



**Eurofi 2008 -  
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**Session [12D] - BANKING  
GROUP SUPERVISION  
PRACTICAL SCENARIOS:  
Information sharing,  
cooperation and decision  
processes within a College;**

**Liquidity management; Effectively alleviating day to day supervisory burdens; Learning from Supervisory Operational Network experience.**

#### The Panel

**Moderator:** **Patrick Pearson**, Head Unit Banking and Financing conglomerates, DG Internal Market, European Commission

**Panellists:** **Christian Lajoie**, Senior Vice-President group Risk Management, BNP Paribas

**Danièle Nouy**, Secretary General, French Banking Commission, Commission Bancaire (CB)

**Ieke van den Burg**, MEP, Member of the Committee on Economic and Monetary Affairs, European Parliament

#### The Debate

**Christian Lajoie**, Senior Vice-President group Risk Management, BNP Paribas, said banks were very pleased to be able to work closely with their industry supervisors. He cited three initiatives launched by the CEBS that the Industry particularly welcome .

- 1) The advisory role in interpreting European regulation
- 2) The operational network launched to make sure that supervision practice was consistent across the banks
- 3) The organisation of the Colleges of Supervisors.

These initiatives were very good for bolstering co-operation between supervisors and also to mandate a dialogue with the banks. "But the complexity of the regulation and the financial crisis has called for stronger links and intimacy between supervisors and banks' management, which requires a lot of resources, while efficiency was obviously an imperative for both parties," said Mr Lajoie.

Efficiency was not always achieved, he said. Both the banking industry and their supervisors lacked resources. Both had to face the crisis, the banks had to manage their risks first, they had to answer questions from the supervisors about what was going on, and work on long-term issues, such as the implementation of Basel II.

The CEBS has mainly played an advisory role. It had been hindered by its club status on the one hand, but also by an intricate system of regulations compounded with multiple options left to national discretion. "In this condition it was up to the CEBS to find a consensus based on alignment to the most demanding supervisor. The internal debate was probably fruitful but the outcome was disappointing for banks despite the openness of the supervisors."

The Supervisory Operational Network (SON), was a superb way for supervisors to understand the nitty gritty of the actual supervision practices of cross-border banks. But the actual impact for the banks was yet to be known. No agreement had been made on common reporting. Supervisors could not understand that for many banks, because of their data processing system, subsidiary reporting could not be made available before the consolidated one. Even on very practical matters, it was hard to make a decision and to listen to the actual difficulties met by the industry. The SON had created a great opportunity for dialogue with the industry but there should have been more concrete outcomes.

"Colleges were also excellent platforms for exchanges and better mutual understanding. They work pretty well," said Mr Lajoie. "however, they lack of a legal framework to reach a decision." They showed, however, their limits when information requests were made to banks from various supervisors all over the world, and even within Europe, in disorder. Colleges should go beyond this stage and should focus on decision-making. The banks, meanwhile, should seize the opportunity to be heard and get an answer to their questions. Too many times, banks' participation was reduced to useful but passive information on their strategies etc.

"The goodwill of all actors, notably supervisors, is not in question. We are at a discovery stage but now we have to draw the lessons that we have learned. Because of that I would dare to suggest a few recommendations.

"Supervisors must have the right resources. It is important to increase the banking business knowledge of the supervisors. This point is really critical if industry wants to avoid invasive and over-regulation, if we want supervision to look forward and to be able to anticipate, which is probably the best way to prevent crisis." There should be more exchanges between supervisors and the industry, and between national supervisors. Supervisors should be paid "at their right price". Supervision deserves adequate and strong resources.

It is also important to make Colleges more effective. "They must become the true collective supervision body of the banking group, which means the parent company and all its constituents, under the chairmanship of the home supervisor. There should be a more detailed agenda established in due time, organising a structure of dialogue with the bank around a

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list of items." There should be an enlargement of the College scope to all supervisory matters. This should be encapsulated in EU regulation to make it effective.

Mr Lajoie said that following the dialogue, a decision must be reached. "Banks need to know what the supervisors are expecting at the end of the day. There must be someone who can make a decision – this must be the home supervisor.

"I understand that some persistent disagreement may appear, and that all supervisors may consider that their opinions have not been well understood or not sufficiently taken into account. In that case a non-suspensive mediation mechanism could be envisaged to settle the issue."

Strengthening CEBS is key, he said. It must be a respected guardian of consistent regulatory implementation and should have an effective decision-making process. "They have already adopted a new approach based to qualified majority voting, which is a breakthrough and I think this is a very good decision. They probably need to enlarge or have a more formal admission of their duties to make sure the rules are consistently implemented."

