

*The Dutch Authority for the  
Financial Markets*

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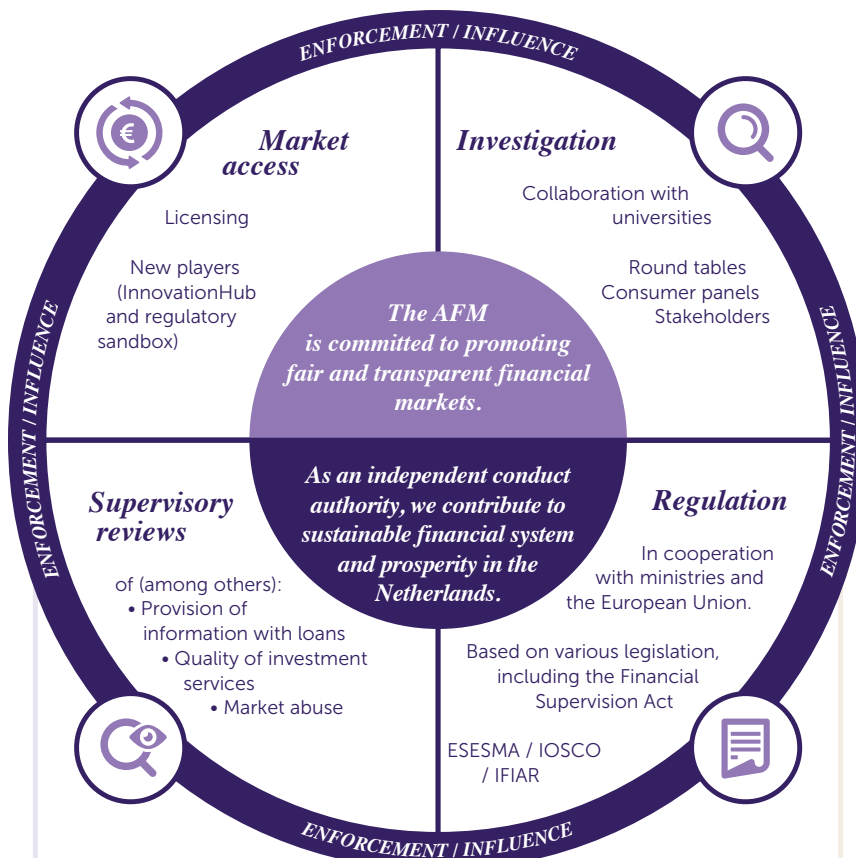
# Annual report 2017





# AFM In Brief

- + Total budget € 98.5 million
- + Since 2002
- + 642 FTE



## Supervisory measures



### Key players in the market:

- Banks
- Insurers
- Pension funds
- Investment funds
- Advisers
- Markets
- Auditors
- Consumers

9,066 organisations under supervision



### Formal

- 2017, including:
- Fines: 12 (€ 4.1 million)
  - 12 orders for incremental penalty payments
  - 315 licences issued, 12 withdrawn
  - 21 public warnings
  - 104 prospectuses assessed: 5 rejected, 4 withdrawn at the applicant's request
  - 1480 persons tested for fitness and propriety



### Informal

- Including:
- Instructive consultations/letters regarding standards 2017: 345
  - Warning letters/conversations 2017: 105
- Dashboard, publications, guidelines





# The financial sector in brief

## *Pension funds/Insurers*

Pension funds subject to supervision<sup>1</sup>



**265**

*pension funds (2017)*

297 pension funds (2016)

Volume of pension savings<sup>1</sup>



**€1,343**

*billion (2017)*

€ 1,225 billion (2016)

Number of pensioners<sup>1</sup>



**€ 3.24**

*million (2017)*

€ 3.19 million (2015)  
€ 3.24 million (2014)

Pension fund cover<sup>1</sup>



**106%**

*funding ratio 2017*

97% (2016)

Pension fund cover<sup>1</sup>



**96/** of 254

*funding ratio above 110%*

40 of 254 (2016)

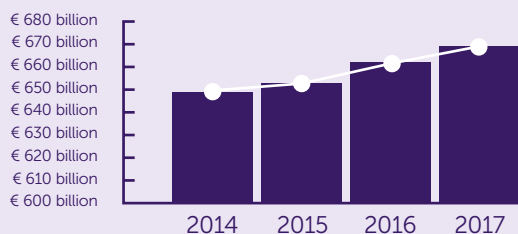
### **Sources**

<sup>1</sup> Source: DNB



## Banks / Insurers

Total amount of outstanding mortgages<sup>1</sup>



**3.5 million**

number of mortgages

Number of people in arrears on their mortgage<sup>3</sup>



Current liabilities households<sup>3</sup>

<i>HY</i> 2016	<b>23.6 billion</b>
2016	<b>21.6 billion</b>
<i>Q3</i> 2017	<b>20.5 billion</b>

Consumer credit

Number of Dutch people with payments in arrears<sup>3</sup>

<i>Start of</i> 2016	<b>778,000</b>
<i>mid</i> 2017	<b>711,000</b>

## Supervision / Collective Investment Companies



**9066**  
organisations subject to supervision (OSTS)<sup>4</sup>



**300**  
collective investment companies<sup>4</sup>



**125**  
licensed managers<sup>4</sup>



**1800**  
investment funds managed by these managers<sup>4</sup>

## Consumers

0 **3.2** 5

Consumer confidence in their own banks<sup>6</sup> (2016: 3.2)

0 **2.9** 5

Consumer confidence in the sector<sup>6</sup> (2016: 2.8)

### Sources

<sup>1</sup> Source: DNB <sup>3</sup> Source: BKR <sup>4</sup> Source: AFM <sup>5</sup> Source: Douwenkoren





