



Fédération Bancaire Européenne
European Banking Federation
Le Secrétaire Général

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Mr. José María Roldán
Chairman
Committee of European Banking Supervisors
Floor 18, Tower 42
25 Old Broad Street
London EC2N 1HQ

Brussels, 08 November 2005

Subject: Consultation Paper (CP09) on Guidelines for Supervisory Cooperation

Dear Mr. Roldán,

The European Banking Federation (FBE)¹ welcomes the opportunity to comment on the Committee of European Banking Supervisors' (CEBS) consultation paper on guidelines for supervisory cooperation. The question of the organisation of the relationship between home and host supervisors is of utmost importance for our members.

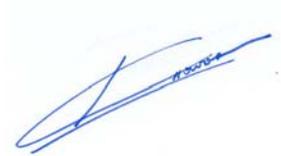
The FBE has often underlined that it considers the promotion of supervisory convergence to be CEBS' overarching goal. We believe that the present paper delivers a broadly constructive proposal when assessed against this background and against the legal and regulatory framework as it currently stands. However, we would like to point out that there are additional tools available to CEBS which are not sufficiently dealt with in the paper. We would urge CEBS to make use of all possible means to alleviate the administrative burden that is placed on banks.

Please find our response enclosed. For any questions, please don't hesitate to contact

¹ Set up in 1960, the European Banking Federation (FBE) is the voice of the European banking sector. It represents the interests of over 4,500 European banks, large and small, with total assets of more than €20,000 billion and over 2.3 million employees.

either myself or my colleagues Cairtriona O'Kelly (C.OKelly@fbe.be) and Uta Wassmuth (u.wassmuth@fbe.be).

Yours sincerely,



Guido RAVOET
Secretary General

Enclosures: 1



Fédération Bancaire Européenne
European Banking Federation

FBE RESPONSE:

**Guidelines for co-operation
between consolidating supervisors and host supervisors**

CEBS CP09

1. The European Banking Federation (FBE) welcomes the opportunity to comment on CEBS' Consultation Paper 09 on guidelines for co-operation between consolidating supervisors and host supervisors. The question of division of supervisory responsibilities is an issue of major concern for our members especially in view of the direct implications that it has in terms of workload and related costs.
2. We acknowledge that, as a first step, CEBS has addressed a limited number of issues in this paper. We look forward to working with CEBS in the coming five years in the run up to the review of the level of application of the CRD, to develop an environment in which a converged and streamlined supervisory framework will facilitate closer coordination. In this context we agree that the issues identified by CEBS (deposit insurance schemes, the lender of last resort function and crisis management provisions) will be, to a greater or lesser degree, central to the medium-term work programme. In particular the FBE looks forward to the Consultation Paper on crisis management. We believe that work on crisis management should take precedence over the other issues.
3. We understand that the consultation paper builds on the legal and regulatory framework of the EU and its Member States and that especially the revised capital adequacy framework (CRD) determines the basic conditions for the regulation of the relationship between consolidating and host supervisors. Against this background we consider CEBS' paper to constitute an appropriate proposal for the organisation of the home/host relationship at this stage and an important first cornerstone in setting out how home and host supervisors should cooperate under Article 129 of the CRD.
4. The FBE welcomes CEBS' recognition of the ongoing developments in European banking supervision. It is the FBE's firm belief that supervision in the EU must move towards an increasingly central role for the consolidating supervisor to deliver an efficient supervisory framework for both supervisors and financial institutions. The review clause that has been incorporated in the CRD on the level of application determines a realistic timeframe for further steps in this direction.
5. In addition to developments in cooperation, the FBE is fully supportive of CEBS' objectives of supervisory convergence and the development of a common European supervisory culture. Both of these goals are crucial to reducing the burden on banks resulting from the current fragmented supervisory framework. The FBE is fully committed to working with CEBS to deliver a coherent and consistent framework.
6. A distinction must be made between local banks and banks active on a cross-border basis. The present guidelines only concern a small number of institutions. However, these institutions account for a disproportionate share of total assets, and they play a particularly important role in integrating Europe's financial markets. Shortcomings in the European supervisory regime will place them at a competitive disadvantage at international level and will weaken the European financial services industry as a whole.