Mr Lajoie said CEBS could help in the liaison with central banks to identify emerging bad or why not good practices in banks. "It's not a matter for them to substitute or interfere with the bank's management. But at least they have a very good position to know in detail the main decisions that have been taken by various banks through the national supervisor network."

"Every time we can identify banks doing the same thing, you are probably in a situation where a crisis is preparing. This could be added to the CEBS objective." The central bank, which is in charge of financial stability and has access to macro economic data, may be comforted by this analysis from the supervisors.

The decision of the CEBS should be binding. An exemption clause could be used, but only for legitimate reasons that are publicly known.

Mr Lajoie said: "The independence and the influence of CEBS can only be built with permanent resources. If they have to rely on the contribution of their members, they are necessarily somehow constrained by that and they need to get some independence from independent resources."

Danièle Nouy, Secretary General, French Banking Commission, Commission Bancaire (CB), said: "We have to deliver something that works practically. In my view colleges are key to deliver an efficient and safe supervisory environment, because they produce exactly what is needed for the supervision of cross-border groups; good co-operation with stable connections between national supervisors, not only the policymakers but the people doing the supervision on a daily basis." She said they were the best way to prepare for crisis situations because, "when you know each other you do a much better job in difficult situations".

A lot of experience had already been gained with positive results but progress was too slow. "We still have significant challenges ahead of us including full implementation of the Ecofin conclusions, so we need to move forward expeditiously."

CEBS had put a lot of efforts into the colleges. Ms Nouy explained the functioning of French colleges, where CB was the home supervisor. "We have regular meetings of these colleges at least twice a year. We have a permanent dialogue with other supervisors between college meetings."

The colleges worked on a two-tier basis. The closest links were with the tier one part of the college, which she referred to as 'the family'. This comprised EU supervisors of European entities, subsidiaries, and significant branches. The tier two part she referred to as 'friends', namely supervisors of significant subsidiaries in third-party countries. "The role of these colleges is to exchange information and to co-ordinate action on supervisory issues. We are firm believers of on-site examinations," said Ms Nouy.

College meetings would include sessions with the banks' representatives. French banks had been very co-operative in this respect, sending high-level people to these meetings. This was important to develop direct contact between senior managers and the supervisors.

"The key outcome of colleges so far in France and the rest of Europe has clearly been the Basel II Pillar 1 approval that has been a wonderful opportunity to start working together. The Pillar 1 approval process has been successful, but this success has been obtained thanks to an excellent well-defined legal framework, article 129 of the Capital Requirements Directive (CRD)." She urged regulators, the Commission, and members of the European Parliament to make more use of this article in European regulation.

"I stress this point because to deliver efficient and consistent supervision, we need to have clear and well-defined decision making process in the colleges. The home supervisor should have a strong co-ordinating role as well as the final say regarding important decisions, and the deciding vote." She recognised the need for a mediation mechanism if there was disagreement.

There were other things to take into account in order to alleviate competition concerns. "The convergence of supervisory practices within the colleges is crucial too. That's why the operational networking project of CEBS is also important." She cited two documents; a range of practices and a template for co-operation within colleges, which was currently being tested and implemented.

"This template will deliver some harmonisation in the functioning of the colleges but not to the extent needed. The template is too long and too complicated and it takes a too legalistic approach, which is not helpful."

However, Ms Nouy stressed that it would take more than colleges' and supervisors' goodwill to promote supervisory convergence. Both colleges

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and supervisors would benefit a lot from more harmonised rules. "It is an understatement to say that given the current legal framework, supervisors face terrible difficulties to apply similar rules, the single rulebook to all entities of a given group in Europe."

There were more than 100 options on national discretion in the CRD, which was the source of many difficulties. "How do you deliver harmonised reporting with so many national discretion options?" asked Ms Nouy. "In my view national discretion options should not exist. I hope the people in charge of Solvency II will be smarter than the banks' supervisors."

If these national discretion options were included merely to get the regulation started, Ms Nouy suggested that there should be a sunset clause on the options. They should automatically disappear after a certain time, or should be limited to domestic entities. Cross-border groups would not have the option of using national discretion options.

CEBS was involved in several projects that should result in more convergence. Large banking groups were requesting 'country neutral regulation' on supervision. Ms Nouy said you had to start with regulation, and then it would be possible to deliver country neutral regulation.

Another promising practical step was the development of a European culture. The idea was to learn and converge by working together. "Colleges have been helpful in this respect but various other initiatives can also foster the development of a supervisory culture. If we have harmonised regulation and supervisors are trained together, at the end of the day they should use it and implement it in the same fashion." She cited a very successful example of this idea of learning by working together as the CEBS project regarding European on-site exams.

"What we need are resources. It's extremely difficult to explain to our bosses that it's a brave new world. What we were doing on a domestic, or at best a bilateral basis, now we have to do on a multi-lateral basis. It takes more time, it takes more people to do it properly, because we have to talk more before taking a decision, but the outcome is of much better quality for everyone."