## Markets / Economy

# 71.1 million

Euronext cash market exchange transactions <sup>4</sup>

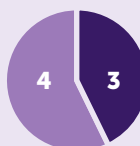
# 5.3 million

Euronext derivatives exchange transactions <sup>4</sup>

# 410 million

TRS market transactions <sup>4</sup>

Number of flotations  
in 2017 <sup>4</sup>



● Euronext  
● NL companies listed  
on markets not regulated  
in the Netherlands

Bandwidth of savings  
interest in 2017

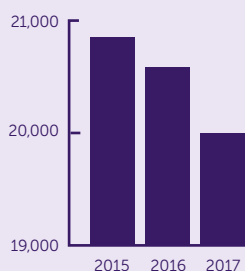


# 0.0%

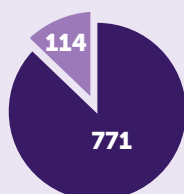
# 0.5%

## Auditors

Number of audits performed  
by auditors



PIE audits  
2017



Other PIE Big 4

Audit firms  
licensees  
2017



# 287

non-PIE

Audit firms  
licensees  
2017



# 9

PIE

## New players

Crowdfunding platform  
exemptions/licences <sup>5</sup>



# 51

Platforms

2 closed | 3 new

# 44

Granted exemption  
callable funds

# 11

Granted financial services  
provider licences

# 6

Granted Collective  
investment company  
licences

Crowdfunding <sup>5</sup>



# 99.5 million

1<sup>st</sup> HY 2017

# 86

million

1<sup>st</sup> HY 2016

# 84

million

2<sup>nd</sup> HY 2016

# 100

million

Whole of 2015

### Sources

<sup>4</sup> Source: AFM <sup>6</sup> Source: NVB





# The AFM in 2017

## at a glance

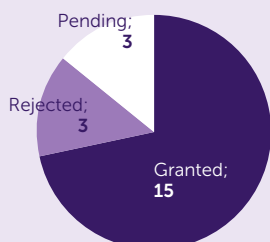
### Priority 1

Reducing undesirable risks in the financial markets through regular and thematic supervision



#### Preparation for MiFID II

MiFID II enables the AFM and ESMA to improve investor protection. Our registers and IT systems have been adjusted so that market parties have been able to submit licence applications from April 2017 and thus obtain their licence in time.

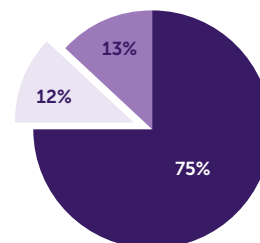


#### Tightening of provisions for crowdfunding

Investors in the crowdfunding market may not have a good overview of the risks. Our evaluation reveals that **60% of investors** ignore the advice to **invest not more than 10% of their freely investable assets**. The provisions have been tightened on the basis of the evaluation. For instance, project information must be provided for all investors on the platform 48 hours before the opening of subscriptions.

#### 1.6 million customers with investment-linked insurances have been approached by 19 insurers

In 2017, the AFM checked whether the insurers were meeting their legal obligation to activate their customers.



Around **75%** of these customers have taken action. For **13%** of these customers, only an obligation to notify applies. It is not known whether these customers have taken action. **12%** of customers have not taken any action to improve their situation, despite the efforts of the insurers. We have therefore urged these customers to seek advice on how to improve their situation, which is currently still available free of charge.

#### Guideline on early repayment

Homeowners have been given more clarity regarding how the payment for early repayment, formerly known as penalty interest, is calculated. A step-by-step plan and a check list have been formulated to assist homeowners in understanding how the payment can be calculated.



## Priority 1

Reducing undesirable risks in the financial markets through regular and thematic supervision



### Warnings on boiler rooms

Boiler rooms approach potential investors by telephone with a 'wonderful investment opportunity'. The AFM wishes to see these organisations removed from the market. We issued **15 warnings** regarding boiler rooms in 2017. We also published these warnings on our website.

### Warnings on risks of cryptos and ICOs

We also issued warnings with respect to the risks involved in Initial Coin Offerings (ICOs), cryptocurrencies and Bitcoin futures. As a result of these risks, there is a strong possibility that investors will lose their entire investment.



### Formation of a Brexit team

The AFM held nearly **100 consultations** with potential applicants in 2017. A special Brexit team has been formed to coordinate all the Brexit-related activities.



### Public offers

There were a number of notable offers last year. We organised a master class for journalists and a technical briefing for the Parliamentary Standing Committee on Economic Affairs of the House of Representatives to explain to stakeholders how the AFM deals with inside information, public offerings and the register notifications.



### Innovation in the customer's interest

Under our Innovation and Fintech programme, we held more than 60 consultations with market parties on innovative concepts. Our Fintech specialists also participated in 27 events, either as a speaker or as a panel member.

In addition, our business desk responded to 84 questions on supervision and associated regulation relating to innovative financial products and services.



### Prospect for a debt-free future

The average repayment component in the monthly instalments for potentially locked-up loans has increased from 24% to 43% for continuous credit with a balance of more than € 10,000 and an interest rate of more than 8% at finance companies reviewed.

This means that more of these loans will be repaid. These customers now have a prospect of a debt-free future.



## Priority 1

Reducing undesirable risks in the financial markets through regular and thematic supervision



Statutory Audits

- Adequate
- Inadequate

### Quality of PIE audit firms inspected

The report 'Quality of PIE audit firms' reveals that in 19 of the 32 statutory audits by Big 4 audit firms that we reviewed, neither sufficient nor appropriate audit evidence was obtained to substantiate the audit opinion. The review also showed that none of the PIE audit firms yet meet all expectations regarding a permanent improvement of audit quality. Some audit firms have made more progress with respect to conduct and culture and governance than others.



