banks, credit institutions, premium pension institutions and investment firms. Issuers and financial instruments (such as structured products and synthetic exchange-traded funds) do not fall under this supervision, nor do foreign providers and various national providers, including investment firms. The AFM is pleased to see that certain groups of institutions that fall outside the standard (either entirely or partially) have committed themselves to a product development standard based on self-regulation.

5. Transition to sustainable business models with priority for customer interests is a long-term challenge

The financial sector in the Netherlands has made progress towards putting the customer's interests first in the past few years. Financial enterprises also have stakeholders other than customers, including employees shareholders and other capital providers. The interests of these stakeholders sometimes coincide, but they are also possibly difficult to reconcile and they are subject to change over time. The various interests can be an obstacle for financial enterprises in the attempt to achieve a stable and sustainable earnings model in which the customer's interests are prioritised.

The ability of banks and insurers to put their customers' interests first depends for example on the return on capital demanded by shareholders and other capital providers. If capital providers demand a high return, there will be incentives for providers to realise high short-term profits. Here it is important that there is also a level playing field, in which banks and insurers are kept to the same standard. It is important over the longer term to find a good balance between the various interests. We continue our dialogue on this with the relevant enterprises.

Other priorities

Furthermore, several financial enterprises are not in a position to change their earnings model fundamentally to reconcile the interests of the business and those of the customers. The reduced confidence in financial institutions among consumers, lower demand and the overcapacity on the market are a challenge to some providers and service providers whose primary concern is survival and resolving problems from the past. In the case of intermediaries, it is especially true that the reconciliation of current earnings models with customer interests cannot be guaranteed. They are being forced to change their business models as a result of the ban on commissions. In the process of guiding service providers through this transition, it may well be that the AFM will not be able to supervise the entire service provider market.

2 External developments

2.1 Introduction

This chapter contains, as much as possible, a factual description of market developments which are relevant for the AFM's supervision. The AFM observes and assesses these market developments with its mission and objectives in mind. The developments cover all aspects of the financial sector and touch upon topics which lie outside the direct competence of the AFM. A broad outlook is however important in order to be able to identify different types of conduct by market parties. The basis for prioritisation of the AFM's supervision lies in observing and analysing these developments. The external developments listed below are leading in making choices between and within the themes.

2.2 External developments

The European Commission predicts a slow recovery of the eurozone, there is still a chance that there will be new setbacks for the global and European economy, given the tension that appears to exist between the need for economic reforms and the limited support among the European population for these reforms. The part of the population that is weary of reforms could vote in such a way that further European reforms are difficult or even impossible to achieve. Moreover, some of the actions needed to repair the European economy are outside the scope of the European central bank. The monetary policy of the central banks of the economic superpowers outside the EU plays an important part in recovery. In addition, some countries in the eurozone still have limited access to the capital markets. Various economic indicators for the Netherlands, including consumer confidence and investment, are below their long-term averages.

The lack of economic recovery is causing uncertainty for consumers and investors in Europe and the Netherlands. Dutch financial enterprises are also operating in a difficult international environment. They are under pressure due to the economic slowdown, the depth of the crisis and the new regulations that have been introduced in response to this. Financial firms have to prepare for new legislation and regulation and have to strengthen their financial position. The direction in which European supervision, European regulation and the market will develop is uncertain. The new market relationships also present new opportunities, as long as financial institutions can make the necessary adjustments in good time. The AFM thus has to take account of various scenarios. In setting its priorities, the AFM will also anticipate these various scenarios.

Restructuring of European supervision

The banking union

With the euro crisis contagion between banks and national governments has manifested. The European Union is working on a banking union in order to prevent the risk of contagion and improve coordination between national supervisors.

European supervision will apply to all banks in the participating countries, and will be performed under the responsibility of the European Central Bank (ECB). The ECB will directly supervise banks with assets of more than EUR 30 billion or 20% of national GDP, in any case the three most significant banks in each member state and additionally banks receiving support from the European Stability Mechanism (ESM). The other banks will come under indirect supervision by the ECB, which will direct implementation by the national supervisors. The ECB may place banks under direct supervision on its own initiative, and will have the authority to collect information from all banks and to make local inspections.

The introduction of European supervision by the ECB will mean a fundamental change in prudential supervision. At the same time, this means that the authorities in the Netherlands will have less scope for regulating and supervising the banks, and settling them when necessary.

European Supervisory Authorities

The European System of Financial Supervisors (ESFS) came into operation in 2011. This system comprises three new sector-based European supervisory authorities, known as ESAs. The European Securities and Markets Authority (ESMA), the European Banking Authority (EBA) and the European Insurance and Occupational Pensions Authority (EIOPA) have been set up in order to promote the quality and harmonisation of European supervision. In addition to these three ESAs, the European Systemic Risk Board (ESRB) has been set up to prevent or mitigate systemic risks. The European Commission is evaluating the relatively new ESFS system in the second half of 2013. The formation of the banking union also will involve reconsideration of some parts of the role of the ESRB.

The evaluation will present opportunities for further development of the supervisory system. Together with DNB and the Ministry of Finance, the AFM will strive for further strengthening of cross-sector supervision in Europe. The sector-based organisation of the ESFS does not yet adequately reflect practice in the financial sector, whereby institutions operate in several subsectors and financial products are often an amalgamation of elements of credit, insurance and investment products.

The AFM supports strong coordination mechanisms in Europe, and therefore actively contributes to the work of the ESFS. Much has been achieved in the early years, especially with the development of the single rule book. The AFM continues to strive towards supervisory convergence. It is a proponent of more far-reaching cooperation in the areas of auditing, financial reporting and market abuse. The powers of the ESAs to carry out peer reviews will be an important instrument for achieving a collective European supervisory culture. However this should take sufficient account of the national context in which the supervision is conducted.

Developments in the Dutch banking landscape

Competition in the Dutch banking sector seems to be further reduced as a result of the financial crisis. This is due to government interventions and nationalisations during the credit crisis and the euro crisis, the ongoing consolidation in the Dutch financial sector and the withdrawal of banks to their home markets. This last point applies to both Dutch banks, which are increasingly withdrawing from international operations, and foreign banks that are abandoning their operations in the Netherlands. Three large banks dominate today's Dutch banking landscape.

Partly as a result of the reduced competition, there is a risk that there will not be enough market discipline to ensure transparency and the further implementation of putting the customer's interests first. In the absence of the disciplinary effect of competition, the AFM will have to make a stronger contribution in order to ensure an adequate degree of transparency towards the market.

The banking landscape will continue to change in the coming years. Plans are being drawn up for the denationalisation of ABN AMRO and SNS Reaal. Banc assurance providers such as ING will also be demerged. The unfavourable market conditions could lead to further consolidation. In the process of denationalisation and further consolidation, new business models will be developed and business cultures and systems will be combined. This is a complex process that will involve both risks and opportunities to embed prioritisation of the customer's interests in the new mission, vision and strategy of these companies.

Risks to stability in the Dutch banking sector

The credit crisis underlined once again how much problems at banks can affect the financial stability and the functioning of the real economy. The policy used to deal with problems in the banking sector appears to be bearing fruit. Given the huge impact of potential risks to stability, this issue will require much attention in the next few years. The availability of good public information on the risks of banks is an important condition for a stable banking sector. Since Dutch banks depend heavily on market funding, this is a point of particular interest. Qualitative good and comparable information with regard to asset valuation, such as credit portfolios and commercial property, reserves and the disclosure is important considering the increase in problem loans and rising credit risk. When the number of mortgage loans in arrears rise, Dutch banks will need to increase their provisions for overdue loans.

The ability of households to meet their payment obligations is coming under pressure as a result of the dip in the economy and the rise in unemployment. Many consumers have taken out mortgages in which the mortgage represents a large proportion of the value of their home (a high loan-to-value ratio). It is estimated that one in five mortgages were 'under water' at the end of 2012. If house prices continue to fall, consumers will not be able to sell their homes, or will be left with a residual debt. Furthermore, the level of income relative to the mortgage debt (the loan-to-income ratio) on existing mortgages plays an important role. While losses on loans for the Dutch banks have remained limited until now, the number of mortgage loans that are now in arrears has risen. Various Dutch banks have thus further increased their provisions for overdue loans.

Lending under pressure

Stricter requirements for capital buffers held by banks as formulated in the Capital Requirements Directive IV (CRD IV) are forcing banks to reduce their balance sheets. This could make banks more cautious regarding the provision of loans, both in the retail market, where mortgage lending is the most important element, and in the business market.

Small and medium-sized enterprises (SME) depend primarily on bank loans. Some SMEs may encounter difficulty in obtaining loans as a result of balance sheet reduction and modest economic prospects. There are alternatives to bank loans, such as finance from credit unions, crowd-funding and SME bonds or direct lending by institutional investors (pension funds and insurers), which are attracting a growing number of investors. In some of these forms of funding lenders and borrowers meet directly, and the line between actions that do not require a licence and the provision of investment services is thin. There is a significant risk that parties will use these direct channels to offer loans with a poor risk-return ratio. This could be due to the offering of inappropriate constructions to investors with lesser expertise, or the use of a charitable objective to tempt investors to be satisfied with a lesser return. This has happened in part of the teak funds business in the past. It is also relatively easy to operate under an exemption and thereby escape supervision by the AFM. The AFM must therefore clearly state what its supervision of alternative forms of funding does and does not include, and what is possible in this respect.

Reform of the housing market

The policy with regard to the housing market, including the limitation of mortgage interest tax relief, has a significant influence on the structure of the mortgage market. According to expectations, annuity mortgages will become the norm as a result of the changes to tax legislation.

In an international perspective, mortgage interest is relatively high in the Netherlands, since providers charge a relatively high surcharge above the market interest rate. There are a number of reasons for this. Funding a high-risk portfolio has become more difficult in the current market circumstances. Dutch mortgages feature high loan-to-value and loan-to-income ratios, and therefore involve high risk. The number of mortgage payments in arrears

has risen, and it emerged in the summer of 2013 that the number of forced sales and thus the claims on the National Mortgage Guarantee (NHG) had increased compared to the previous year. There were also more mortgage holders with payments in arrears than there were in the previous six months. Another possible reason for the relatively high interest rate could be the lack of competition between the large mortgage providers. As a result of new regulations, the mortgage market is becoming more comprehensible and accessible, which could reduce the barriers to entry the Dutch market for new foreign parties.

Pressure on earnings and business models

The earnings models of financial enterprises are under pressure as a result of the difficult macroeconomic conditions, low interest rates and the new regulations introduced in response to the crisis. Disappointing sales and rising costs could be a risk to the theme of putting the customer's interests first for the whole market. This is potentially a dilemma for conduct supervision, since the continuity of a business is also in the customer's interests.

Banks

A significant proportion of the mortgage portfolios of the Dutch banks is funded from the capital market. The retail market, or the savings held by Dutch households, is not large enough. Funding costs have risen due to the deteriorated situation in the funding markets. In addition, rising losses on loans in the mortgage portfolio directly affect sales, and therefore the business model, of one of the biggest divisions of the Dutch banks.

More expensive capital market funding means there is a risk that banks will introduce more complex products to the retail market for their own funding purposes. On the demand side, consumers are looking for return due to the continuing low level of interest rates. It is therefore more likely that consumers will come into contact with non-standard investment products. The AFM is following this development closely. The increase in execution-only services increases the risk of non-standard investment products. With an execution-only service, consumers purchase products themselves, without the intermediation of an adviser.

Insurers

Insurers are mostly active in both the non-life and the life insurance markets, so that the developments in these two markets are linked. Since sales and profitability are disappointing in the life insurance segment and insurance groups that operate in the life segment usually also operate in the non-life segment, the negative developments in the life segment are also affecting the non-life segment. As a result of the contracting life insurance segment, consolidation is to be expected in the whole insurance market. This does not alter the fact that insurance groups that can control their costs, despite falling sales in the life market, can also maintain their right to independent existence.