7. We understand that joint model validation is only one of the elements in the consultation paper but stress that for the industry, a clear understanding of operational network mechanisms is crucial. We would therefore request CEBS to outline clearer guidelines on the division of tasks and on arrangements for the case of disagreements given that CP10 did not adequately address these issues.
8. There has been evidence in the past that there is no automatic development towards convergence. We would urge CEBS to make use of all tools available to it within the given legal framework to achieve targeted harmonisation in a short timeframe. We would also urge CEBS to consider how the legal framework could evolve in the coming period to allow for a supervisory framework which is consistent both with supervisory responsibilities and the current risk management practices of banks. It is apparent to the FBE that continuing to operate within the current legal framework will prevent the European banking industry from growing and innovating. Neither industry nor the supervisors can afford not to explore alternative arrangements.
9. In this context, the delegation of tasks and responsibilities is central to the home/host framework. We appreciate the emphasis on this in CP09. Article 52 (9) of Directive 2000/12/EC (Article 131 in the revised Directive) already provides for the delegation of supervisory responsibilities. We are however concerned that this provision has never been utilised to date. We therefore urge CEBS to explore the use of this provision to the fullest possible extent under the new framework.
10. We support CEBS' objective of promoting efficient, coherent, cost- and resource-effective cross-border supervision. At the same time we wish to stress that effectiveness should also be measured against institutions' needs and working processes. We broadly believe that the paper achieves an appropriate fit with the current arrangements within financial institutions. Obviously this fit needs to be monitored on a case-by-case basis and over time.
11. Ongoing dialogue is crucial to the home/host framework so that there is transparency and so that its effectiveness can be monitored on an ongoing basis. The FBE feels that there could be more emphasis on dialogue with the group in CP09. There must be communication between the college of supervisors and the banking group on the agreed mechanisms for validation, distribution of responsibilities and information exchange.
12. This ongoing dialogue is furthermore important in the context of dealing with inconsistent application of national discretions by the supervisors of a banking group and the resulting regulatory burden. Each case of national discretion multiplies the implementation and maintenance cost of the reporting tools. Banks will suffer further cost and administrative burdens from potential requirements to implement models based on local data which will not be consistent with the group models. It is therefore imperative that the relevant supervisors, in dialogue with the bank, cooperate and reach agreement on a unique set of regulatory requirements to be used for consolidated reporting purposes.
13. The FBE fully welcomes CEBS' emphasis on the need to ensure that the information exchange process be proportionate and risk-focussed. It is also vitally important that the bureaucracy attached to information exchange be limited to a minimum. In that context we welcome CEBS' objective of encouraging supervisors to be as spontaneous as possible and we also welcome in particular the objective of agreeing a communication strategy as early as possible in the process. However, we would request CEBS to highlight that the proposed spontaneity should not lead to unnecessarily frequent requests. We would also underline that spontaneous

arrangements do not compensate for, nor stand in contradiction to, the need of a central point of contact for banks. For the sake of clarity and efficiency, information flows must as far as possible be channelled through the consolidating supervisor, and results must be recognised at group level. Furthermore, an appropriate vehicle for the exchange of information between supervisors should be developed. In this respect the FBE has proposed a qualification certificate in its response to CP10. This is just one example of how information exchange between supervisors could be streamlined and simplified.

14. The overriding objective of the information exchange arrangements should be to eliminate duplicative information requests to the group and to foster trust and cooperation between the supervisors. The FBE, therefore, agrees with CEBS that the home supervisor is best placed to provide information relating to the entire group. While senior management of local subsidiaries of a banking group should be well-informed about the group's roll-out plan as it relates to their jurisdiction and business lines, the group should communicate the plan as a whole to its home supervisor. The documentation of a bank's processes, mechanisms and plans on Basel/CRD implementation is too vast to communicate across a group. It is normally stored in a central data warehouse within the group head office. We would therefore strongly urge CEBS to clarify that the host supervisor should direct its information requests to the home supervisor and should limit its contact with local management as far as possible to points of clarification of that material relating to the specific jurisdiction.
15. Furthermore, the arrangements for information exchange agreed by the supervisors should be communicated to the group so that it is clear how the host supervisors will communicate with both the home supervisor and the group within the agreed operational networks.
16. The determination of significance is key to the framework set out in CP09. The FBE feels that CEBS has made significant progress in identifying the criteria that will be used in the determination. We have repeatedly called on the Commission and supervisors to lay down markers to clarify the concepts of materiality/significance/systemic relevance. We agree that this cannot be done in absolute terms. However, there remains significant uncertainty between banks and supervisors on how individual subsidiaries will be treated. We welcome CEBS' proposal in paragraph 8 to give the consolidating supervisor the key role in determining materiality in cooperation with the host supervisors but remain concerned about the lack of clarity in this area. We also underline that supervisory transparency will play an important role in this respect.
17. We would hope that the process of determining significance will lead to a balanced judgement based on the relative materiality of the subsidiary in the group versus its materiality in the host country. Work on determining the treatment of subsidiaries is urgent and needs to take place at the earliest date possible. The FBE would urge CEBS to press this point amongst its members.
18. While it is clear that there is optimism within CEBS that the determination of significance will be a reasonably smooth process, we feel that there is a clear need for the bank to be kept informed on the progress of the discussions by its home supervisor and, if necessary, to challenge the decision taken. In the same way that supervisors cannot place quantitative limits within the determination of significance, banking groups use qualitative, strategic reasoning to determine the treatment of a subsidiary within the group. If a bank feels that this reasoning has not been sufficiently taken into account in the supervisory discussions, there must be scope to challenge the supervisors reasoning before the final decision is taken.