### The compensation framework for interest-rate derivatives

- **19,000** small and medium-sized business owners with an interest-rate derivative contract have to be given an appropriate solution. To ensure that these business owners can rely on receiving financial compensation, the AFM has ensured that the banks make an advance payment. By 31 October 2017, **400** million had already been offered in compensation.

## Priority 2

Strengthening and renewing supervision through focused investment in technology and methodologies



### Data-driven supervision

- Under the 'Spot On' programme, various pilot studies were carried out which resulted in improved insight for the supervision of market developments and the related risk indicators.
- By strengthening our cooperation with other supervisors, we can share data sources. This makes risky situations more visible.
- 140 digital reviews were carried out, varying from open source intelligence to e-discovery reviews.

### Application of behavioural science review

The Authority for the Financial Markets (AFM), ING and Florius conducted collective behavioural science experiments with the aim of activating consumers and thus help them to avoid financial problems.



### Conduct and culture at companies subject to supervision

- The AFM report 'Learning from Mistakes' ['Leren van Fouten'] offers advice to financial enterprises as to how to deal with mistakes and incidents at their company.
- The AFM report 'Balanced Decision-Making' ['Evenwichtige besluitvorming'] offers practical and feasible methods to reduce blind spots.





## Priority 3

Increasing the effectiveness, efficiency and adaptability of the AFM's organisation

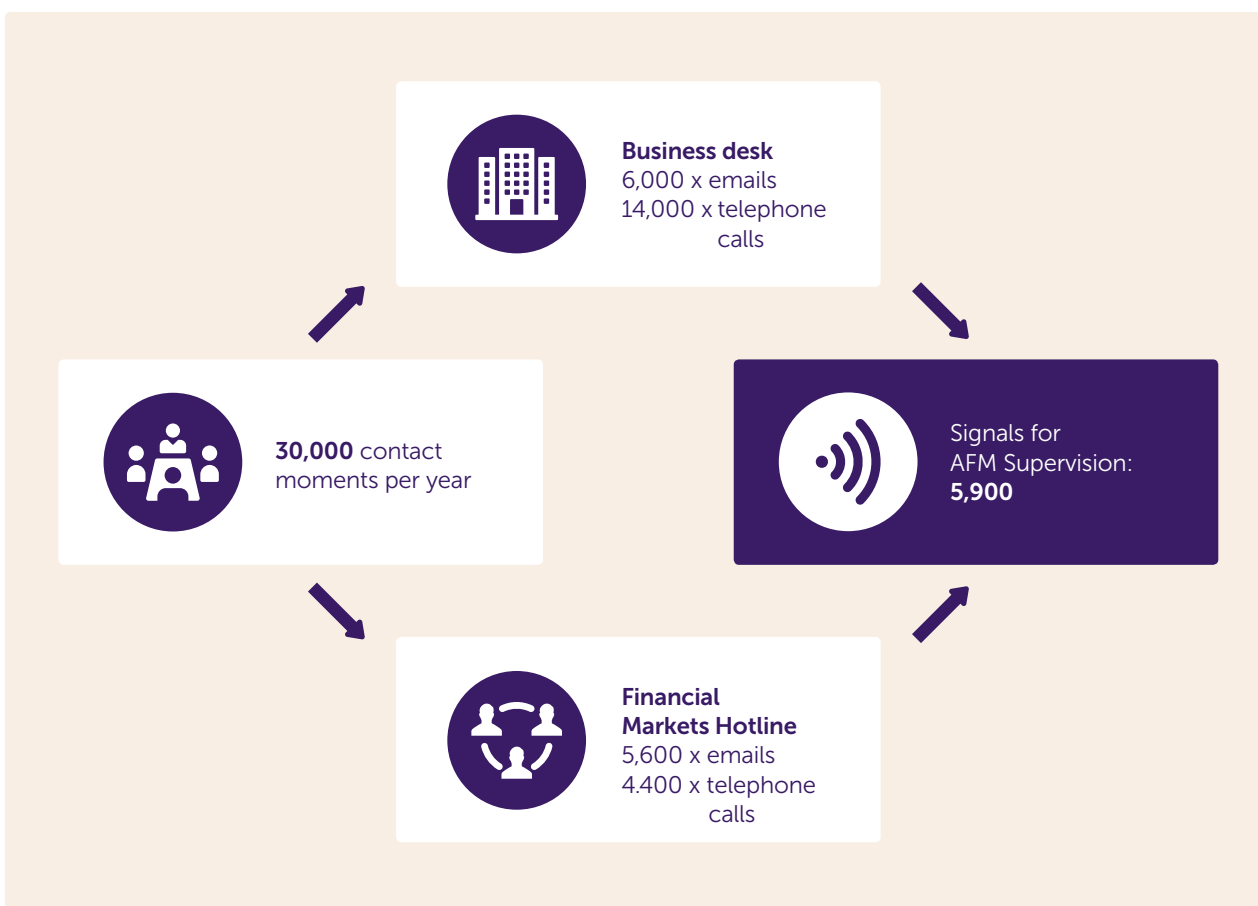
### Transparent reporting

Frequent and regular contact with stakeholders. 40 subjects were discussed on our forum with 240 reactions from respondents. These will be used to further refine our supervision.



### Strengthening management

- The leadership programme in combination with management dashboards contributes to continuous dialogue on our performance and timely adjustment where necessary.
- KPIs are a permanent item on our agenda with effect from 2018. Account will be given of this in our 2018 annual report.



### Making our operation more professional

- As part of the Information Provision master plan, the AFM-wide implementation of the Customer Relationship Management (CRM) system to replace a number of legacy systems is an important milestone.
- Risk management is integrated and embedded in our business operation.





# Foreword



The Dutch economy continued to grow last year. With growth above 3%, rising business investment, a clear increase in household consumption and further declines in unemployment, it would seem that all the signs are positive. House prices have also returned to their former levels in various regions.