The life insurance market is divided into the provision of individual policies and of group policies. Sales in the group policy market, the management of second-pillar pensions, are stable. The capital position of life insurers with individual policies is however under pressure. There are several reasons for this: first of all, the current (and long-lasting) low level of interest rates in combination with the high guarantees that life insurers agreed with their customers in the past. The sector is also feeling the effects of the tax reforms, the rise of bank savings and lower consumer confidence due to events like the *woekerpolis* affair and the general economic conditions.

Profitability is under pressure, and therefore there is also continuing pressure to cut costs. An increasing number of life insurers are distinguishing between their active portfolio and their 'closed book' portfolio. The active portfolio consists of products that are still actively sold and administered in new IT systems at lower cost. It is also true for these products that life insurance products have generally become less attractive as a result of the developments described above. In addition to this, the risk-free capital markets interest rate is low, meaning that the offering of interest-rate guarantees has become very expensive. The closed book portfolios consist of life products that are no longer sold, but for which premium is still received. These are administered in older systems that involve

higher management costs, and are in fact portfolios containing products that are no longer viable. The AFM will discuss with relevant parties whether in such a situation they are in a position to safeguard their customers' interests and maintain an acceptable level of service.

Lastly, the insurers are exposed to a balance sheet risk on the funds they have provided to intermediaries now that the earnings model of intermediaries is under pressure. Most intermediaries have a current account with insurers. Estimates of the total funds outstanding by insurers range from EUR 1 to 3 billion.

Financial services providers and portfolio managers

The market conditions and the reforms are also affecting the earnings and business models of financial services providers and portfolio managers. Not all market parties have adjusted their earnings model to take account of the ban on inducements for complex products. The coming ban on inducements for investment services will also put the business model of independent portfolio managers whose earnings model is based on commission income under pressure. The smaller service providers will experience the most pressure on their business model. Assets under management need to be of significant size for a direct management fee to be cost-effective. Consumers will not be helped by an excessive management fee. So these portfolio managers will either have to change their earnings model or achieve bigger scale through consolidation.

Structural changes in insurance distribution

After the ban on inducements takes effect, consumers will often go directly to their insurer to purchase a product. Demand for execution-only products is high, and the insurers want to meet this growing consumer demand by setting up a direct channel within their organisation which will be increasingly dedicated to the development of execution-only propositions that will be offered online.

A number of intermediaries is attempting to circumvent the ban on inducements by acting increasingly as an authorised agent of an insurance company. An authorised agent acts on behalf of the insurer and is therefore not an intermediary, so the ban on inducements no longer applies. The AFM is monitoring the payments received by authorised agents: this must be in proportion to the activities carried by the agent for the insurer.

Those acting as intermediaries in pension insurance must, after application of the professional competence requirements, have the Wft module Pensioen professional qualification. Many intermediaries have decided not to obtain this Wft module. The portfolios of the intermediaries that will cease this business will be transferred to the provider. The insurers are experiencing difficulty in placing these portfolios with other intermediaries, and are themselves not set up to provide the advice and management services for the contracts in these portfolios. This constitutes the risk that these customers will not be serviced with due care.

Changes to service provision

The ban on inducements has structural consequences for service provision. A ban on inducements means changes to the fee structure of service providers whereby the price paid for the service provision will become more visible to consumers. Consumers may therefore be expected to be more aware of the charges for the service provision, and to be more alert and critical with regard to the added value of the service provision. In addition to the ban on inducements, a measure of charges is being developed for the provision of investment services. This will state the total charges for an investment and thus increase price transparency. Price transparency will affect the structure of the market, competitive relationships and the costs of service provision, with the ultimate objective being that the ban on inducements and the cost measure will, over time, contribute to increased competition and lower charges for the provision of services.

The pressure on charges as a result of the ban on inducements will encourage innovation, because innovation can reduce the costs of service provision if new and cheaper forms of service provision become possible as a result of technological advances. If more service providers use automated management, this will increase dependence on digital resources and thereby increase the importance of reliable software (including advisory software) and ICT infrastructure.

Now that more information is available on the Internet and the costs of advice are directly visible, consumers can gather more information on financial services and products independently. It is however a fact that many consumers have difficulty finding their way through the plethora of available information and choosing the financial product that is right for them. In this case, it is in the customer's interest to pay for advice. The different charging structure as a result of the ban on inducements should not be an obstacle to this. Many consumers pay more attention to the costs in the short term rather than the long term, and tend either to not take advice or choose the lowest-cost adviser. The immediate visibility of the charges for service provision will increasingly turn consumers towards the direct channels of providers, banks and insurers, where advice appears to be cheaper or where they can invest independently or purchase products directly, without the services of an adviser. This does not mean that execution-only services are not suitable for certain customers: they have enough knowledge and the risk tolerance for an execution-only service, and thus are better off making their own decisions, without the intervention of an adviser.

Regulation of service provision to semi-professional en professional parties

Service provision to semi-professional en professional customers

Until now, it has always been assumed that semi-professional en professional customers (hereafter: 'professional' customers) were sufficiently competent to be able to ensure they were treated with due care. However, there have been developments and incidents in recent years that cast doubt on this assumption. Some professional parties are vulnerable in this respect, as in some cases it is quite likely that they do not have adequate knowledge of financial products and financial services, or of financial and other assets, to analyse products and service provision effectively. And although they lack knowledge, the products sold to professional parties are often complicated, meaning there is a greater need for good advice. These professional parties may be purchasing important financial products for themselves and their employees. There is a chance that the service provision may not be sufficiently appropriate.

Implementation of the AIFM directive

With the implementation of the AIFM directive in July 2013, many alternative investment firms such as pension providers, hedge funds, private equity funds and property funds that have until now been unregulated are now subject to supervision. The AIFM directive in principle applies to all managers at investment firms that do not fall under the regime for Undertakings for Collective Investment in Transferable Securities (UCITS). In practical terms, this means that the managers of these funds are required to obtain a licence or to join a public register and are now subject to ongoing supervision by the AFM.

The new supervision has the aim of gaining more control of the systemic risks that can be disseminated and/or reinforced by the behaviour of managers of large investment firms, including alternative investment firms. At the same time, the intention is to apply a consistent approach to the consequences of systemic risks for investors and markets in the European Union through the creation of an internal market for AIFMs with a consistent and strict regulatory and supervisory framework. The primary focus of the AIFM directive is on professional investors and their protection, but a continuing high level of protection for retail investors is also an important principle. The directive allows for the possibility of setting additional national regulations with regard to offers to retail investors. The new regulatory framework needs to be robust and adequately reflect Europe's chosen direction.

Pressure on the pensions system

The financial crisis, relatively low interest rates, increased life expectancy and demographic changes are pressuring the financial viability of the Dutch pensions system. Confidence in pension funds has declined, and the principle of intergenerational solidarity is under fire. Pension scheme members are facing a lower than expected pension and are taking more risk themselves as a result of the pension agreement. The effectiveness and the credibility of the second pillar pension is up for debate, since accrued claims no longer seem to be a certainty. This is feeding the public debate about the design of the pensions system.

Pension providers will be subject to a lot of new legislation. This requires well-substantiated choices by the pension providers as regards their ambitions and investment policies, and may require significant administrative changes by the pension providers. The new legislation on pensions communication is expected to include more open-ended standards. The market will have to communicate with the scheme members in a different way. Finally, the proposed limitation of the pension accrual that is tax-deductible will significantly affect the amount of pension accrued by scheme members. This will also require changes at the pension providers.

Low interest rates affects pension funds, insurers and institutional investors

Interest rates are low in the Netherlands and most of the rest of the world, in both nominal and real terms. The low level of long-term interest rates, as reflected in the yield on Dutch government bonds, is partly due to a flight to quality along with the policy stance on interest rates of the ECB. Low market interest rates encourage professional and other investors to take on more risk, for instance by investing in high yield bonds, in order to meet their return and solvency targets. The long-lasting low level of long-term interest rates has a significant and negative effect on the capital positions of pension funds, insurers and large institutional investors. The obligations of these institutions to policyholders and scheme members mostly have a very long term to maturity, and their value increases rapidly when interest rates fall. This effect is reinforced by low interest rates. The investments held against these obligations mostly have a shorter term to maturity and therefore they increase less in value. For insurers, these obligations mainly concern sizeable portfolios of guarantee products that were concluded in the past. The returns promised on the obligations are higher than the current market interest rates.

Quality of financial reporting

In view of the current economic conditions and prospects, issues regarding the valuation of assets, provisions and the associated disclosures will continue to be an important focus of attention in the next few years. In particular, the correct valuation of loan portfolios and commercial property is important for financial stability. It is still difficult to assess how reliable the information provided on property valuations actually is. Transparency regarding the valuation of assets and related issues is therefore a prominent item on the European agenda. The same applies to the comparability of financial reporting within Europe. The forthcoming Asset Quality Review (in connection with the announced formation of the banking union) will have a significant effect on the market, especially for banks in Southern Europe. It is important that the Asset Quality Review sets the same standards for all banks, which will in itself be a major challenge. The possibility that the Asset Quality Review will lead to further write-downs, also by Dutch banks, cannot be ruled out.

The continuing economic weakness could also affect the degree of transparency provided by financial and other enterprises, which will more often attempt to postpone unwelcome messages or measures. There is also the possibility that prospective developments will not be announced promptly and clearly enough. This will require the AFM to take an active role in encouraging parties to communicate adequately and in good time.

Excessive transparency requirements can have the opposite effect of that which is desired. There are increasing signals appearing, also internationally, regarding the scale of the information that must be disclosed in the annual report and financial statements. Users need to be able to access relevant information, and this is not always

achieved by providing more information. There is also a debate ongoing in Europe as to whether there should be a separate IFRS regime for SMEs. A (future) separate regime for SMEs could create two levels of transparency requirements in regulated markets.

The current (IFRS) reporting standards state the information that has to be presented, however until now there has been no standard for the quality of the presentation of this information. In the Netherlands, the development that the SBR/XBRL format for the provision of financial statements is expected to become mandatory as of 2015 is also a factor. The AFM will have to anticipate this in good time, make preparations and also inform investors if this turns out to be necessary.

Developments in the IFRS reporting standards could have a significant effect on the result and the statement of financial position of financial enterprises and construction companies (IFRS 9 and 11). Prudential elements will also increasingly feature in reporting, such as provisions for loans.

Increasing public attention for integrated reporting

Integrated reporting describes both a company's strategy, governance, performance and prospects and the social, economic and environmental context in which it operates. Integrated reporting thus addresses the questions asked by the public, which focus on understanding a company's performance instead of its figures. This new form of reporting is currently under intensive development. The European Parliament has stated that it will strive to achieve fully integrated reporting by 2020. The first draft framework of standards for integrated reporting does not include a role for auditors in the provision of certainty regarding the reliability of the non-financial information reported.

Developments in governance

Studies of the causes of the financial crisis show that problems at companies were to some extent due to inadequate governance and insufficient transparency with respect to governance. The European Commission recently announced measures intended to bring governance and shareholdership at issuing institutions to a higher level. In addition, CRD-IV is coming into operation for financial institutions and sets numerous new requirements for matters such as remuneration policy and the role of supervisory directors. In the spring of 2013, the government announced that it would submit a bill which would compel companies to be more transparent regarding their employees and directors earning high salaries.

Audit committees play an important part in safeguarding the quality of the reporting and the audit of the company. The issues they deal with include the selection and the evaluation of the quality of the auditor, the interaction with the auditor and how to deal with the information obtained from the supervisor regarding the quality of the audit (transparency with respect to the supervisor's findings). Audit committees appear not to have fully taken up this role, or not to be fully aware of it. Some audit committees can actively change the situation, since when appointing an external auditor they have to take account of the rotation of the audit firm they use, which will be mandatory from 2016. This new market situation in the Netherlands moreover means that audit committees will need more information in order to take up their role and thus give practical form to competition between audit firms on the basis of quality.

Now that these responsibilities are becoming increasingly explicit, there will be increasing pressure on supervisory boards, audit committees and other committees. The permanent provision of reporting to various stakeholders, the liability and the limitation of the number of supervisory directors are making supervisory directorships or membership of an audit committee more onerous. Companies will find it more and more difficult to find sufficiently qualified people who are eligible to be supervisory directors.