19. We wish to underline the important role that the concept of supervisory disclosure plays in the context of developing the home/host relationship. The FBE firmly believes that the information provided through the disclosure framework will allow for peer review over time to act as a catalyst for cooperation and convergence. It is crucial that the full scope of the disclosure regime has buy-in from all of CEBS' members. In the context of determination of significance, it would be useful for CEBS to report aggregate statistical data across the EU of significant subsidiaries and branches on an annual basis.

Detailed comments

Introductory statements

20. CEBS sets out the objectives of the legal and regulatory framework in paragraph 6. The FBE fully supports the objectives of prudential supervision which are listed. However we note that the list is limited to prudential objectives. It ignores the situation of the large, internationally active banks and therefore does not reflect the role of European supervisors in facilitating the Single Market by removing supervisory obstacles to cross-border consolidation of the sector. Neither does it reflect the need for supervisors to facilitate the development of increasingly complex and centralised risk management systems within banks. We would encourage CEBS to have more vision in defining the purpose of the legal and regulatory framework for supervision in Europe. In this context the objective in paragraph 15 of providing sufficient flexibility to adapt to a changing environment is welcome.
21. The FBE understands paragraph 7 to propose mutual recognition of the 'fit and proper' assessment. If this is the case, we fully support this statement. Mutual recognition of this assessment would contribute significantly to reducing the burden on banks seeking to enter new jurisdictions. This would be fully in line with the Commission's review of Article 16 of the Consolidated Banking Directive.

1. Are there any changes not mentioned here that you deem significantly impacting on the European financial sector and, in particular, on the supervision of cross-border banking groups?

22. The supervisory environment in Europe is shaped by a number of factors from both inside and outside Europe that mutually determine and reinforce each other. This includes globalisation, EU enlargement and the deepening of European market integration through an increasing number of cross-border mergers and changes in the funding of subsidiaries and branches. Importantly, these developments imply an increased complexity of regulation and a crucial need to find solutions on a global as well as on a European level. Supervisory arrangements can have competitive implications, and the duplication of work that results from different supervisory requirements imposes major administrative costs on banks. It must be ensured that the supervisory regime in Europe does not put Europe's financial services industry at a competitive disadvantage vis-à-vis its competitors in other jurisdictions.
23. In this context, the objective of consolidated supervision that has been laid down in the CRD and the framework for implementation as defined in the banking supervision section of the European Commission's Green Paper on Financial Services Policy (2005-2010) must be given special consideration. Against this background we welcome the emphasis on the role of the home supervisor as set out in CP09. We also encourage CEBS to continue to bring its work to the table in the AIG so that best practices developed at a European level can influence how home and host supervisors will interact on a global basis. In particular, the possibility of mutual recognition of home country supervisions between EU supervisors on the one hand, and supervisors with

equivalent supervisory approaches and standards – in particular Switzerland, the US, Canada, Japan and Australia – on the other hand should be explored.

II. What are your views on the need for a co-operative framework among supervisions that is at the same time comprehensive and flexible?

24. The FBE agrees that a co-operative framework among supervisors must be both comprehensive and flexible. However, flexibility should not stand in contradiction to convergence. Provision must be made against the risk of increasing fragmentation of the supervisory environment especially in view of the complexity of the CRD and its high number of national discretions. CEBS should have a clear strategy on how to avoid further disparities and to promote common approaches. This also includes the regular monitoring of progress and problems encountered.