## **The financial sector is changing radically.**

In addition to this economic growth, 2017 showed that technological development in the financial sector is accelerating. Products, services and data are moving rapidly across national borders and across the borders of the traditional sectors. The rise of cryptos and the continuing attention these have received from the public is perhaps the most obvious example.

Companies, whether they come from the traditional financial sector or not, no longer think in terms of borders and restrictions. New players with innovative revenue models are finding their way to consumers and businesses looking for yield in today's low interest-rate environment. Low interest rates, blurred borders in financial markets and increasing digitalisation can also lead to innovative products that are in the customer's interest. But this same combination also creates a breeding ground for misleading products that get consumers into financial difficulties.

## **Solving old problems**

We made good progress last year on resolving problems originating in the past. Together with various market parties, we have found sustainable solutions for consumers with 'locked up' loans from their consumer credit provider. Whereas previously a move to another credit provider was impossible because consumers were 'stuck' as a result of the loan conditions, these people now have the prospect of a debt-free future.

More than one and a half million customers with an investment-linked insurance now also have a better understanding of the financial situation of their policies and have been offered possibilities for improving this situation. We have urged the insurers to correctly fulfil their duty of care.

The delay at the banks in the implementation of the Uniform Compensation Framework for Interest-Rate Derivatives in 2017 was disappointing news for the SMEs concerned. The AFM has accordingly insisted that a financial payment be made to business owners who have not yet received an offer. The banks responded to this and € 400 million in advance payments was paid in 2017.





### New vigilance

This internationalisation and the current extremely rapid pace of technical developments demand a new vigilance from the AFM. Investing in cryptos and Initial Coin Offerings (ICOs) is gaining in popularity, but there is the danger of a classic bubble or indeed fraud. And if this happens, more than a half a million people will lose part of their capital in the Netherlands alone. The AFM had good reason to issue warnings in this context in 2017 and it will continue to do so.

The technological developments in the financial sector also mean that risky products such as binary options and CfDs can be offered in a tempting manner to novice investors. The use and misuse of data is the decisive factor. Risky financial products are increasingly offered to people using seductive techniques that we know from the world of games and online gambling.

### Internationalisation

In a financial market in which money, data and services flow across national borders, legislation and regulation also has to be international. International legislation and standards largely determine the supervisory framework of the AFM. And the European supervisory framework calls for more cooperation and harmonisation between the various supervisors. Much work was done last year on legislative packages that came into effect at the beginning of 2018, such as MiFID II. This represents significant progress in making European financial markets more transparent and strengthening the protection of investors. It also gives us the tools to remove cross-border high-risk products such as binary options from the market.

*“International legislation and standards largely determine the supervisory framework of the AFM”*

### Renewal of supervision

The many changes in the financial sector also place different demands on our own organisation. The use of data is increasingly the decisive factor. As a supervisor, it is not enough for us to simply understand what is going on. We also have to evaluate the risks appropriately and be able to respond. The transformation we need to make into a data-driven, ground-breaking supervisor is increasingly taking shape.

We set out our ambitions in our Multi-Year Agenda for 2016-2018. Half-way through this period, we are on track. While carrying out our current supervision, we have improved our supervisory approach and methodologies. We ran several data-driven pilot studies in 2017 and strengthened our data-management and analytical skills. This produced important insights that have led to further refinement of our data-driven supervisory approach. This is done at all times with the aim of bringing our supervision into line with rapid technological change.





### **Raising professional standards in the organisation**

The transformation of our organisation obviously presents challenges. We have made good progress in making the AFM more professional and putting our own house in order. In 2017, we saw that this was sometimes more difficult than we would have wished. The exceeding of our cost framework, largely due to the move to a new pension provider, was evidence of this. But despite the renovation works, the supervisory operation is still open for business as usual. This means that on every occasion we have to make the right choices on the basis of risk and our limited capacity.

### **Staying in touch**

Society continues to have high expectations of the financial sector. The AFM is committed to promoting fair and transparent financial markets, but always in cooperation with the sector. This means we have to stay in touch with all the parties involved without losing sight of our autonomous role as a supervisor.

The courts ruled that the AFM's current interpretation of the duty of care is not tenable and upheld the appeal by EY and PwC. Although the AFM is appealing against this ruling, we are using this opportunity to consult with all those involved: the sector, the legislature, investors and the audited entities themselves. After all, the point that the process of improving quality in the auditing sector needs to accelerate is not disputed, and here there is a common interest.

This dialogue is also becoming increasingly important internationally. The internationalisation and digitalisation of the financial sector requires a cross-border response from supervisors, in the form of increased cooperation and in some cases even by transferring duties to the European level. By actively participating in this dialogue, we continue to be a player. And we can continue to contribute to sustainable prosperity in the Netherlands both now and in the years to come.

On behalf of the Executive Board,

Merel van Vroonhoven  
Chair of the Executive Board of the AFM





# Management summary

This annual report describes how the AFM conducted its supervision in 2017 and how we addressed the risks and opportunities in the financial markets.

Last year was the second year of the realisation of our strategic priorities as set out in our Multi-Year Agenda for 2016-2018. The Multi-Year Agenda describes the market risks we see and deal with, how we further strengthen and redefine our supervision and how we can make our internal organisation more adaptable.

We made good progress towards realising the ambitions in the Multi-Year Agenda in 2017. But permanent change takes time.

The AFM identified three major trends that are producing risks for financial markets and financial consumers alike:

1. Increasing digitalisation
2. Low interest rates
3. Blurred borders of financial markets.

Moreover, these three trends interact, thus increasing both the complexity and the risks of the financial playing field.

The trends have been leading in the identification of the top 10 risks that we wish to prevent or whose adverse effects we wish to mitigate.

These top 10 risks constitute a key parameter for the deployment of our supervisory capacity. Alongside tackling the top risks, we also carry out standard supervisory tasks, such as granting licences, testing directors and approving prospectuses.

