



Fédération Bancaire Européenne
European Banking Federation
Le Secrétaire Général

N°0027
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Mr. Charlie McCreevy
European Commissioner for Internal Market and Services
European Commission
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Subject: Consolidated supervision in the Capital Requirements Directive

Dear Commissioner McCreevy,

The FBE would like to bring to your attention a number of issues within the Capital Requirements Directive (CRD), which, we feel, will impede the objective of a Single Market for Financial Services in Europe.

We believe consolidated supervision to be the only mechanism which can deliver an efficient supervisory environment for banks active on a cross-border basis in the EU. The current CRD proposed by the Commission lays some of the groundwork necessary for such a framework but fails to deliver the full principle. In our view, this aspect of the CRD is a retrograde step from the current situation.

The main obstacle to consolidated supervision is Article 68 of the proposal, which requires the quantitative capital requirements of the Directive to be applied at the legal entity level. It is true that Article 69 allows the Member States to waive this individual application but only for the subsidiaries within their jurisdiction and under very strict conditions. By restricting the waiver to within national boundaries, the European nature of banking groups is not entirely recognised and non-consolidated requirements at the parent entity level are generated. These requirements do not currently exist in the home country and serve no prudential purpose.

It is a paradox that the European Union, with a clear objective of a unified financial market, should choose a fragmented approach to banking supervision, burdening banks with multiple reporting requirements and additional capital constraints.

Banking groups are managed in an integrated and centralised manner on the basis of business lines and central functions. Specialisation calls for centralisation of expert centres. Risks must be measured consistently and aggregated to be efficiently managed by a risk management system operated on a group-wide basis. Risk models are conceived, monitored and implemented from head office. The interaction between risks, risk tolerance, capital planning and strategy is the domain of group executive management.

A clear example of this is the Advanced Measurement Approach for Operational Risk. Article 68 of the Directive implies that operational risk be measured on an individual level. However, banks measure and manage operational risk at group level taking diversification benefits into account. Given the scarcity of operational risk data, it is impossible to implement separate statistically meaningful operational risk models at a subsidiary level.

This business reality is clearly understood and recognised by the Basel Committee, which set the consolidated approach as a principle. The current CRD proposal is, therefore, the source of a major inconsistency with the international framework and a significant competitive distortion with the rest of the world. US banks, for example, will only be subjected to consolidated capital requirements.

We are told that the current fragmented legal framework in the EU is the reason behind this contradictory situation. If the current proposal for a Directive, which is supposed to deliver effective supervision for the banking industry, cannot overcome this obstacle, and if Articles 68 and 69 do not apply the Directive at the consolidated level, the need for the barriers to consolidated supervision to be removed should be clearly asserted.

The FBE understands that the Commission intends to work on this objective over the next 5 years as part of the post-FSAP agenda by harmonising *inter alia* deposit guarantee schemes, liquidity management and the lender of last resort at EU level. The FBE welcomes this forward agenda in the context of an overall review of a coherent framework for banking supervision in Europe. We urge the Commission to make its work plan public by mid-February at the latest and to set a specific timeframe for the work. These objectives and agenda should also be explicitly referred to in the CRD. We believe that a recital should be included which will refer to the need to review the level of application of the Directive once the Commission's work has been completed and in no longer than five years;

In the meantime, the main drawbacks of Article 68 must be alleviated. The following points provide a broad outline of the necessary changes to the proposal for a Directive. We are happy to address these ideas in more detail at any time.

1. Article 129, which gives the final say to the consolidating supervisor for internal model validation, is a first step in the right direction. However, the Supervisory Review and Evaluation Process and, more generally, most of the Pillar 2 and 3 requirements need to be applied at the consolidated level and therefore come under the global responsibility of the home supervisor with due regard for the responsibilities of the host supervisor. The Home Supervisor should coordinate both the Pillar 2 activities and reporting under Pillar 3 with the host supervisors and ensure that they are kept informed and provided with a single point of contact for the banking group. In our view, this is the only way to streamline the process and ensure that the objective of reflecting the entire risk profile of the group is met.

2. The Article 69 waiver should not be restricted to within a Member State. Given the current legal impediments the national option will provide Member States with the necessary flexibility to move towards consolidated supervision. However, against the background of the final objective of establishing a level playing field the national option should be removed after a transitional period of 5 years. Article 69 should also be extended to the parent company in order to avoid combining entity and consolidated level requirements. As stated the current proposal is a step backwards from the current situation in this regard. Article 52(7) of Directive 2000/12/EC explicitly allows exemption of the parent undertaking from the individual application.
3. Article 80 (7), which allows a zero per cent risk-weighting to be applied to domestic intra-group exposures under strict prudential conditions, should not be a national discretion and should no longer be restricted to national transactions. Most intra-group exposures are cross border as they relate to the centralised organisation of banking groups with risk management at consolidated level. There is no reason to distinguish between subsidiaries in the EU based on their country of registration and, hence to advantage national transactions over those between two Member States.

The new solvency framework is a major contributor to the financial stability of the global banking industry. The Capital Requirements Directive must be more than the sum of different national implementation projects. It should establish banking supervision as a Single Market concept, which aims to resolve the obstacles raised by separate national requirements and regulatory rigidities.

The FBE intends to develop these positions in more detail in the coming weeks and we are at your disposal should you wish to discuss these matters further.

Yours sincerely,

Guido RAVOET