25. We are disappointed that the proposed home/host framework does not provide guidance on the treatment of the high number of national discretions in the CRD. The framework must facilitate agreement on consistency of approach amongst the supervisors of a banking group at least for the purposes of consolidated reporting. It is not clear at this point how banking groups will cope with group level consolidation where there are differing requirements in the jurisdictions in which they are active. For large cross-border groups which have centralised systems for the reporting of the solvency ratio, the existence of separate calculation requirements by home and host supervisors is both costly and administratively burdensome. Moreover, some national discretions concern not only the calculation method, but the underlying risk model itself. We therefore recommend that as regards consolidated reporting, the options chosen by the home supervisor be applicable for the entire group. In the case of local reporting, we accept that the problem will have to be dealt with on a case by case basis to take account of local conditions. We would, however, again insist that there be transparency around the decision making process.

III. What are your views on the description of the respective roles of consolidating and local supervisors within the proposed framework?

26. While the FBE believes that CP09 delivers a significant step forward in describing the process relating to the distribution of tasks, we view the lack of process for the case of disagreement between different supervisors to be a shortcoming. In our view, there should be a clear role for the home supervisor in managing the process where there is disagreement. Furthermore, the current multiplicity of approaches across the EU could constitute an obstacle for the clear allocation of responsibilities. To deliver real efficiency there is a need for general convergence of supervisory approaches.

IV. What are your views on the concept that supervisory co-operation should go beyond the mere exchange of information in order to enhance effectiveness?

27. The mere exchange of information between supervisors would clearly be insufficient. Convergence is not a natural trend. On the contrary, the complexity of the CRD and its high number of national discretions will result in additional fragmentation of the European supervisory environment. In order to prevent this, there is a need for a range of different instruments that includes as a key feature the delegation of tasks and responsibilities with a clear role for the home supervisor.

28. We believe that the most effective and efficient way of organising co-operation between home and host supervisors is through colleges of supervisors under the leadership of the home supervisor. These meetings should be physical and should take place on a regular basis. Whilst we agree that the host supervisor will be best placed to perform certain specific tasks and to provide input relating to local conditions,

the responsibility for the final evaluation of a banking group – including its subsidiaries – should be clearly allocated to the home supervisor.

V. *What are your views on the suggestion that supervisors should, with a view on efficiency, consider the possibility to perform tasks on behalf of one another in strict respect of each other's powers and responsibilities?*

29. The sharing of tasks and the voluntary delegation of responsibilities is a key feature of the efficient organisation of the relationship between home and host supervisors. If supervisors do not begin to operate outside their national legal frameworks to some extent, the FBE believes that there will eventually be a need for a full overhaul of the supervisory framework in Europe with the possibility of more radical changes. We think it is in both the supervisors and industry's interests to think imaginatively about how to push out the boundaries of the current system as far as possible. In this context we urge CEBS to make extensive use of this instrument in accordance with Articles 123 and 131 of the revised CRD.

VI. *Do you see major risks for duplication of tasks under the proposed framework? If yes, which are these?*

30. It is difficult to say at this point how the framework will work in practice. However, we do have concerns that if host supervisors do not rely heavily on the home supervisor, particularly in the exchange of information, there could be duplication which will be burdensome for both industry and the supervisors themselves. For example, under the current framework host supervisors could decide not to rely on the home supervisor's rating model validation for certain elements and will thus need to carry out a separate validation for these specific elements of the rating models used in their country. To the extent that models are centrally developed and validated, this would imply major additional and unnecessary workload for institutions. It is essential that this process be formalised so that host supervisors do not challenge the underlying architecture of the models and that the home agrees on which aspects to delegate to the host in relation to local specificities. Again this should be done in dialogue with the bank.

VII. *Do you wish to make any comments or suggestions with regard to the considerations set out in this chapter?*

31. We agree that both the consolidating supervisor and the local host supervisors have a legitimate interest and role in the supervision of EU banking groups. We believe that the appropriate tool to combine the different stakes involved in the supervision of EU banking groups is a consultative process between the supervisors concerned, notably in the format of colleges of supervisors led by the home supervisor. To take account of the different interests involved and to achieve an efficient and effective supervisory environment, supervisors should agree on a voluntary basis to a two-way delegation of powers pursuant to Article 131 of the CRD.

VIII. *What are your views on significance of each entity within a group and/or within its domestic market as key elements, with a view on proportionality, for structuring the process?*

32. The FBE agrees that both materiality within the banking group and systemic significance are relevant factors in determining the treatment of a subsidiary, or the role of the host supervisor in the case of a branch. However, the determination of significant subsidiaries should in the first place rely on the institution's own qualitative assessment.