In order to address these risks effectively (and encourage opportunities), the AFM focused on three priorities:

1. Reducing undesirable risks in the financial markets through regular and thematic supervision;
2. Strengthening and renewing supervision through focused investment in technology and methodologies;
3. Increasing the effectiveness, efficiency and adaptability of the AFM's organisation

## Key results priority 1

'Reducing undesirable risks in the financial markets through regular and thematic supervision'

### Risk 1

*Limiting vulnerability due to lengthy period of low interest rates*

The AFM wishes to prevent financial enterprises from offering unsuitable products in the current low interest-rate environment or taking insufficient account of a potential increase in interest rates. The focus last year was on making consumers less vulnerable. As part of this process, we made a list of unsuitable products.

We want financial enterprises to assist vulnerable households to reduce their debt and accumulate capital. This is especially important for vulnerable homeowners with interest-only or investment-linked mortgages. The current low level of interest rates means it is attractive to repay these mortgages now or accumulate capital.



The risk of 'limiting vulnerability due to interest rates remaining low for long periods' as an underlying phenomenon was increasingly integrated in the approach to the other top 10 risks in 2017.

#### Reporting:

- + Behavioural science research has been used in cooperation with mortgage providers to study how potentially vulnerable homeowners can be encouraged to limit the financial risks of interest-only or investment-linked mortgages. ([Report 'Learning from experiments: a joint effort towards activation' \[Experimenteren: samen leren activeren\]](#))
- + Mortgage providers know how to quantify the financial cost of early repayment of a mortgage
- + Homeowners have a better understanding of how the payment - formerly known as penalty interest - is calculated. ([Guideline 'Payment for early mortgage repayment' \[Vergoeding voor de vervroegde aflossing van de hypotheek\]](#))
- + Consumers know the consequences and potential effects of changing the loan conditions for mortgages.

#### Risk 2

##### *Risk of excessive borrowing*

To prevent consumers from excessive borrowing, the AFM has focused on the following priorities: encouraging responsible service provision by market parties, combating ill-intentioned parties in the consumer credit market and developing a supervisory strategy for the consumer credit market. For this we use our insights from research into how consumers behave and make decisions. As result of our efforts, the online decision-making environment for consumer credit has been changed and providers have improved their acceptance and management policies. This will enable further control of the risk of excessive borrowing in this market.

#### Reporting:

- + Credit providers and intermediaries are improving their fulfilment of their duty of care with respect to continuous credit by freeing up existing locked-up situations and preventing this from happening in future.

- + Consumers taking out a hire purchase agreement will be better protected, because providers of these loans are becoming more responsible in their lending policies.
- + Our efforts to reduce the number of pay-day loan providers have led to a reduction in the offering of very expensive short-term loans in the Netherlands.

#### Risk 3

##### *The search for yield*

As a result of the current low level of interest rates, consumers and professional parties are looking for more yield. This can lead to irresponsible risk-taking. The AFM aims to protect investors and limit the risks as far as possible. We have identified the extent to which the market is moving towards new and risky products and services and the risks that this entails. We have studied the search for yield by retail investors and the risks and consequences of this. We have also studied which alternative suitability test would offer more effective protection for execution-only investors than the current test.

We take effective action against and issue warnings with respect to ill-intentioned providers. The quality of investment products has improved and more harmful products have been removed from the market.

#### Reporting:

- + Increased quality of investment products and thereby better investor protection, partly due to MiFID II and PRIIPs, international legislation relating to product development and product intervention. The AFM played an active role in the processes of developing this legislation.
- + The AFM also worked on investor protection at international (ESMA) level in the area of CfDs and binary options.
- + Attention was devoted to the risks of cryptocurrencies and [Initial Coin Offerings \(ICOs\)](#) on several occasions.





- + In 2017 the AFM called for clear communication about the differences between saving products and investment products and to explicitly state the risks of investment products. As a consequence the information providers of investment products give to consumers has been improved.
- + 37 inequitable revenue models of providers of investment products have been stopped.

#### Risk 4

##### *Disappointing financial position after retirement*

The AFM believes it is important that pension funds ensure that scheme members have realistic expectations with respect to their pension. Consumers must therefore have an integrated overview of their income and assets at and before their retirement date. They should be aware in good time of any possible loss of income when they retire and know what they can do to compensate for this. Last year, we focused on groups that are particularly vulnerable in this respect, such as self-employed people and couples who have separated. The AFM also calls for pension products that are cost-efficient and meet the needs of consumers or scheme members.

##### Reporting:

- + Information on the commutation of small pensions has improved.
- + Better provision of information to pension scheme members on the likelihood of indexation and the possibility of reductions, partly due to the implementation of many of our recommendations in our pensions review 'Financial Planning and Information' [Financiële Opzet en Informatie] in 2016.
- + Better insight into how pension insurers advise scheme members when choosing between a fixed or a variable pension.

#### Risk 5

##### *Legacy problems at insurers*

In 2017 the AFM looked at both how insurers are dealing with problems from the past and the future of the insurance industry. We identified vulnerable consumers

with investment-linked insurance policies, and then made an extensive, final inspection of the activation of customers with investment-linked insurances linked to pension or a mortgage. We have supervised that these people have been demonstrably helped by financial enterprises.

##### Reporting:

- + Customers with an investment-linked insurance, whether linked to a pension or mortgage or not, now have a better understanding of the financial situation of their policies because they have been approached by their insurers. Around 75% of these customers have taken action.
- + The findings of the analysis of the future of the chain of insurers, underwriting agents, advisers and intermediaries have been included in the supervisory strategy for insurers for the period 2018-2022.