Reform of the auditing profession

Reviews by the AFM in recent years have identified significant problems and risks in relation to the quality of statutory audits at all types of audit firm. The risk and problem-driven selection of the statutory audits reviewed show that in a number of cases auditors had obtained insufficient or inappropriate audit information and had not conducted their audits with an adequately professional and critical attitude. Although some firms have already initiated a change in behaviour, or have already completed this process and dealt with the underlying causes of the problem, a great many firms still have some way to go in this respect.

At the same time, the public perception of the role of auditor and what is expected of an auditor is changing, with respect to both the scope of their activities and the audit work they perform. The public still has doubts regarding the added value of the auditor in his role as gatekeeper. This impression has been reinforced by a number of scandals.

The regulations applying to auditors and audit firms are continually changing. In view of the impact of the proposed regulation of the auditing profession as a whole and the supervision by the AFM, the AFM has much work to do here. At national level, this mainly concerns the proposals of the Netherlands Institute of Chartered Accountants (*Nederlandse Beroepsorganisatie van Accountants*, or 'NBA') for a new Regulation of conduct and professional rules and rules with regard to independence, the introduction of new rules for the separation of audit work from other activities (including advice) at the audit firms and rules for firm rotation. The Netherlands is leading internationally with this legislation. The AFM considers this to be an important step that will contribute to increasing the quality of the professional conduct of auditors in the Netherlands. At European level, the most important proposals concern those of the European Commission for the reform of the auditing profession (the Barnier proposals) and how centralised supervision should be conducted (either a role for ESMA in the supervision of audit firms or a European Board of Audit Oversight Bodies). These proposals will significantly affect regulations in the Netherlands. At global level, there are the proposals for new standards by the International Accounting Standards Board (IASB), the International Auditing and Assurance Standards Board (IAASB) and the European Enforcement Coordination Sessions (EECS).

Important changes in the trading location landscape

The locations at which financial instruments are traded in the Netherlands and Europe are currently subject to important changes and uncertainties as a result of developments in the regulatory framework and in the market. The major developments in the regulatory framework concern MiFID II, the European Market Infrastructure Regulation (EMIR), the Short Selling Regulation, the Central Securities Depository Regulation (CSDR), and possibly the financial transaction tax, all of which will greatly affect the market structure and the methods of processing and clearing of financial instruments. The most important development in the market is the forthcoming acquisition of NYSE Euronext by ICE, which involves a risk that the seat of the regulated market in the Netherlands will directly or indirectly disappear. For the management of the Amsterdam stock exchange and Dutch issuing institutions, there is a risk that they will have less of a grip on with trading in the market, less ability to innovate and less access to the market. Dependence on foreign supervisors will also increase, which could seriously affect the effectiveness of the Dutch capital market.

Another development in the market that will affect its structure concerns competition between and consolidation of stock exchanges and Central Counterparties (CCPs), and multilateral and bilateral trading locations. The profit

margins in securities trading and securities brokerage are under pressure due to the financial crisis, intense competition and technological advances. The growth potential for stock exchanges currently lies mainly in non-equity and derivatives trading, and the offering of integrated clearing services, also as a result of the (new) mandatory clearing and multilateral processing of certain Over The Counter (OTC) derivatives.

We are also seeing a trend whereby order flows are moving towards 'dark pools', at the expense of the stock exchanges (or 'lit venues'). The underlying motives are firstly the concerns of traders regarding the impact of large orders on the market and prices (pre- and post-trade transparency), and secondly the need of flow providers to reduce trading costs. As a result of the fragmentation of trading, the stock exchange is no longer the central location for monitoring trade. CCPs will over time develop into locations where all transactions come together.

Despite the implementation of the revised market abuse regulation in 2014, new forms of manipulation are developing that require attention. Cross-market and cross-asset manipulation are increasingly demanding attention from both supervisors and the trading platforms. Cross-market supervision is therefore increasing in importance. Non-EU parties are playing an increasingly significant part in this form of market abuse, which is making enforcement more difficult or even impossible. The arrival of automated trading in news on the basis of posts in social media could lead to new forms of information manipulation. The AFM is following these developments closely, so that it can take prompt action if necessary.

Further requirements for algorithm trading

The debate regarding the usefulness and added value of high frequency trading (HFT) is still ongoing. The European coordinated regulation is being driven by current political sentiment and the critical attitude of the public towards high frequency traders and algorithm traders. For instance, MiFID II will contain stricter requirements for this group, as well as the proposal for a coordinated European transaction tax. CRD IV, finally, may set additional requirements for proprietary algorithm traders. For a number of players, this will have irrevocable consequences for their earnings models.

Developments in the trading, clearing and derivatives market chain

The introduction of EMIR supervision in 2013 brings a group of non-financial enterprises under supervision by the AFM, including energy companies and non-financial trading houses. The effects of adjacent legislation in relation to the ban on derivatives trading by public and semi-public institutions are not clear. In particular, it is essential that the use of other instruments by these institutions instead of derivatives is monitored.

Increasing risk of corruption and fraud

Since the onset of the crisis and the financial pressure on the sector that ensued, parties whose earnings model has come under pressure are more likely to be tempted to trade in conflict with the regulations. The risk of fraud, or complicity with fraud, is thus expected to rise. In particular, we expect to see more signals and notifications with respect to the financial services sector. The risk of trading in breach of regulations is also increased as a result of the new and stricter regulations. Licensed parties are increasingly using evasive constructions, for example in order to circumvent new testing by policymakers, either due to bans or compulsory withdrawal of licences or for other reasons.

Financial criminality is increasingly becoming a cross-border phenomenon. More and more ill-intentioned fundraisers and loan providers from outside the Netherlands are now able to reach Dutch consumers. This emphasises the necessity of cooperation with foreign supervisors.

A number of financial institutions have become involved in various affairs in recent years in which unethical behaviour in the form of bribery and/or conflicts of interest by individuals played a role. Corruption harms

confidence in the financial sector. This type of breach of integrity affects the supervisory duties of the AFM. Recent affairs such as those involving SNS, Vestia and Imtech illustrate once again that the risk of (and involvement in) unethical behaviour is serious.

3 Targets for 2014 (thematic plans, in general terms)

The supervision conducted by the AFM is risk-driven. This means that the AFM carries out a risk analysis of the market and selects its supervisory themes on this basis. The AFM wants to concentrate its presence where the risks are greatest. Based on its strategic objectives and the external developments it observes, the AFM has decided to continue its nine supervisory themes in 2014.

This section describes the AFM's plans with respect to its nine supervisory themes in 2014, and lists the targets, intended effects and estimated resources needed for each theme. A long-term objective has been formulated for each theme, as well as the intended effects associated with this ("the strategic part"). Specific targets and effects have also been included for 2014 ("the operational part"). Each theme plan includes a section on the measurement of effects, in which we state how we will measure the intended effects of the theme in question.

In each theme, we refer to consumer behaviour, for example in the targets and intended effects. The AFM's efforts are nevertheless not strongly and directly focused on consumers. The effect of our supervision on consumers is largely indirect. We influence the financial enterprises by focusing our supervision on better provision of services and products for consumers. Here, consumers also have their own responsibility.

3.1 Product providers put the customer's interests first

Strategic part

Problem analysis

The theme of 'Product providers put the customer's interests first' was started at the end of 2009 in response to the credit crisis. The financial sector indicated at the time that the restoration of confidence was a top priority. The AFM's view is that keeping this promise to put the customer's interests first is essential for the restoration of confidence on a sustainable and well-founded basis. This is a lengthy process, and can be compared to a marathon.

A deeper reason for why the customer's interests are not automatically given priority in the financial market is that consumers do not exert sufficient pressure with respect to the price/quality ratio of the products and the services provided. The AFM does not see a realistic possibility that this will change much in the near future. The customer's interests will therefore only be given permanent priority if financial enterprises decide to embed this in their business models.

The theme focuses on financial enterprises, mainly banks and insurers (the providers). They have made great strides in recent years. Not only concerning adjustments to their mission, vision, core values and culture, but also in more practical areas such as policy on savings, interest-rate policy for mortgages, complaints management, the provision of investment services and product development, all of which directly benefit consumers.

The next phase of the marathon will also require changes to the business model (apart from changes imposed from outside such as the ban on inducements) and the intrinsic motivation and corporate culture. Furthermore, the degree to which a systematic link is made between the new mission and vision on putting the customer's interests first and integrated reflection of this in the targets, actions and results of the whole organisation varies per provider. In order to regain customer confidence in a sustainable way, the providers also have to work on their capacity for self-criticism, for instance with regard to the quality of their products and product development processes in the context of the customer's interests.

Main objective for the long term

The AFM wishes to encourage providers to continue to give the customer's interests priority in their culture and business conduct. This means that the customer's interests should play an essential part in their policy and practice. Providers should have a business model that continues to be profitable and focuses on the customer's interests. They should find a good balance between the interests of all stakeholders. Stakeholders should be able to rely on this. The products and services of the providers should meet the quality requirements of customers and of society, and not include any material disappointments that are foreseeable and that could get groups of customers into financial difficulties. Large-scale product-related scandals should thus be a thing of the past. Stakeholders, including consumers, should have the possibility of exercising effective influence on the providers. No special pressure from the supervisor is required for this new balance. All this contributes to renewed and deserved confidence in the financial sector.

Intended effects for the long term

The intended effect of the theme for society at large is a well-founded recovery of confidence in financial enterprises among consumers. The intention with respect to compliance is that providers should put their customers' interests first. Consumer confidence depends on many more factors than the scope of this theme, but achieving this compliance effect is certainly a precondition for achieving the desired social effect.

Operational part

Targets for 2014

- The AFM urges that products and services from providers should better serve the interests of customers.
We oppose the offering (or continued offering) of services, product types or features by providers that clearly do not serve the interests of customers. We are effectively encouraging the big 10 banks and insurers (G10) to achieve improvements through using the Customer Interests Dashboard to measure efficiently the extent to which they are prioritising their customers' interests. The AFM is encouraging them to contribute to improving this tool and to make these measurements.
- The AFM supports providers in their effort to focus more closely on the interests of customers.
We are encouraging the G10 to work towards a future individual business model in which priority for the customer's interests is fully embedded. Together with DNB, the AFM informs the providers regarding their individual limitations and opportunities for achieving the change they have in mind and encourages them to work continually towards this goal. We establish whether the G10 are in a position to measure their business conduct and to move towards putting the customer's interests first. Where needed, we encourage medium-sized providers to be self-critical and systematically improve their focus on putting the customer's interests first.
- The AFM makes it possible for the other social stakeholders of providers to play their part in the transformation to putting the customer's interests first.
We are increasing public involvement in the Customer Interests First process, for instance by publishing dashboard scores. We work together with other stakeholders of the G10 to encourage them to exercise effective influence on the G10 where possible and encourage consumers to take more responsibility themselves.

Intended effects in 2014

The intended effect on compliance – that financial enterprises should put the customer's interests first – has so far been increasingly successful. In terms of products and services, this is shown by the Customer Interests Dashboard. The target for 2014 is that the providers (the G10 and others) should continue this trend. Where necessary, we also want the providers to be more self-critical and more genuinely motivated to put the customer's interests first. We also want to see the G10 feeling more pressure from stakeholders other than the AFM to make the transition to 'Customer Interests First'.

Measurement

We measure the realisation of our targets systematically by means of the Customer Interests Dashboard (which shows the extent to which the G10 are fulfilling their commitment to put the customer's interests first in their products and their service provision) and our products radar (which we use to identify issues in product types and features). We also use more qualitative and anecdotal measures such as observations of the providers' internal organisations and management in the context of putting the customer's interests first.

Resources

Product providers put customer's interests first	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	13,6	12,0	10,9	-20%
Expenses as % of total	16%	14%	13%	-19%

*Estimated theme expenses (*EUR 1 m)*

3.2 The quality of financial service provision has improved

Strategic part

Problem analysis

The approach to the theme of 'The quality of financial service provision has improved' originates from our observation that on average the quality of advice provided by financial services providers was not up to standard. In 2010, we concluded that while quality had visibly improved, this development was proceeding too slowly and there had not been enough of an improvement in terms of a change of behaviour. The introduction of a ban on inducements for complex products with effect from 1 January 2013 was intended to bring about a change of culture from product-driven sales to customer-oriented service. This represented a radical change to the earnings models of the financial services providers, and has created competition on price and the quality of the service itself. In addition, consumers were (for the first time) confronted with fees for advice and for distribution. They thus became more critical with respect to price and the added value of the service. The challenge for this theme is to guide market parties and consumers through this transition, and at the same time to continue to strive for improvements to the actual quality of the service.