33. Regarding permanent partial use of the standardised approach for insignificant portfolios, the responsibility for determining exemptions should lie with the institution. The consolidating supervisor should review the institution's assessment in co-ordination with the host supervisors concerned. However, we would request CEBS to recognise that in case of dissent it is up to the home supervisor to take the final decision.
34. In order for the process of assessment of significance to work in practice, there must be peer review on the number of significant subsidiaries within a jurisdiction and the total assets of those subsidiaries. While political considerations cannot be ignored, the determination of significance must be in the best interests of the group and of all the supervisors involved with the group. Individual supervisory authorities should not argue the case of systemic significance purely to enhance their political standing within their jurisdiction.
35. In addition, the resources of the supervisory authorities should be taken into account. A large number of subsidiaries in one Member State should not be classified as significant if the supervisory authority cannot demonstrate the capacity to cope with the relevant duties.
36. The significance of the local market should also be a determining factor. Where the risk of global contagion from a systemic crisis in a specific local market is greater this would justify the host supervisor having more control where the resources are available. Equally where income from the financial services industry in a Member State accounts is disproportionately high compared to income from other sectors this should be taken into account.

IX. What are your views on the proposed approach to assess significance? Do you want to make any suggestion as to improve this approach?

37. The FBE agrees that the significance of each entity both within a group and within its domestic market play a key role in structuring the process of supervisory co-ordination. However, to make this principle work there is a need for a common understanding by home and host supervisors on what constitutes significance and how to solve disagreements on this assessment. The FBE has already commented above on this. We would again reiterate that:
- a. the rational of the banking group must be taken into account;
 - b. there must be full transparency in the process;
 - c. the banking group must have the right to challenge the supervisors;
 - d. disclosure of key aggregate data by CEBS would help to make this an informed evolutionary process.
38. Furthermore, the FBE considers it crucial that decisions on significance of a branch or subsidiary not be carved in stone but must be subject to periodical review. Both the quantitative and qualitative elements will be subject to change over time. The institution should, therefore, not just be able to challenge the original determination before a final decision is made, but should also be able to challenge the decision at a later stage where circumstances change.

X. What are your views on the general description of the process as set out in the tables above? Does it depict a logical, workable and comprehensive approach?

39. We believe that the description laid out in the tables provides a useful basis for the co-operation process and we support in particular the clear distinction between the roles of the consolidating supervisor and of host subsidiary supervisors respectively. CEBS'

assertion that the relationship between the consolidating supervisor and host branch supervisors should aim at ensuring a free exchange of information is appropriate. It should also, of course, aim at fostering a European supervisory culture. However, firms must be duly informed about the exchange of information pertaining to them between the different supervisors involved. On adverse developments they should be given the chance to comment in a bilateral meeting with the relevant supervisor *before* the information is passed on. This is especially true on matters of judgement rather than proven facts.

XI. Do you see additional potential for streamlining the process of co-operation, under the present legal provisions? What suggestions do you wish to make in this respect?

40. As a priority supervisory co-ordination should be conducted on a multilateral basis rather than bilaterally. This will help to avoid contradictions between different approaches and enhance a common supervisory approach in the supervision of banking groups.

41. In addition, as stated earlier in the paper, the FBE would encourage CEBS to explore the possibilities for delegation of responsibilities as far as possible. We would also encourage CEBS to monitor the delegation of responsibilities over time with a view to identifying further potential.

42. We would also reiterate the need to promote mechanisms similar to those set out in CP09 in a global context. If AIG members were to accept part or all of these proposals as a working method, it would achieve a considerable alleviation of the cost burden for international banks.

XII. What are your views on the general description of the process as set out in the tables above? Does it depict a logical, workable and comprehensive approach?

43. We believe that the proposed process is broadly logical and workable, and we welcome in particular CEBS' clear differentiation between home and host supervisors as well as the description of their respective roles. However, in the practical framework provision must be made for the case of differences of opinion between the different supervisors involved.

XIII. Do you see additional potential for streamlining the process of co-operation, under the present legal provisions? What suggestions do you wish to make in this respect?

44. See response to answer XI.

XIV. Do you see any serious obstacles to the smooth process of model approval stemming from the proposed tasks executed by the consolidating supervisor and the host supervisors? If yes, what are they and how to remove them?

45. Whilst we agree that potential areas of disagreement should be identified as early as possible and that supervisors should try to find a common approach we would urge CEBS to acknowledge that the home supervisor should take the final decision on model approval.

46. With a view to paragraph 67 we would encourage CEBS to adopt a generally more open and forward-going approach. CEBS should not just react on an ad-hoc basis to the legal requirements, but also provide guidance for the future adaptation of banking supervision to industry developments.