#### Risk 6

##### *Inadequate audit quality*

Investors, pension scheme members and other consumers must be able to rely on the opinion issued by an auditor. The AFM is working on a multi-year programme to contribute to permanent improvement of the quality of statutory audits by audit firms. Last year, the AFM focused mainly on testing the quality of audits. There were also reviews of the progress of the implementation and embedding of improvement programmes at all PIE audit firms and the quality of statutory audits at the Big 4 audit firms.

##### Reporting:

- + It was made clear that progress on improving quality at PIE audit firms is too slow. Our report '[Quality of PIE audit firms](#)' [Kwaliteit OOB-accountantsorganisaties] showed that in 19 of the 32 statutory audits that we reviewed, neither sufficient nor appropriate audit evidence was obtained to substantiate the audit opinion.
- + This report also concluded that none of the PIE audit firms reviewed yet meet all expectations regarding a permanent improvement of audit quality. The rate of progress does, however, vary. Some audit firms have made more progress than others.



- + The AFM has established its 'Policy Rule on fitness Wta' [Beleidsregel geschiktheid Wta]. This is the framework for testing the fitness of policymakers at PIE audit firms. Persons responsible or co-responsible for determining the daily policy of a PIE audit firm must be fit and proper.

### Risk 7

#### *Vulnerability of customer data*

The AFM promotes the careful and appropriate use of customer data in the financial sector. The increasing use of data has both advantages and disadvantages. Products and services are better suited to customer behaviour, costs are lower and the identification of fraud is improving. Customer profiling can however also lead to the undesirable exclusion of customers. Undesirable advertising techniques and marketing at personal level can be used to sell inappropriate products. In its supervision, the AFM is anticipating the use of customer data at financial enterprises.

#### Reporting:

- + We have offered advice to financial enterprises regarding the use of customer data and digital marketing. Since new regulation usually takes time to materialise and the line between influence and undesirable manipulation is not always easy to define, the AFM has issued guidance to the sector.
- + Guidelines issued for automated advice. Financial enterprises must ensure that information on the customer situation is complete and reliable before making an association with financial products in their online advice.

### Risk 8

#### *Cyber crime*

The AFM strongly urges financial enterprises to ensure that their business operation is adequately robust with respect to cyber-related threats. In its supervision of the risk of cyber criminality, the AFM focused last year mainly on the extent to which the trading chain is resistant to cyber-related threats.

#### Reporting:

- + Research of securities investment systems and custodian banks to establish the risks of unauthorised access to the online transaction environment.
- + Survey of cyber risks, including listing of the most urgent and relevant cyber risks in the information and business chain, such as distributors of inside information.
- + Expansion of expertise on IT controls and cyber crime. The Operations and IT team (OPIT) is intensifying its supervision of operational and IT risks at financial enterprises and is responsible for an AFM-wide supervisory strategy for cyber crime.

### Risk 9

#### *Arrival of new players*

The combination of technical developments and the blurring of financial boundaries is leading to new and existing parties launching new products and services in the market. The AFM is accordingly developing a view regarding a controlled and ethical business operation in the digitalised environment for both existing and new players. In this context we also supervise the governance and delegation of the IT operation.

Last year, the AFM also focused on the further development of its supervisory strategy with respect to crowdfunding, with insights from research into consumer behaviour. This development requires a new vision regarding the fulfilment of the duty of care in innovative financial services.

The AFM supervises that financial enterprises apply the AFM's view regarding the fulfilment and application of the duty of care to a controlled business operation in a digitalised environment.

#### Reporting:

- + Evaluation of the regulations for crowdfunding platforms. The current regulations have been tightened in certain respects on this basis.
- + New players have been notified that outsourcing must not be at the expense of a controlled business operation.







- + Development of new vision regarding the fulfilment of the duty of care in a digitalised environment.
- + Preparation of international ban on the marketing of risky financial products such as binary options, CfDs and high cost credit products.
- + Emphasising the general duty of care of investment firms regarding the offering of Bitcoin futures to retail and other investors. The AFM also issued several warnings to consumers regarding investments in ICOs and cryptocurrencies.

## Risk 10

### *Price formation in the capital markets*

To prevent trading becoming fragmented and to ensure that price formation is as transparent as possible, the AFM focused last year on closer attention to controlled trading and took adequate measures to ensure a robust trading infrastructure. We also focused on efficient and transparent price formation, and expanded our supervision of the capital markets. This is linked with data-driven risk analysis and close attention to new market segments. This requires quantitative supervision of the trading behaviour of companies, so that we are able to respond quickly to risky behaviour.

#### Reporting:

- + Review of conduct and culture at companies with a view to reducing risks in the trading infrastructure. (Report 'Learning from mistakes' [Leren van fouten]). The recommendations should lead to improved quality of the service provided to customers and better performance by the company concerned.
- + Crowdfunding platforms are urged to make the risks of investment clearer. Our research of the information provided by crowdfunding platforms on payments in arrears, write-offs and the average return revealed that not enough effort is being made to inform investors regarding the risks.
- + Through further expansion of our own data-driven supervision, we can supervise trading on the stock exchange in real time. This enables us to identify market abuse more quickly.
- + Rigorous assessment of new parties entering the capital markets

- + In cooperation with foreign supervisors, a transaction reporting system has been developed to provide better insight into the trading behaviour of companies.

#### Ongoing supervision and measures

In our ongoing supervision we continually study notable developments in the market, receive and in some cases investigate notifications from consumers and other market parties and carry out signal analyses.

Notable themes in 2017 included MiFID II, the Interest-Rate Derivatives Compensation Framework and Brexit.

#### + **MiFID II**

The advent of MiFID II enables the AFM and ESMA to improve investor protection. In 2017, we formulated our strategy with respect MiFID II issues, compared our supervisory approach to that of other European supervisors and improved our product monitoring capacity. We prepared for new licence applications as a result of this new legislation. Our registers and IT systems were accordingly adjusted so that market parties were able to submit licence applications from April 2017 and thus obtain their licence in time.