Main objectives for the long term

The strategic objective for this theme is to improve the quality of financial services provision. Financial services provision means the entire process of service provision, which starts with identifying the customer's needs, leading in turn to good advice and/or a product solution, and which is continued with after-sales service if appropriate. This process can take various forms, with or without the intermediation of an adviser. The quality that we wish to see meets the following conditions: the service should be cost-effective, useful, safe and comprehensible. This requires a fundamental change of behaviour by advisers, as well as by product providers and consumers. The theme has the following three medium to long term objectives:

- The AFM encourages advisers to act in the interests of customers.
- The AFM ensures that product providers make it possible for advisers (either independent or not) to serve the interests of customers.
- The AFM promotes an environment in which consumers are in a position to make well-considered decisions regarding their financial position.

Intended effects for the long term

The primary intention of this theme in a social context is that consumers should be assured of good quality if they need financial advice and/or they are themselves considering whether to purchase a product. This also means that consumers will be better able to find their way in this market and that they take a more active stance and make well-considered decisions in ordering and maintaining their financial housekeeping. This should contribute to proper provision for the consumer's financial future. The intended compliance targets relating to this are that financial services providers and product providers should as far as possible put the customer's interests first on their own initiative, and that they should be guided by the spirit and not only the letter of the law.

Operational part

Targets for 2014

A successful change process is based on the interplay of four mutually reinforcing elements: reward (and enforcement), direction, support and encouragement. In 2013 the emphasis in this theme was on the elements 'reward and enforce', and 'direction'. We did this by providing clarity to the market, and influencing or taking action against parties failing to comply with the ban on inducements and attempting to evade the pure market model. In the run-up to 2014 and during 2014, the intention is to emphasise support and to encourage positive developments. We are also responding to a clear appeal from the market. Furthermore, we will continue to monitor the degree of quality that is actually delivered.

- The AFM ensures that the new service concepts serve the customer's interests. Providers and independent advisers or intermediaries are developing new service concepts or adjusting existing models. This development represents both an opportunity and a risk with respect to the achievement of this theme's strategic objectives. In other words, we both encourage innovation that is in the customer's interests and at the same time act against harmful earnings models.
- The AFM checks that the quality of the service has actually improved, and encourages further improvement to the quality of financial services. We will concentrate more on the actual quality of the service provision. We thus intend to obtain information on the status of the actual quality of the service provision. We will furthermore focus on influencing service providers by encouraging them to make further progress with respect to quality in 2014.
- The AFM supports consumers in their efforts to find their way through the market for financial services. One unintended side-effect of the ban on inducements could be that consumers will be less inclined to take expert advice, even though they have difficulty in finding their own way. The service provision document has been one of the measures to overcome this risk. In 2014, we want to create boundary conditions for consumers to understand the pricing of the various kinds of service provision, what they receive for this and what this can yield for them. This will enable consumers to make well-informed decisions. We also wish to contribute by improving the consumers' awareness of what they can do themselves. This means that consumers are in a position to take action and know what actions they can take themselves.

Intended effects in 2014

In 2014, we want to see an increase in the number of new and existing business models from financial services providers that put their customer's interests first. In addition, the quality of the provision of financial services should improve in comparison to the previous 0-point and 1-point assessments for mortgage advice and the 0-point score for pensions advice. Depending on their needs, consumers will be able to find the right form of assistance or service to meet those needs, and be able to find this quickly.

Measurement

We carry out market research to become aware of the developments occurring and whether more new service concepts are being developed that put the customer's interests first. We take measurements (including reviews relating to duty of care) in order to determine the actual quality of the services being delivered. We will measure consumer behaviour by means of the consumer monitor that is frequently used by the AFM. We carry out stakeholder reviews to determine what the market thinks of the AFM's supervision in relation to the above objectives.

All these measurements are combined in the Market Monitor, which gives an overview of all the developments in the market and provides information on the changes in behaviour of the various players.

Resources

The quality of financial service provision has improved	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	12,0	12,2	7,0	-42%
Expenses as % of total	14%	15%	8%	-41%

*Estimated theme expenses (*EUR 1 m)*

The costs will be lower than in 2013, because some of the activities have been moved to the theme 'Harmful behaviour and financial crime diminish'. Without this move, the costs of this theme will fall by around 10%.

3.3 The quality of capital accumulation has improved

Strategic part

Problem analysis

Approximately one million households in the Netherlands invest actively. However the vast majority of households invest passively, by means of savings products or capital accumulation as part of a mortgage, for the accrual of a pension or an annuity product. This will only become more prevalent in the near future, due among other things to the underfunding of pension funds and the growing number of employees that are responsible for their own pension accrual (including self-employed persons with no employees (ZZP-ers)). Based on past experience and the lack of knowledge among consumers, combined with factors such as the complexity of investing and the charging structures of products and services, there is a serious risk (and therefore it is foreseeable) that consumers will be disappointed. Various signals and reviews show that the customer's interests are not put first in the services on offer for the retention and accumulation of capital, and that customers are not always aware of the substance, risks and charges involved in these services.

Main objectives for the long term

The AFM encourages investment firms and collective investment institutions to put the customer's interests first in their services for the retention and accumulation of capital. The underlying aims here are:

- The AFM strives to improve the quality of services to consumers for the retention and accumulation of capital.
- The AFM contributes to raising awareness and consumer scepticism with respect to services for the retention and accumulation of capital.

Intended effects for the long term

The intention of the theme in social terms is to encourage justifiable consumer confidence in the services for the retention or accumulation of capital that suit their specific financial situation and needs. To achieve this, it is crucial that consumers can really rely on the quality of the services and the service providers. There are two aims in terms of compliance and the social context:

- The quality of services for the retention and accumulation of capital is increased, and these services add value for customers.
- Consumers become more aware and more critical with respect to the realisation of goals, the charges and the added value of services for the retention and accumulation of capital.

Operational part

Targets for 2014

- The AFM will promote improvement to the quality of investment advice and individual portfolio management by investment firms.
- The AFM will strive to increase the quality of services and service concepts of investment firms for execution-only services.
- The AFM will encourage innovative possibilities for the offering of bespoke services and service concepts by investment firms.
- The AFM will contribute to the implementation of the ban on inducements for investment firms.
- The AFM will offer practical instruments and tools to consumers (and their representatives) to enable them to more aware and more critical with regard to the capital retention or accumulation.
- The AFM will promote the implementation of measures to enable consumers to easily understand the costs of the service provision.

Intended effects in 2014

In 2014 we hope to achieve a situation in which the quality of services improves with respect to specific elements in the field of investment advice and individual portfolio management. The services and service concepts of investment firms for execution-only services should add value and be of sufficient quality, and innovative options should be used for the offering of bespoke services and service concepts. Market parties and consumers will use direct fees for services. Consumers (and their representatives) will then be in a better position to take a critical view of services for capital retention and accumulation. Consumers will be in a position to easily (or more easily) understand the costs of the services provided by investment firms and collective investment schemes.

Measurement

- Based on the AFM Consumer Monitor and other studies, we will establish whether confidence in and behaviour with respect to services for capital retention and accumulation is changing;
- On this basis, we also establish whether consumer evaluation of services for capital retention and accumulation is changing. With the Customer Interests Dashboard 2014, we will measure whether the quality and degree of cost transparency of investment services is changing;
- We will critically review how many banks and investment firms are moving to a commission-free model during 2014;
- Based on the self-assessment by investment firms and collective investment schemes, we will check the extent to which there is a change in the attitude and behaviour of financial institutions.

Supervision of alternative collective investment schemes as a result of the AIFM directive

As a result of the introduction of the AIFM directive, the AFM has been supervising alternative collective investment schemes such as hedge funds, private equity funds and property funds since July 2013. In practical terms, this new duty means that AIFMs are required to obtain a licence or to join the public register, and be subject to supervision.

The AFM's targets for this group of AIFMs are:

- The AFM is making a substantial contribution to the further development of a robust (European) harmonised and stringent regulatory framework.
We will do this through cooperation and dialogue with the market, the government and foreign supervisors. The intention here is not only to achieve harmonised regulations for the protection of professional investors, but also to ensure that retail investors continue to enjoy a high level of protection.
- The AFM will monitor the issuance of licences and registration, and will provide guidance to market parties in the implementation of measures in order to comply with legislation and regulation.
In addition to the existing 110 non-UCITS fund managers that are currently in possession of a licence based on our national Wft regime, the AFM expects to grant licences to approximately 70 new fund managers and to register a further 180. The new AIFM regulations constitute a significant change from the existing rules applying to collective investment schemes. We will provide guidance, in particular with respect to new issues such as remuneration policy and regulations applying to custodians, and we will monitor compliance.
- The AFM will work together with DNB in order to identify potential systemic risks arising from the behaviour of managers of alternative and traditional collective investment schemes.
We will focus on the conduct aspects, such as the avoidance of conflicts of interests, appropriate risk and liquidity management, independent measurement of the assets and transparency with respect to obligations.

- The AFM will develop an effective supervisory framework and strategy in 2014.
We will increase our focus on potential problems and will adjust our future supervisory strategy in this light with the aim of maintaining supervision that is problem and risk driven.

Intended effects in 2014

- European harmonised regulation will create a level playing field for market parties and will create an internal market for AIFMs.
- Retail investors will continue to enjoy a high level of protection.
- Market parties will know what to expect from the AFM, and what the AFM expects of them in the light of the AIFM regulations.
- Better control of systemic risks that can be disseminated and/or reinforced by the behaviour of large alternative and traditional investment funds.

Resources

The quality of capital accumulation has improved	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	7,4	8,7	10,4	40%
Expenses as % of total	9%	10%	12%	41%

*Estimated theme expenses (*EUR 1 m)*

The costs of this theme will rise in 2014 as a result of the introduction of the AIFM directive. The costs of this theme do not include the costs of non-recurring services (such as the AIFM licences and public registrations). The costs of non-recurring services must, under the Financial Supervision (Funding) Act (Wet bekostiging financieel toezicht), be stated separately and are therefore included in section 3.10.

3.4 Financial services provided to professional and semi-professional parties is appropriate

Strategic part

Problem analysis

There were developments and incidents occurring in 2012 and 2013 that raised questions regarding the assumption that all professional and semi-professional parties (hereafter: 'professional parties') needed less legal protection than consumers. Until now, it had always been assumed that professional parties were able to look after themselves, or that they would be sufficiently assertive and/or possess sufficient financial resources to obtain adequate assistance. Supervisory information indicates that this does not apply to all professional parties.

The AFM has observed signals that there are problems relating to inappropriate service provision to SMEs with respect to interest-rate derivatives. It is difficult for these business parties to avoid losses as a result of an inadequate financial product or inappropriate financial service and to recoup these losses afterwards. SMEs often do not have adequate knowledge and experience of financial products and services. They also do not have the time or the capacity to check whether the products and services concerned are suitable. They are therefore not very different from the average consumer, however they do not enjoy the same level of legal protection. This may also apply to self-employed persons and some other professional parties in the civil society, for instance in health care, education and social housing.

Some of these developments and incidents concerned:

- Problems resulting from interest-rate derivatives at public and semi-public institutions.
- The service provision by some banks to professional SMEs in the purchase of interest-rate derivatives could be improved.
- The growing number of smaller companies and self-employed persons that are similar to consumers in many respects, but which do not (always) enjoy the same level of legal protection.

Main objectives for the long term

The AFM promotes adequate service provision for professional parties that encounter problems. The AFM will do this by obtaining information on the market for service provision to businesses and the potential problems in that market. In addition, we are formulating a role that is appropriate for us in reducing (or helping to reduce) potential problems and preventing them occurring in future.