#### + **The Interest-Rate Derivatives Compensation Framework**

Small and medium-sized business owners with an interest-rate derivative contract have to be given an appropriate solution. The AFM produced two progress reports in 2017. These showed that the banks had unfortunately delayed the implementation of the compensation. To ensure that these business owners can rely on receiving financial compensation, the AFM has ensured that the banks make an advance payment. Business owners not able to expect an offer before the end of 2017 received an advance payment of 100% of the leniency payment that forms part of the Uniform Compensation Framework.

#### + **Brexit**

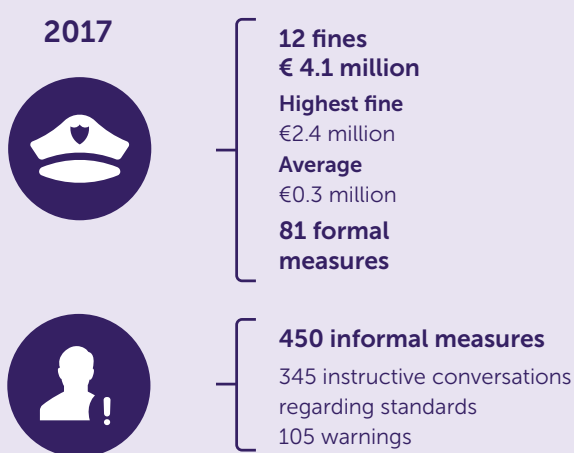
As a result of Brexit, financial enterprises from the United Kingdom will apply for a licence in one of the 27 EU Member States. The Netherlands is an attractive country for various reasons for trading platforms, asset managers, traders and data service providers,





among others. The AFM held nearly 100 consultations with potential applicants in 2017. A special Brexit project organisation has been formed to coordinate all the Brexit-related activities.

The AFM also uses informal measures to address supervisory risks. These frequently concern instructive conversations or letters regarding standards, or warning conversations or letters. We issue an instruction regarding standards in cases where we have identified a violation that is not serious enough to warrant the imposition of a fine. We issue a warning in cases where we suspect there may be a violation, for instance on the basis of signals we have received. Informal measures were also used to reduce the risk of excessive borrowing in 2017. As a result, advertising emphasising the speed and convenience of getting a loan was stopped and the advertising of pay-day loans became less tempting. Action was also taken against unbalanced presentations of returns and risks by asset managers. In addition, we called to account parties possibly providing advice on financial products illegally (without a licence), failing to submit the market monitor in time, or failing to comply correctly with the exemption scheme and the requirements relating to advertising. We also reminded parties licensed under the Audit Firms Supervision Act (the Wta) of their obligations in relation to the management of integrity risks, and instructive conversations regarding standards were conducted in relation to the ban on inducements.



The AFM reduced the risks ‘Search for yield’ and ‘Excessive borrowing’ by imposing fines on unfair revenue models and irresponsible lenders in 2017. The risk ‘Price formation in the capital markets’ was reduced by the imposition of fines on market parties failing to notify transactions and thus obstructing our supervision of market abuse. The cases that ultimately led to fines being imposed were intensive in terms of preparation, investigation and processing. The AFM uses this instrument in a targeted manner, meaning that the nature of the fine and its social effect are more important than the number of fines imposed. There were 12 fines imposed in 2017 (2016: 15).

The risks ‘Search for yield’ and ‘Excessive borrowing’ were also dealt with by the use of orders for incremental penalty payments. An order for incremental penalty payments is often used to obtain information from companies that fail to respond to our normal requests for information. As compliance with our requests for information improves, we will have to use this measure less frequently. The number of orders for incremental penalty payments imposed was 12 (2016: 17).

The number of informal measures may fluctuate widely from one year to another, partly due to the complexity of the investigations carried out. The total number of informal measures was 650 (2016: 450).

The AFM’s policy in relation to fines was an issue in various court cases in 2017.

In October 2017, the Trade and Industry Appeals Tribunal (CBb) reversed court rulings from 2016 on higher appeal. These rulings stated that the process of imposition of administrative fines did not comply with the applicable requirements of segregation of duties. The CBb thus confirmed that the fine procedure at the AFM was in line with the law.

On 20 December, the administrative court ruled on the appeal made by EY and PwC against the fines imposed by the AFM in 2016 for failing to exercise their duty of





care. The court ruled that the AFM's interpretation of the duty of care is not tenable and upheld the appeal by EY and PwC. The effect of this ruling is that audit firms can no longer be directly called to account for deficiencies in audits of financial statements by individual auditors. The AFM accordingly announced in January 2018 that it would take the case to higher appeal. This ruling has no effect on the financial statements for 2017.

## Key results priority 2

*'Strengthening and renewing supervision through focused investment in technology and methodologies'*

The analysis and application of data enable us to continually increase the effectiveness of our supervision. This is reinforced by new insights into the behaviour of consumers and investors and culture. Our focus with respect to technological and methodological innovation is on three priorities:

1. Consumer and investor behaviour;
2. Conduct and culture at companies subject to supervision;
3. Data-driven supervision.

By utilising behavioural science, we are improving our understanding of why consumers make certain choices and how they are influenced. Knowledge and understanding of decision-making behaviour, in combination with thorough field research, helps us to develop forms of intervention. This makes our supervision more effective. We work closely with universities, financial enterprises and other stakeholders.

The AFM placed the theme of conduct and culture on the agenda in 2017 so that the financial sector would start to address this issue. We strongly support an organisational culture at financial markets parties and sectors in which fair and transparent provision of services is encouraged. Instruments and methodologies are being developed in order to gain better and timelier insight into undesirable behaviour at financial enterprises.

To be able to keep up with technological changes, we are investing in new systems that enable us to analyse

large quantities of market data. This means we can identify trends and risks in the market at an early stage. In the past year, various pilot studies were carried out which resulted in improved insight into market developments and the related risk indicators.

We are also increasing our collaboration with other supervisors. We are increasing our efficiency and effectiveness by making data sources available and sharing knowledge with respect to analytical techniques.

The AFM carried out 140 digital reviews in 2017, varying from open source intelligence to e-discovery reviews. These reviews studied data sources such as e-mail and (mobile) business data. This involves enforcement and integrity investigations in financial markets and of unlicensed parties.

## Innovation and Fintech programme

Under our Innovation and Fintech programme, we held more than 60 consultations with market parties on innovative concepts. Our fintech specialists also participated in 27 events, either as a speaker or as a panel member.

In addition, our Innovation Hub responded to 84 questions on supervision and associated regulation relating to innovative financial products and services.

## Key results priority 3

*'Increasing the effectiveness, efficiency and adaptability of the AFM's organisation'*

To be able to react in an alert manner to external challenges, our internal organisation needs to change. We worked on strengthening our governance, and making our business conduct more professional and accountable in 2017.

The refinement and design of the AFM's governance model includes a focus on the further development of leadership among our people. This is also part of our leadership programme. Management dashboards





have also been implemented. In combination with internal KPIs, these contribute to the ongoing dialogue regarding our performance and timely adjustment where needed.

The AFM exceeded the tolerance level for unjustified procurement and obligations of 1 per cent of actual expenditure in 2017. The total amount of unjustified expenditure and commitments amounted to € 4.9 million in 2017. This equates to 4.8% of the actual expenditure of € 102.2 million. This is due to agreements concluded in the past. In addition, changed insights in relation to the interpretation of procurement law for several large contracts led to a higher amount of unjustified expenditure than in 2016.

In 2017, the AFM put unjustified contracts out to tender again where possible, a policy for temporary hires and procurement was established and a decision was made to set up a future-proof central procurement organisation. This organisational change came into effect on 1 January 2018. Significant progress has thus been made on reducing unjustified expenditure. At the same time, permanent improvements to the organisation take time.

The IT organisation has been made more professional. The Master Plan for Information Provision is based on three pillars: improving the infrastructure, simplifying the application landscape and improving IT processes.

Attracting and retaining talented employees is of great importance for the AFM, as is the continuous development of our employees. We invest in the knowledge and competences of our employees and attract new experts with diverse backgrounds (data analysts, behavioural economists and psychologists). This has led to the recruitment of 122 new colleagues, partly thanks to a new recruitment website. This compensated for part of the employee turnover of 11.4%. Temporary hires are used to fill vacancies in important positions. The number of employees increased in 2017 from 574 FTE in 2016 to 596 FTE.

As a supervisory authority, we are always under scrutiny. At the same time, we have a serious responsibility to deliver good work. If we want the public to see us as an

authority, we have to accept this responsibility. For this, it is important that we show how we deal with mistakes. We believe it is important to be transparent when things go wrong, so that we have the opportunity to limit the damage and avoid making the same mistakes in the future by learning from these experiences. We do this by assessing mistakes and studying how to learn from them, so that we apply the same principles to ourselves as we apply to the sector.

We demonstrated how we deal with mistakes in our approach to the short-sell incident. After an evaluation of the process, the AFM immediately adjusted a number of its checks and balances procedures. The process of short-sell notifications was fully automated in June 2017.

We continued with our professional approach to contacts with stakeholders in 2017, among other things with round table meetings and discussions with ConsumerPanel and the Advisory Panel.

The AFM undertakes various activities in the ongoing dialogue with its environment, for example by explaining our supervision at national and international events, round table sessions and conventions or meetings for various interest groups. All these occasions provide moments for self-reflection as well as opportunities for dialogue and exchange of knowledge.

2017 was also a year in which the composition of our Executive Board and our Supervisory Board (SB) changed. Bart Koolstra stepped down as a member of the SB in April. In November, Diana van Everdingen stepped down as a member of the SB on completion of her second term. In October, the AFM appointed Ellen van Schoten as an Executive Board member not mandated under the articles of association. She holds the position of Chief Operating Officer (COO). Femke de Vries stepped down as a member of the Executive Board on 1 January 2018.

The Supervisory Board is working on filling the vacancies on the Executive Board and the SB.





## Financial

The AFM exceeded the budget for its regular business operation by € 0.8 million in 2017. This is 0.8% of the total budget of € 98.4 million. The cause included a non-recurring and unforeseen higher expense as a result of the transfer to a new pension provider (€ 1.7 million), which was only partially offset by cost savings.

This is the first time in five years that the AFM has reported a negative operating balance. This means that our total expenditure was higher than our total income. In previous years, there has always been a positive operating balance. Operating differences are settled with market parties and/or the government. A positive operating difference is therefore deducted from

the levies and/or paid to the State. The amount to be deducted in 2017 was € 5.3 million.

Despite our negative operating balance in 2017, the amount to be settled in 2018 is still positive at € 0.4 million, and will thus be deducted from the levies. In addition, there was a non-recurring excess expenditure for the interest-rate derivatives project of € 3.0 million. These costs were associated with the implementation of the Uniform Compensation Framework and the delay that occurred at the banks. This concerns a provision for expenses that will be made in both 2017 and 2018. This non-recurring amount will be settled with the six banks involved in the compensation framework and thus will not be charged to the other enterprises subject to supervision.

### Statement of income and expenditure

*For the years ending on 31 December*

(Figures in EUR x 1,000)	<b>2017</b>	<b>Budget 2017</b>	<b>2016</b>
Total income	98,902	98,448	92,337
Total expense	102,238	98,448	90,086
Operating balance	-3,337	-	2,251