Our focus will be on professional parties which in view of their knowledge and experience of financial products and services are not sufficiently equipped to estimate the potential risks in this area. We shall also focus on professional parties designated as public or semi-public institutions or which are in civil society, for example in the education or the health care sector.

Intended effects for the long term

The provision of more appropriate financial services to professional parties which in view of their knowledge and experience of financial products and services are not sufficiently equipped to estimate the potential risks in this area. Financial enterprises should exercise due care in consideration of the legitimate interests of these parties and should act in their interests. With a more appropriate service provision, professional parties will be able to make more well-considered choices in their financial decisions. The services and financial products provided to these professional parties should add value, and the information provided should be balanced and clear.

Operational part

Targets for 2014

- The AFM will obtain information on the market for service provision to businesses, and the potential problems in that market.
- The AFM will influence the behaviour of the financial enterprises concerned, by means of both encouragement and enforcement, so that business parties purchase suitable products or financial services. The financial enterprise will base its service on the interests of the business party concerned.

Intended effects in 2014

A financial enterprise will exercise due care in the consideration of the legitimate interests of the business party, and in cases where it gives advice, it will act more in this party's interests. More financial products offered and/or recommended by financial enterprises will offer sufficient added value for the business party.–Furthermore, the provision of information on financial services and products will be more balanced and clearer.

Measurement

We will conduct case reviews regarding advice and the offering of products other than interest-rate derivatives and will review the external and internal policy of the banks and insurers with respect to their product development process. We will also carry out checks with respect to transparency requirements and fulfilment of the duty of care in relation to specific products (for instance, in case of the provision of information).

Resources

Financial services provided to professional and semi-professional parties is appropriate	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	1,6	0,9	1,4	-10%
Expenses as % of total	2%	1%	2%	-9%

*Estimated theme expenses (*EUR 1 m)*

3.5 Pension providers provide an overview of and insight into the amount of pension, and the risks to pension

Strategic part

Problem analysis

Economic, demographic, market-related and policy-related developments will lead to a curtailment of pensions and increasing transference of risks to the scheme members. Ideally, pension scheme members will anticipate their future loss of income on retirement and the uncertainty related to this in good time. Most pension scheme members however are not interested in planning for retirement. Only one in ten employees in salaried employment says they are aware of their pension income, in other words whether this will be sufficient and what possibilities there are for additional savings. This is partly due to the way in which pension information is provided, which does not always include the information that scheme members need. Scheme members are not being given enough guidance on how they can take independent action to make financial plans for their retirement.

The transference of risk from employers and pension funds to the scheme members also makes it more important that scheme members save in a cost-effective pension scheme that is tailored to meet their requirements. Due to the significant effect on future pension incomes, attention should be devoted to the comparability of pension schemes. Currently, there is no information available on which to base a comparison of pension schemes in an easily accessible form. This means that employees who change their job have little information on the difference between their current and future pension schemes, and whether they need to adjust their financial planning. Scheme members moreover have different risk tolerances, and it is becoming increasingly important that pension funds take account of this. Lastly, economic, demographic, market and policy developments will put the effectiveness and credibility of second pillar pensions under pressure. This is feeding the public debate about the design of the pensions system.

Main objectives for the long term

- With its work, the AFM will contribute to the possibilities for pension scheme members to take action and for a credible pension.
- The AFM will encourage a gradual development of the pensions public register into a pensions dashboard, and into a financial dashboard in the longer term. It will thus contribute to a form of information provision that will enable pension scheme members to make well-considered decisions and to plan for their retirement.
- The AFM will encourage the sector to provide a cost-effective pension that is as simple as possible and is appropriate for the scheme members. It will contribute to the comparability of pension schemes for various stakeholders. Lastly, the AFM will follow the debate on the design of the system and will, if so desired and if appropriate, contribute on the basis of its expertise and mission.

Intended effects for the long term

Consumers should be able to plan for their retirement on the basis of clear information on pensions. The sector should provide a cost-effective pension scheme that is not unnecessarily complicated and that is appropriate for the scheme members.

Operational part

Targets for 2014

The AFM will give advice regarding the further development of the pensions public register into a pensions dashboard, so that more scheme members will be in a position to make effective financial plans for their retirement. It will also consider the content of new legislation with regard to communication on pensions in 2014. This legislation is expected to include more open-ended standards, instead of the narrowly defined regulations we have been used to until now. This will make the resource of pension information better suited to the objective (to

enable consumers to make effective financial plans for their retirement). The AFM will also consider the practical options for the design of pensions comparison tool.

The AFM will influence the elaboration of the technical standards of the European pensions regulator associated with a proposal from the European Commission on governance and the provision of information. The AFM expects to contribute to a review by the European pensions regulator of the provision of information and the fulfilment of the duty of care regarding investment decisions in contribution-based agreements.

The AFM will encourage appropriate communication by pension providers to scheme members as part of the transition to a new Financial Assessment Framework. This will require substantiation of the choices made by the pension providers with respect to their ambitions, the pension agreement and their investment policy. A new Financial Assessment Framework is scheduled to come into effect in 2015.

Intended effects in 2014

Pensions communication should contribute to financial planning for retirement. Pension providers should see additional opportunities for providing information on pensions that enable scheme members to plan financially for their retirement, and policy should be developed to reflect this. The pensions public register should plan for the development of a pensions dashboard. Lastly, interested scheme members should be able to find easily accessible information on the implications of the transition to new contracts for personal pension accumulation, the choices these pension providers have made for the new contract and the arguments taken into consideration in this process. The sector should provide efficient and not unnecessarily complicated pension schemes. The administration costs of pension funds should become more transparent. Pension providers should moreover ensure that their pension schemes are tailored to the scheme members. There should be information on the extent to which account is taken of scheme member profiles in the choice of investment strategy and the consideration of interests and decision-making in this context.

Measurement

- A thematic review of the accessibility and comprehensibility of information from pension providers and in the pensions register;
- A review of the accessibility and comprehensibility of information on the new contracts, the implications of this and the considerations that the pension providers have made;
- A review among consumers as to how they access information and whether they understand this information.

Resources

Pension providers provide an overview of and insight into the amount of pension and the risks to pension	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	3,9	4,3	3,5	-10%
Expenses as % of total	5%	5%	4%	-9%

*Estimated theme expenses (*EUR 1 m)*

3.6 The quality of governance, reporting and audits will improve

Strategic part

Problem analysis

The proper functioning of the capital markets depends on the conduct of the players in those markets. Problems at companies are to some extent explained by shortcomings in governance and lack of transparency in this area. Audit committees apparently are not fully exercising their role with respect to the quality of the company's reporting and auditing process.

Good corporate governance contributes to the proper functioning of the capital markets. Good corporate governance and transparent reporting on the design and operation of corporate governance deserves attention, as well as reporting on the company's strategy and financial and non-financial performance and the company's risks and risk management related to this performance. Auditors check the reliability of the reporting and the accounting included therein, and avoid a situation in which every user would have to check for reliability themselves. The critical exercise of this role and the quality of both the preparers and the auditors of reporting are therefore essential for good corporate governance.

Transparency with regard to financial and non-financial performance also continues to be crucial. Issues relating to the measurement of assets and provisions and the disclosure of these items will continue to require close attention in the coming years. The importance of comparability of financial reporting, both in Europe and worldwide, is increasing. The current regulatory trend is that an increasing amount of information should be excluded. Relevant information has to be included, but this does not always mean including more information. Better quality information, for instance in the disclosures, is what is needed.

The quality of the statutory audits performed by auditors working for audit firms is not yet at a satisfactory level. Although as a result of its reviews of the audit firms the AFM has called for the initiation of a change in behaviour and for the audit firms to deal with the causes that underlie the existing shortcomings, a large number of organisations still need to make further efforts in this area. Furthermore, the regulations governing auditors and audit firms are changing; a change that is needed. This constitutes both additional directions and challenges for the AFM's supervision.

Main objectives for the long term

The main objective of this theme is to increase the quality of governance, reporting and auditing. This is subdivided into four subsidiary objectives:

- The AFM will appeal effectively to institutions' individual sense of responsibility, achieving a change of attitude, and thereby increase the quality of governance.
- The AFM will encourage the development towards a reporting system of integrated reporting in the long term. Companies will present both their strategy and their financial and non-financial performance in integrated form. The current reporting model focuses mainly on the financial performance and position alone. This model offers limited scope for communication on non-financial factors that are also relevant for the realisation of the company's targets and for the development of the company's value in the longer term. Furthermore, integrated reporting presents a more balanced view of the company's risk profile, its dependencies and its ability to continue as a going concern. This wider focus and integrated reporting is also expected to manifest itself in the way the company is managed and the priorities it sets.
- The AFM will strive to ensure that statutory audits are conducted with professional scepticism and are of adequate quality. The audit firms will set the right standards for their internal quality monitoring and will themselves review the quality of audits on a regular basis. It is essential that they obtain information on the quality of their external auditors, the quality measures relating to the audits and the extent to which their corporate culture encourages quality. The AFM wishes to see more competition between audit firms with regard to the quality of their service provision instead of competing on the basis of price alone.

- The AFM will make a contribution whereby regulations will become more effective, and enforcement will be better and more consistent. The AFM will participate in the relevant national and international forums with this aim.

Intended effects for the long term

The effects we wish to achieve with this theme are described in more detail for each subsidiary objective below:

- Supervisory boards should exercise more effective supervision of the quality of reporting and auditing. The 'audit quality indicators framework' that is being developed by various parties internationally is an important tool in the initiation of a dialogue with the audit firms regarding their role in relation to the auditor.
- Reporting should more frequently meet qualitative criteria such as relevance, a true and fair view, comparability, comprehensibility, timeliness and the possibility of verification.
- Auditors should identify risks, report on these risks and their statements should become more transparent and be more frequently adequately substantiated, and the activities of auditors should at all times be carried out with a professionally sceptical attitude.
- National and international legislation and regulation should encourage better quality reporting and auditing.

Operational part

Targets for 2014

- The AFM will intensify the ongoing dialogue with audit committees next year. Audit committees play an important part in safeguarding the quality of the reporting and the audit of the company. If audit committees do their job properly, the AFM would expect to see the benefits of this in its supervision.
- The AFM will ensure that reporting more frequently meets the qualitative criteria stated above. The AFM will devote special attention to transparency with respect to assets, and their measurement. In the context of the debate on the plethora of disclosures, the quality of the information presented will be improved, but not the quantity. The AFM will moreover support the formulation of good international standards for integrated reporting and their application in a national context, and, where possible, the AFM will contribute to further improvement in the quality of integrated reporting.
- The AFM will obtain information on the quality of the audits conducted by the Big 4 firms. Where necessary, it will also bring about a change of behaviour at all types of audit firm with the aim of increasing the quality of audits; Lastly, it will enter into dialogue with the global top six audit networks through consultative bodies including the International Forum of Independent Audit Regulators (IFIAR) and the European Audit Inspection Group (EAIG) with the aim of increasing quality at international level.
- The AFM will influence developments in legislation and regulation through the relevant national and international regulators with the aim of improving the quality of reporting and auditing. It will contribute to ensuring consistent application of the reporting regulations in Europe, with the aim of increasing the international comparability of financial reporting.

Intended effects in 2014

- A more critical attitude by audit committees to improve the quality of the audit and the company's reporting. A more independent stance by the auditor towards the company being audited.
- Better quality financial reporting as a result of more notifications being adopted by companies, less use of standard texts ('clutter' or 'boilerplate language'), and inclusion of more relevant disclosures. Increased use of integrated reporting by companies.
- Audits will meet the expectations of the public more frequently and will be of better quality, the Big 4 firms will be aware of the factors that raise or limit quality, and the Next Nine PIE firms will show a real change in behaviour. The quality standards used by the AFM will be clearly understood by the people at the audit firms charged with quality control; The sector, the NBA and the Association of Chartered Accountants (*Samenwerkende Registeraccountants en Accountants-administratieconsulenten*, the 'SRA'), will take measures to improve quality.

- Better regulation and more consistent application of the European regulations, for both reporting and auditing, and clear, unambiguous and more restrictive regulation regarding independence and uniform regulation for the reports issued by auditors to financial and non-financial reporting.

Measurement

We will use the following indicators to measure effectiveness in realising the targets for 2014:

- The number of notifications in relation to financial reporting that are adopted;
- The number of requests for information sent, and the number of notification letters per reporting issue;
- The number of companies that apply integrated reporting;
- The findings of the reviews of the audits by Big 4 firms and the non-PIE firms reviewed in 2013 (1-point assessments); The 0-point assessment was carried out for the Big 4 firms in 2009/2010, and for 50 non-PIE firms in 2013;
- The findings of the tests carried out by the NBA and SRA in 2014;
- The way in which the Big 4 firms and the Next Nine PIE firms express themselves publicly with respect to the quality of their statutory audits and the measures that they take in this context.

Resources

The quality of governance, reporting and audits will improve	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	13,9	14,0	14,3	3%
Expenses as % of total	16%	17%	17%	4%

*Estimated theme expenses (*EUR 1 m)*

3.7 The securities markets operate fairly and efficiently, and the infrastructure remains robust

Strategic part

Problem analysis

The capital markets have gone through many changes in past years, involving increasing competition and rapid technological development. Competition for the central role that used to be the preserve of the stock exchange has led to fragmentation. To some extent this is due to technological developments, but European and national regulation has also played a role. The strategic role of the stock exchange and alternative trading platforms will once again have to be determined by the market, but also by the supervisory agencies. European harmonisation is needed for a strong European market with a global orientation. Technological developments also affect the capital markets and innovation in these markets. Information is more rapidly available on the order books and transactions in these markets, also when they are situated in various locations. Technological innovation also has a dark side, in the form of cybercrime. This risk is also recognised by external parties. The use of social media can moreover have a large impact on forms of market abuse.

Attention to the systemic risk of clearing and settlement organisations has rightly increased. Regulations for this are being developed in Europe and elsewhere, but new parties will become subject to supervision also at national level as a result of the implementation of EMIR.

Investors need to have sufficient information in order to make decisions. They need to be as well informed as possible in order to assess whether the products on offer in the capital markets are in their interests. Experience in practice shows that the information provided by market parties often does not meet the needs of the various types of investor, while the products that are offered are not always in the interests of investors.

Main objectives for the long term

The strategic objective of this theme is the fair and efficient operation of the capital markets. This will enable the capital market in the Netherlands to optimally serve the real economy on the basis of its four key functions: the allocation of capital, the redistribution of financial risk, the valuation of financial instruments and the provision of liquidity. This objective contributes to reducing the risk of market failures in the capital market and the justified confidence of the various participants in the market.

This theme includes the following subsidiary objectives:

- The AFM will act against market abuse and will control the most serious forms of market abuse through proactive and effective action.
- The AFM will contribute to the stability of the capital markets system.
- The AFM will promote the efficient and orderly functioning of the infrastructure.
- The AFM will contribute to investors having all the information they need to make well-informed investment decisions, both in the primary capital market and for public takeover bids.
- The AFM will encourage the provision of information on the products being offered in the capital market to state prominently that these products are in the interests of investors.
- The AFM will contribute to even-handed treatment of shareholders in case of public takeover bids for securities and an orderly takeover process.
- The AFM will strive to achieve effective national and international cooperation in order to realise its objectives.
- The AFM will influence and promote the quality of European regulation.

Intended effects for the long term

The aim of this theme in social terms is that the Dutch capital markets should operate as efficiently as possible. The Dutch capital markets enjoy justified confidence, they are stable and have low barriers to trading and admission. This allows the capital markets to serve the real economy to the greatest possible extent, which contributes to a favourable environment for investment, economic growth and the creation of collective prosperity. More specifically, we aim to achieve the following effects:

- The perception in the market should be that the AFM is in control with respect to market abuse and the settlement of transactions.
- The infrastructure should operate robustly and feature orderly access, efficiency, transparency and competition.
- The integrity of market participants should increase as a result of the AFM's supervision, so that they take adequate action on their own initiative to prevent abuses. Moreover, market parties will be more inclined to enter the capital markets.
- Investors should have the necessary information to take well-founded investment decisions, they should be treated equally during public offerings and the information and products provided should be in their interests. In addition, the bidding process should be orderly.
- European regulation with respect to the capital markets should correspond to the objectives of the AFM.

Operational part

Targets for 2014

In its supervision of market abuse, the AFM will continue to develop the risk-driven approach initiated in 2013. The AFM acts decisively against market manipulation, insider trading and failure to publish price-sensitive information promptly or in full. The focus is on significant cases that could seriously undermine confidence in the capital markets. We will also focus on a number of as yet unused opportunities to combat market abuse through our thematic reviews and the application of various influential measures.

In 2014, the AFM will study what investments are needed in IT to keep its monitoring and investigative systems up to date. Ongoing technological innovation will place additional demands in 2014 (and thereafter) with respect to the prevention of market abuse and supervision of the financial infrastructure. In this context we are looking mainly at market abuse by taking simultaneous positions or executing transactions in different (more or less transparent) markets or in different financial instruments, other than genuine arbitrage, and the increasing threat of cybercrime.

The AFM will further roll out the supervisory strategy in relation to EMIR, meaning that there will be three areas of attention. These are: risk management of OTC derivatives transactions and the reporting thereof, mitigation of central counterparty risk and the setting up of a transactions register.

The AFM will contribute to necessary information being made available to investors by means of reviewing prospectuses, offering memorandums and advertisements. In addition, there will be a focus in 2014 on encouraging a situation in which the information provided to investors on the products offered in the capital market and the products themselves are in the interests of investors. In case of a public takeover bid, the AFM monitors that the conduct rules governing the equal treatment of shareholders and the orderly conduct of the bidding process are observed.

The AFM strives to influence European regulation and focuses on the implementation of the rules governing market abuse and infrastructure (Market Abuse Directive II (MAD II), Market Abuse Regulation (MAR), MiFID II, MiFIR and CSDR). The technical details of this implementation will be worked out in the context of ESMA in 2014. The AFM will moreover contribute to influencing the harmonisation of prospectus requirements in the context of ESMA.

Intended effects in 2014

We expect achievement of our targets to have the following effects:

- The AFM will be seen by the market as an effective supervisor in the areas of market abuse and securities transaction settlement.
- More market parties will report potential abuses and will take adequate action against abuses on their own initiative.
- The risks taken by market parties will receive increased attention on the basis of the notifications in the EMIR transactions register and the steps taken by the AFM.
- For investors, information will become available on capital market transactions that is necessary for taking a well-founded investment decision. Parties raising capital will put the interests of investors first in the provision of information and the offering of products. Products that may not be in the interests of investors will be more visible in the market.
- Bidding processes will proceed in an orderly manner and investors will be treated equally.
- Influence on European and national regulation will contribute to improved regulation.

Measurement

- Quantitative performance indicators such as availability of trading systems, information on errors in the settlement process, but also in the number of notifications of market abuse and administrative penalties and legal judgments;
- More information will be obtained on qualitative criteria through stakeholder analysis;
- Comparison with foreign supervisors as regards their supervisory strategy and quantitative indicators;
- Assessment of the extent to which information for investors is changed as a result of supervision, and the extent to which the bidding rules are observed by the bidders;
- The number of products that are changed or withdrawn by parties seeking to raise capital as a result of the need to inform investors properly and to put the interests of investors first.

Resources

The securities markets operate fairly and efficiently and the infrastructure remains robust	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	11,9	11,8	12,4	4%
Expenses as % of total	14%	14%	15%	5%

*Estimated theme expenses (*EUR 1 m)*

The costs of this theme do not include the costs of non-recurring services (such as the testing of prospectuses and tender offers). The costs of non-recurring services must, under the Financial Supervision (Funding) Act (*Wet bekostiging financieel toezicht*), be stated separately and are therefore included in section 3.10.

3.8 Conduct supervision contributes to the stability of the financial system

Strategic part

Problem analysis

Financial stability has only become more important in the aftermath of the credit crisis and the debt crisis. There are several important lessons to be learnt from the crises in relation to the supervision of financial stability. The feature of financial stability supervision in the recent past is that supervision has been conducted mainly at sector level, or at the level of individual institutions. The focus has been mainly on increasing the capital of financial institutions in order to absorb shocks, with relatively little attention paid to the markets through which institutions are mutually connected. Market problems such as a false impression among investors of the risks of financial products and the (alleged) hiding of losses in bank balance sheets were actually the cause of the current crisis. The financial system may become unstable due to the occurrence of a particular risk (a shock), whereby several 'players' in the financial system get into difficulties because of interconnection (contagion). In view of the social function of the financial system, disruption can have negative consequences for the real economy. The fact that problems usually affect several sectors and cross borders is a challenge for this theme. It is thus important that a system-wide perspective is maintained, so that the right sort of cooperation is initiated and so the AFM can effectively fulfil its role with regard to financial stability thereafter.

Main objectives for the long term

The AFM identifies potential risks to stability in the Dutch financial system and initiates activities through its conduct supervision to limit these risks. Together with DNB, the AFM creates the preconditions for a financial system with manageable and transparent risks. As the conduct supervisor, the AFM supervises the orderly operation and stability of the trading infrastructure, the actions of market parties that could undermine financial stability and the transparency of systemic risks.

Intended effects for the long term

The AFM's intention with this theme is to overcome risks and keep risks that threaten the stability of the Dutch financial system manageable. We strive to limit risks to stability, to reduce the exposure of players in the financial system (such as financial institutions, markets, and clearing and settlement organisations) to stability risk, and to reduce the effect of stability risk on the financial system.

Operational part

Targets for 2014

As in 2013, the focus of this theme in 2014 will be on the identification, analysis and itemisation of systemic risks and risks with systemic relevance. In addition, projects may be initiated in order to mitigate risks to stability. The AFM works closely here with DNB and the Financial Stability Committee (FSC), which has been formed in order to obtain a good overview of risks at national level. The FSC consists of representatives of the Ministry of Finance, DNB and the AFM. The committee identifies developments that are important for financial stability and can make recommendations. The AFM identifies systemic risks arising from the conduct of participants and the products offered in the securities and other markets, instability in the trading infrastructure and lack of transparency, and draws attention to these issues in the FSC. At international level, this activity is carried out through the European cooperative agreements ESMA, ESRB and IOSCO (International Organisation of Securities Commissions), the global organisation for securities regulators.

With our partners, we strive to reduce risks to stability in priority areas at national and international level. Prior to this, the AFM's contribution consists of identifying, establishing the nature of and prioritising potential risks to the stability of the Dutch financial system.

Intended effects in 2014

The effect intended is that a true picture is obtained of the major potential risks to the stability of the Dutch financial system in 2014. Measures have been taken in relation to some of the risks identified that reduce the potential impact of the risk concerned and the exposure of individual participants to that risk.

Measurement

Financial stability is not an area in which the effects of supervision can be easily measured. It is indeed difficult to measure the effect of supervision that focuses on preventing a particular situation occurring. Measurement will therefore consist of establishing the likelihood that a certain risk forms a threat to the operation of the Dutch financial system, and therefore constitutes a potential risk to stability. The assessment of the likelihood that stability supervision will be effective is based on a number of derived indicators, based on the minimum conditions necessary for the existence of instability in the financial system, such as: stability risk, vulnerability of participants in the financial system and the impact of this risk on the financial system. The effect is measured on the basis of the reduction in the identified risk to stability, the reduction of vulnerability of participants to the risk and the reduction of the potential impact of the risk on the financial system.

Resources

Conduct supervision contributes to the stability of the financial system	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	1,9	1,5	1,7	-8%
Expenses as % of total	2%	2%	2%	-7%

*Estimated theme expenses (*EUR 1 m)*

3.9 Harmful behaviour and financial crime diminish

Strategic part

Problem analysis

Some market participants will always exhibit harmful behaviour, just because there are opportunities to make money easily from consumers by misleading them, in the broadest sense of the word. Harmful behaviour is continually adjusting to market developments, and therefore manifests in different forms. A minority of market parties go further than exhibiting harmful behaviour and are either guilty of criminal behaviour themselves or facilitate such behaviour by others. This type of behaviour seriously damages consumer confidence, it disrupts the level playing field for market participants, and damages the integrity of the system.

In addition, the financial crisis has increased the risk that market participants will display harmful behaviour, since they are under financial pressure and may therefore be more easily tempted to break the law. In order to be able to act effectively against harmful behaviour, it is essential that the AFM considers the entire chain for the provision of financial services and cooperates effectively with its partners in the enforcement chain.

Main objectives for the long term

The strategic objectives of this theme are:

- reducing the impact of harmful behaviour on the financial market; and
- reducing the number of parties guilty of criminality or facilitation of criminality, and deterring those inclined to indulge in such activity.

The first objective concerns harmful behaviour that has the greatest effect on consumer confidence in the market and the level playing field for market parties. This concerns intentional misleading activity in the service provision chain and gross abuses in the rescheduling market. Both strategic objectives contribute to strengthening confidence in the financial market among consumers, investors, capital providers and financial institutions, protecting a level playing field and strengthening the integrity of the system. By extension of the above, the AFM intends to improve its operational intelligence gathering, as well as the cooperation with other national and international partners in the enforcement chain.

Intended effects for the long term

The intended long-term effects of the above objective are:

- Previous offenders will no longer operate in the financial market, or will improve their compliance with financial legislation and regulations, and will act in the spirit of the legislation and regulations.
- The impact of damaging earnings models and financial products will decline substantially, so that the losses suffered by consumers and the harmfulness to market participants acting in good faith will be reduced.
- A decline in the 'copycat effect', meaning that new potential offenders will be deterred by the actions of the AFM.
- Improved system integrity so that criminal activity is more difficult to commit, or be facilitated by financial enterprises.
- A stronger perception in the market that harmful behaviour will be dealt with.

Operational part

Targets for 2014

In its actions against harmful behaviour, the AFM always has to make clear choices regarding which types of behaviour it will actively deal with and which it will not. The decision-making process regarding which types of supervisory issues are to be dealt with is driven by the effect of the harmful behaviour in question. Furthermore, successfully dealing with harmful behaviour in the market requires an integrated approach to the supervisory

issue whereby the entire chain of market participants concerned that contribute to the supervisory issue is considered. This requires effective cooperation with the partners in the enforcement chain.

The targets for this theme in 2014 are:

- The AFM will identify harmful earnings models and will act against those earnings models that have the most serious impact on consumer confidence in the market and the level playing field for market participants. The AFM will devote special attention in 2014 to the risks associated with the mass distribution of products for consumers such as funeral insurance, life insurance products and consumer credit. The AFM will in particular act against harmful earnings models in which:
 - consumers are misled regarding the charges for advice and/or intermediation, and
 - charges for advice and/or intermediation are imposed that are disproportionate to the activities performed. This is related to the ban on inducements.
- The AFM will act against abuse in the rescheduling market, for instance in relation to funeral insurance policies.
- The AFM will act against ill-intentioned providers and ill-intentioned products: in 2014 we will focus on acting against ill-intentioned fundraisers (for instance in the property market), boiler rooms and illegal credit providers.
- The AFM will act against intentionally illegal activities: in 2014 we will focus on action against major recidivists and serious criminals (with more than ten offences) in order to increase the perception amongst this group that they are likely to be arrested.
- The AFM will (possibly together with DNB) intervene in financial institutions that facilitate criminal activity;
- The AFM will take action in cases relating to the reliability of policymakers and unethical conduct by licensees.
- The AFM will vet the reliability of policymakers at audit firms with a review of their records, including tax records.
- The AFM will gather information on undesirable conflicts of interests, corruption, and the approach to this, in which the focus will be (among other things) on the service provision chain of parties that manage large sums of public or private money. In addition, the AFM will act in cases in which investors have been disadvantaged by the lack of prompt publication of price-sensitive information relating to involvement in corruption.

Intended effects in 2014

The intended effects below are limited to the specific supervisory issues that will be the focus of this theme in 2014. The intended effects in 2014 are:

- The number of harmful earnings models will be reduced.
- The charges for advice and/or intermediation will be made visible to the consumer prior to the provision of the service.
- The charges for advice and/or intermediation will be reasonable and proportionate to the activities performed;
- When financial products are rescheduled or extended, the customer's interests will be given priority.
- The number of ill-intentioned providers and products will be reduced.
- Major recidivists and serious criminals will be less inclined to commit illegal activities, or to continue committing such activities.
- Financial institutions will be less inclined to cooperate with criminal behaviour;
- The integrity of licensees will improve.
- Market parties that manage large sums of public or private money will become more aware of the likelihood of arrest in case of involvement in corruption.

Measurement

The size and composition of the population of market parties that display harmful behaviour is not exactly known, since there are unlicensed operators in the market (including those operating illegally and enterprises that are

exempt from the licensing requirement) as well as licensees. This makes it difficult to measure the intended effect of this theme accurately. However we believe that a perception among market parties that harmful behaviour is more likely to be dealt with will lead to better compliance with financial legislation and regulation. We will use the following indicators to measure effectiveness in realising the targets for 2014:

- We will measure the status of the number of harmful earnings models selected by the AFM and against which the AFM takes action on the basis of:
 - 0-point and 1-point measurement of the revenue of market parties with harmful earnings models;
 - 0-point and 1-point measurements of the production of market parties with harmful earnings models;
 - 0-point and 1-point signals (including complaints to the Financial Services Ombudsman (*Klachteninstituut Financiële Dienstverlening*, or 'Kifid')).
 - measurement and profiling of newcomers with an earnings model that makes harmful behaviour a possibility;
 - information from the self-assessments and information requests distributed by the AFM;
 - public information such as service provision documents including information on the nature, scope and charges for the service.
- We will study how the market perceives the effectiveness and efficiency (speed of action) of action taken by the AFM (the perceived likelihood of being caught).

Resources

Harmful behaviour and financial crime diminish	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	9,7	9,8	14,3	47%
Expenses as % of total	11%	12%	17%	48%

*Estimated theme expenses (*EUR 1 m)*

The costs will be higher than in 2013, because some of the activities have been moved from the theme 'The quality of financial service provision has improved' to the theme 'Harmful behaviour and financial crime diminish'. Without this move, the costs of this theme would rise by around 7%.

3.10 Non-recurring services

Some of the AFM's supervisory duties are not grouped under the themes because they are less suited to a problem-driven approach. These are non-recurring services, such as the issuing of licences, the testing of the suitability and reliability of policymakers and co-policymakers, and the approval of prospectuses and tender offers. For the parties subject to our supervision, it is important that these activities are carried out with high and consistent quality, and in the most customer-friendly and efficient manner possible. This involves specific requirements for the management and organisational structure of these activities. It moreover requires a strong focus on continuing improvement of our processes. The AFM charges the costs of these activities to the applicants. The fees for non-recurring services were in principle fixed in 2013 for five years.

Resources

Non-recurring services	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	8,8	8,4	8,0	-9%
Expenses as % of total	10%	10%	10%	-8%

*Estimated theme expenses (*EUR 1 m)*

3.11 Supervision of the BES Islands

Since 1 July 2012, the AFM has had responsibility for conduct supervision on Bonaire, St. Eustace and Saba (known as the BES Islands) pursuant to the BES Islands Financial Markets Act (*Wet financiële markten BES*, or 'Wfm BES') and the Money Laundering and Terrorism Financing (BES Islands) Act (*Wet ter voorkoming van witwassen en financieren van terrorisme BES*, or 'Wwft BES').

The supervision of the BES Islands has to ensure that institutions on the islands properly implement and comply with the conduct rules, most importantly in relation to responsible lending, appropriate advice and good provision of information. For lending, the conduct rules are elaborated in a model that can be used to determine whether an institution can provide a loan that is responsible. Loans may only be granted to customers who can also repay the loan on the basis of their financial situation. Regarding appropriate advice, the focus of the supervision is on establishing that institutions obtain more detailed information on their customers. Institutions must also ensure that the information they provide is factually correct, comprehensible and not misleading.

In 2013, the new legislation for the BES Islands was not yet sufficiently embedded in all the institutions subject to supervision. Furthermore, this legislation is different to the regulations applying to the head offices on Curaçao and St. Martin, where conduct supervision has not yet been introduced. This requires continuous and visible attention from the AFM. The AFM will therefore undertake the following activities in 2014:

- Review of specific items of attention;
- Requests for case files for loans from a number of institutions;
- Supervisory visits in order to achieve a visible presence, due to the lack of a local office;
- Contribution to consumer awareness on the BES Islands.

We will strive to achieve the following long-term effects:

- Institutions will follow the results of the model for responsible lending;

- Consumers will receive all relevant and mandatory information before signing an agreement, so that they can make well-considered decisions;
- The information provided is factually correct, comprehensible and not misleading.

Resources

Supervision of BES Islands	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses	0,5	0,5	0,4	-23%
Expenses as % of total	1%	1%	<1%	-22%

*Estimated theme expenses (*EUR 1 m)*

4 Finances in 2014

This section deals with the consequences of policy for our budget. We then turn to the key figures, the expenses per type and the investment budget. We conclude with a description of how the AFM is funded.

4.1 Key figures

The total budgeted expenses amount to EUR 84.3 million, which is 1% lower than in the budget for 2013. This is the net effect of the addition of new duties, more efficient performance of the existing activities and lower pension expenses. The net expenses concern the total expenses excluding expenses paid by third parties, and amount to EUR 83.1 million. The average budgeted workforce will rise by 7 FTE in 2014 to 570 FTE.

Key figures	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013	Actual 2012
Total expenses	85,3	84,0	84,3	-1%	81,0
Net expenses	83,9	82,8	83,1	-1%	79,8
Average no. FTE including externals	563	557	570	1%	549

Table 4.1 Key figures (x EUR 1m)

In its arrangement for the financial supervisors, the Ministry of Finance has included a cost framework for the period 2013-2016. Based on this framework, the cost framework for the AFM for 2014 amounts to EUR 86.7 million. A breakdown of this figure is given in appendix 1. The AFM has decided to prepare a budget for 2014 that is well below the level stated in the cost framework. The total budgeted expenses of EUR 84.3 million are EUR 2.4 million lower than the figure in the cost framework.

4.2 Expenses per type

Expenses per type	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013	Actual 2012
Employee expenses	62,8	61,8	62,2	-1%	61,0
Premises costs	5,8	5,7	5,8	1%	5,4
Consultancy expenses	3,9	4,3	3,8	-4%	2,9
IT expenses	4,6	4,8	4,2	-9%	4,6
Miscellaneous expenses	4,9	4,6	5,5	12%	3,5
Amortisation/depreciation	3,0	2,7	2,6	-12%	3,6
Financial income and expense	0,1	0,1	0,2	23%	-0,0
Total expenses	85,3	84,0	84,3	-1%	81,0
Paid by third parties	-1,4	-1,3	-1,2	-13%	-1,2
Net expenses	83,9	82,8	83,1	-1%	79,8

Table 4.2 Expenses by type (x EUR 1m)

The most important developments in the expenses per type in comparison to the budget for 2013 are explained below:

- Employee expenses are 0.7 million lower. This is the net effect of higher salary expenses and social insurance expenses (+1.7 million), lower pension expenses (-2.1 million) and lower costs for hiring of external employees (-0.3 million). Salary and social insurance expenses are up as a result of additional capacity for new supervisory duties, and because the average expense per FTE has risen due to changes in salary;

- Advisory expenses are down 0.1 million, partly due to new set-off agreements with DNB. Hours spent giving advice, for which the supervisors have an individual statutory duty, will no longer be charged on an aggregate basis;
- IT expenses are expected to be 0.4 million lower, as a result of an efficiency programme designed to permanently reduce the costs of the usage and maintenance of hardware and software;
- General expenses will rise by 0.6 million, partly due to a higher contribution to ESMA and an item for unforeseen expenses;
- Amortisation and depreciation will be lower than in the budget for 2013, mainly because there was less investment in 2012 and 2013 in bespoke software compared to the preceding years. On the other hand, investment in the building and the inventory needed for the AFM's new workstation concept have led to an increase in depreciation. On balance, this leads to a fall of 0.4 million in amortisation and depreciation;
- Financial income and expense is up 0.1 million on balance, due to lower income from statutory interest because the amount of outstanding receivables has fallen;
- The costs paid for by third parties will decline by 0.2 million, mainly due to new set-off agreements with DNB. Hours spent giving advice, for which the supervisors have an individual statutory duty, will no longer be charged on an aggregate basis.

4.3 Investment budget

Investments	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013	Actual 2012
Renovation	0,4	0,9	0,0	-98%	0,0
Inventory	0,7	1,5	0,1	-89%	0,2
Computer equipment and standard software	0,3	0,7	1,1	212%	0,9
Bespoke software	0,8	0,7	1,2	59%	0,0
Total	2,2	3,8	2,2	75%	1,2

Table 4.3 Investment budget (x EUR 1m)

The total investment budget for 2014 (2.2 million) is the same as for 2013, however there has been a shift between the various investment items. In 2013, investment was made in a new workstation concept at the AFM. As a result of this, the forecast for investments in 2013 (in the semi-annual report) was adjusted upwards. For 2014, this means that no investments (or replacement investments) in the building are needed, and only limited investment has to be made in the inventory. The higher investments in computer equipment and standard software are related to the need to modernise the landline network, and the effort to give additional support for flexible working with additional investment in the end-user environment. Furthermore, the continuing development of the website of the AFM and the development of software to support the primary process have led to a higher investment in bespoke software.

4.4 From budget to levies

Since 2013, the AFM's total costs have been funded on the basis of the Financial Supervision (Funding) Act (*Wet bekostiging financieel toezicht, or 'Wbft'*). Under the Wbft, the costs of supervision of the BES Islands (Bonaire, St. Eustace and Saba) pursuant to the BES Islands Financial Markets Act (*Wet financiële markten BES, or 'Wfm BES'*) and the Money Laundering and Terrorism Financing (BES Islands) Act (*Wet ter voorkoming van witwassen en financieren van terrorisme BES, or 'Wwft BES'*) have to be reported separately. As a result of this, a distinction is made between funding on the basis of the Wbft and funding for supervision of the BES Islands.

The breakdown of the total costs is as follows:

Total expenses	Budget 2013	Semi-annual report 2013	Budget 2014	Change vs. B2013
Expenses Wbft	84,8	83,5	83,9	-1%
Expenses BES	0,5	0,5	0,4	-22%
Total expenses	85,3	84,0	84,3	-1%

Table 4.4 Total expenses classified according to Wbft and BES (x EUR 1m)

4.4.1 The Financial Supervision (Funding) Act (Wet bekostiging financieel toezicht, or 'Wbft')

The budgeted costs pursuant to the Wbft amount to 83.9 million. The funding of the budgeted costs is shown in the table below.

Operating difference Wbft	Budget 2013	Semi-annual report 2013	Budget 2014
Expenses	84,8	83,5	83,9
<i>Market contribution ongoing supervision</i>	55,9	55,9	55,7
<i>Market contribution non-recurring services</i>	8,8	4,4	4,5
<i>Penalties and incremental penalties</i>		1,0	
<i>Government contribution</i>	20,0	20,0	20,2
<i>Paid by third parties</i>	1,4	1,3	1,2
Income	86,1	82,6	81,6
Operating difference	1,4	-0,9	-2,4

Table 4.5 Operating difference Wbft (x EUR 1m)

The market pays the costs of the AFM that are not covered by the contribution from the government. The AFM charges these costs to the market in two ways: a fee per service and/or an annual levy for the costs of ongoing supervision.

Market contribution to ongoing supervision

The costs charged as an annual levy on market parties are calculated on the basis of the Wbft as follows:

Market contribution ongoing supervision	Budget 2013	Budget 2014
Expenses Wbft	84,8	83,9
<i>Government contribution</i>	20,0	20,2
<i>Expenses for non-recurring services</i>	8,8	8,0
	28,8	28,3
Levy for ongoing supervision	55,9	55,7

Table 4.6 Levy for ongoing supervision under the Wbft (x EUR 1m)

The market contribution for ongoing supervision will decline from 55.9 million in the budget for 2013 to 55.7 million in 2014. This market contribution excludes the operating difference to be set off for 2013. The decline in the levy for ongoing supervision is the balance of lower total costs, a higher government contribution and lower expenses for non-recurring services. The expenses for non-recurring services are shown in section 3.10.

The amount to be levied is allocated across 14 categories of institutions subject to supervision according to fixed percentages. These percentages are in principle¹ fixed for five years and are stated in Annex 2 of the Wbft. The annual adjustments to the fees concern only changes to the measurement values and/or populations, changes in the overall costs of supervision and the amount of the operating difference. The amounts to be levied (excluding amounts to be offset from previous years) per institutional category on the basis of these percentages are included in the table below and form the basis for the fees for ongoing supervision in 2014.

Levy for ongoing supervision	Percentages 2013	Percentages 2014	Levy in 2013	Levy in 2014	Change vs. B2013
Credit providers	2,3%	2,5%	1,3	1,4	8,2%
Audit firms	11,8%	10,9%	6,6	6,1	-8,1%
Advisers and intermediaries	21,8%	20,2%	12,2	11,2	-7,8%
Payment and electronic money institutions	0,1%	0,1%	0,1	0,1	-0,5%
Banks and clearing institutions	17,1%	16,5%	9,6	9,2	-4,0%
Investment firms and providers of investments	8,6%	12,4%	4,8	6,9	43,5%
Investment firms not for own account, excluding operators of an MTF	3,3%	3,0%	1,8	1,7	-9,5%
Investment firms for own account	0,5%	0,4%	0,3	0,2	-20,4%
Central counterparties	n.v.t.	0,3%	n.v.t.	0,2	n.v.t.
Securities issuers: market	5,3%	4,9%	3,0	2,7	-8,0%
Securities issuers: reporting	9,1%	8,4%	5,1	4,7	-8,1%
Financial infrastructure: market operators and operators of an MTF	2,5%	2,0%	1,4	1,1	-20,4%
Pension funds and premium pensions institutions	4,4%	4,1%	2,5	2,3	-7,3%
Insurers: life and pensions	11,4%	12,1%	6,4	6,7	5,6%
Insurers: non-life	1,8%	2,2%	1,0	1,2	21,6%
Total	100,0%	100,0%	55,9	55,7	-0,5%

Table 4.7 Levy for ongoing supervision excl. amounts to be offset from previous years (x EUR 1m)

Market contribution for non-recurring services

The fees for non-recurring services, such as licence applications and the vetting of directors, are fixed for five years and are stated in Annex 1 Wbft, thus making these costs predictable over the longer term. The fees are set on the basis of cost-effectiveness, apart from the fees for the supervision of prospectuses. The estimated income has fallen from 5.2 million in the budget for 2013 to 4.5 million in the budget for 2014.

Penalties and incremental penalties

Income from penalties and incremental penalties is not estimated, however it is passed on to the overall market through the operating difference.

Government contribution

The government contribution is established as a fixed sum in the Wbft, adjusted for price inflation annually and any additional duties imposed. The government contribution rises from 20.0 million in the budget for 2013 to 20.2 million in the budget for 2014.

¹ The percentages are subject to change as a result of changes to supervisory legislation and/or the composition of a supervisory category, if the change in composition entails a substantial change to the supervision of that category. The percentages for 2014 have been changed due to the AIFM and the product development process.

Paid by third parties

Costs paid by third parties relate mainly to the sublease of part of the office building. Costs paid by third parties will fall from 1.4 million in the budget for 2013 to 1.2 million in the budget for 2014.

Operating difference

Operating differences occur every year as a result of differences between budgeted and actual expenses and income. The budget also already includes an operating difference due to the way in which the market contribution for ongoing supervision is calculated². Operating differences are settled with the market on the basis of the stated fixed percentages. As shown in table 4.5, the budgeted operating shortfall for 2014 is 2.4 million, which is 0.1 million higher than the operating shortfall budgeted for 2013.

4.4.2 Supervision of the BES islands

The funding of the supervision of the BES Islands is arranged in the BES Islands Financial Markets Act (*Wet financiële markten BES*, or 'Wfm BES') and the Money Laundering and Terrorism Financing (BES Islands) Act (*Wet ter voorkoming van witwassen en financieren van terrorisme BES*, or 'Wwft BES'). The fees for non-recurring supervisory duties and for ongoing supervision are stated in the underlying Regulation for the BES Islands Financial Markets (*Regeling financiële markten BES*). The government reimburses costs in excess of the market contribution, since the fees were not established on a cost-effective basis.

Operating difference BES	Budget 2013	Semi-annual report 2013	Budget 2014
Expenses	0,5	0,5	0,4
<i>Market contribution ongoing supervision</i>	<i>0,0</i>	<i>0,0</i>	<i>0,0</i>
<i>Market contribution non-recurring services</i>	<i>0,0</i>	<i>0,0</i>	<i>0,0</i>
<i>Government contribution</i>	<i>0,5</i>	<i>0,5</i>	<i>0,4</i>
Income	0,5	0,5	0,4
Operating difference	0,0	0,0	0,0

Table 4.8 Operating difference BES (x EUR 1m)

The table above shows that the market contribution is very low, and rounded to the nearest million is actually nil.

² Under the Wbft, the market contribution for ongoing supervision is calculated as the total expenses less the costs of non-recurring services and the government contribution. Due to the fact that not all the fees for non-recurring services are cost-effective, a shortfall is budgeted. This budgeted shortfall will be muted since payments from third parties will not be deducted from the total expenses.

Appendix 1: Ministry of Finance Cost Structure for Supervision

Cost structure	2013	2014	
Base cost structure year t-1	80,4	85,3	
Change in salaries	1,3	-1,1	3
Change in prices	0,6	0,8	4
Permanent change in duties	3,0	1,6	
<i>AIFM</i>	0,5	1,1	
<i>EMIR</i>	0,7	0,5	
<i>Product development process</i>	1,8	0,0	
Change in costs due to European supervision	0,0	0,1	
Final cost structure year t	85,3	86,7	

Cost structure (x EUR 1m)

³ Change in salary. This concerns the most recent information regarding the expected development of salaries and employer expenses. The downward adjustment for 2014 is mainly due to the lower forecast for pension expenses.

⁴ Change in prices. One-third of the base amount in the cost structure (adjusted for temporary duties) is adjusted in line with the CBS consumer price index.

Appendix 2: Overview of expenses per theme/activity

Theme/activity	Budget 2013		Semi-annual report 2013		Budget 2014		Change vs. B2013
	expenses	% total	expenses	% total	expenses	% total	
Product providers put customer's interests first	13,6	16%	12,0	14%	10,9	13%	-20%
The quality of financial service provision has improved	12,0	14%	12,2	15%	7,0	8%	-42%
The quality of capital accumulation has improved	7,4	9%	8,7	10%	10,4	12%	40%
Financial services provided to professional and semi-professional parties is appropriate	1,6	2%	0,9	1%	1,4	2%	-10%
Pension providers provide an overview of and insight into the amount of pension and the risks to pension	3,9	5%	4,3	5%	3,5	4%	-10%
The quality of governance, reporting and audits will improve	13,9	16%	14,0	17%	14,3	17%	3%
The securities markets operate fairly and efficiently and the infrastructure remains robust	11,9	14%	11,8	14%	12,4	15%	4%
Conduct supervision contributes to the stability of the financial system	1,9	2%	1,5	2%	1,7	2%	-8%
Harmful behaviour and financial crime diminish	9,7	11%	9,8	12%	14,3	17%	47%
Non-recurring services	8,8	10%	8,4	10%	8,0	10%	-9%
Supervision of BES Islands	0,5	1%	0,5	1%	0,4	<1%	-23%
Total expenses	85,3	100%	84,0	100%	84,3	100%	-1%

Expenses per theme/activity (x EUR 1m)

Compared to 2013, some activities have been moved from the theme 'The quality of financial service provision has improved' to the theme 'Harmful behaviour and financial crime diminish'. The costs of the 'The quality of financial service provision has improved' will rise in 2014 as a result of the introduction of the AIFM directive.