She said incentive was a problem for reporting. "What are the incentives for supervisors to reduce the regulatory burden?" It was very hard to explain to her colleagues that they could request fewer reports, that they did not need that much to do their job. During the crisis reports were arriving regularly but were not the most useful tool. Ms Nouy suggested dialogue with the banks could have been more helpful.

"At the end of the day, the efficiency of this EU decentralised model, based on the efficiency of Colleges, requires a strong CEBS to ensure convergence. I hope the implementation of the Lamfalussy road map, as well as the lessons learned from the turmoil, will help us move forward."

**Ieke van den Burg**, MEP, Member of the Committee on Economic and Monetary Affairs, European Parliament said to address this issue you had to speak about the architecture and burden sharing.

She recalled a previous panel in which the Former Minister of Economy and Finance for Italy, Tommaso Padoa-Schioppa, blamed the supervisors for not getting further in terms of co-operation.

She refuted this argument. Neither the supervisors, nor the Commission were to blame for the obstacles created by national discretion options. "The background of national discretions and the brakes on further progress are more at the political and national level. There are some really important economic interests of member states involved in keeping structures as they are. There is a close link of national mandates of supervisors with national interests of being the most attractive and competitive financial services marketplace. We really have to move towards a more independent supervisory architecture."

She suggested something similar to Ms Nouy's proposal: a European system of supervisors built on the present structure of national and sectoral supervisors, but with something added on top, like the European System of Central Banks, to make sure that joint responsibilities were taken.

She said it would be difficult to achieve this structure before the end of the year. Parliament had therefore decided to take a short and a long-term approach. "For the longer term, I hope there will be a decision in this period of the French presidency, to establish a group of wise women and men to create an architecture. For the short-term, we have asked some very concrete legislative proposals from the Commission to establish mandatory Colleges and to legally underpin the status of the Level 3 committees."

Many people were afraid that as soon as you spoke about European supervision bodies, you are creating huge new bureaucratic structures, which leads to a new debate, for instance in the Ecofin council, about where they should be located. "I was really surprised when I first was engaged six, seven years ago in the debate about establishing the Lamfalussy L3 committees, that for the Council the main discussion was about where these should be based," said Ms van den Burg. "This underlines once more that there are national interests, which are much more dominating than the real purpose and perspective of creating a solid structure. The time is over for this. We have serious problems in the financial markets. What we should do is put every effort together to create an efficient structure of supervision."

Cross-sector co-operation was also important. "Take the example of Société Générale and this rogue trader Jerome Kerviel. It was already noted by the securities supervisor in Hessen Germany that something strange was happening but this information did not reach the French banking supervisor in due time. Would we have had a better structure of common exchange of information, we could have prevented a lot of losses for Société Générale."

On colleges and the decision-making structures of home and host supervisors, Ms van den Burg agreed with the other panellists on the need for a lead supervisor and she stressed the importance of relations

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with third country supervisors. Major US banks based in London should also create and participate in this type of structure. All this micro prudential information about the large financial conglomerates should be linked to information available with the central banks, and the markets supervisors.

There was great concern in member states that only host subsidiaries and branches of foreign large groups, that they would not have a clear say in the colleges. "They are worried that the lead supervisor will put upon them many things, without taking their concerns seriously" she said. "You need to have a balance if you want to build this on trust and confidence."

Mediation was important when there was not a common position and there was a conflict between the supervisors in a college. "We need to have a binding and more solid and independent impartial system of mediation. The present Article 129 structure and the proposals in Solvency II are only a "comply or explain" system: the final decision is taken by the lead supervisor. But there must be a mediation structure that can overrule if there is really a conflict."

Ms Nouy responded to a question from the floor about who should be in the colleges, and their legal authorisation. "It is practically very easy. We consider that Europe is the domestic territory of banks. We start the college meeting with everybody; third countries and European countries. That can last for a day for example. Then we have the second day with 'the family', to get more into the details, to share more because we are part of a common market for banks. We want to have excellent relations with our transatlantic colleagues.

"Regarding the legal question, I would be a bit provocative and say, please don't speak about legalistic issues. That's not what we need. We need a clear will of supervisors to find solutions together, practical solutions to practical problems in a bottom up approach. Then at the end of the day, if it is a German bank they would draft it in the German framework. If we start by saying what is possible in the legal German environment, we will fail.

"That's the same for burden sharing. We don't care that much about who will take the bill after a crisis at this stage. What do we need to address a crisis properly? We need to have defences that are in good shape, well thought-out and that are regularly stress tested. We do a lot of stress testing in the EU environment. What we know is that if there is a crisis, the defences are there, they work, they have been tested. After the first crisis we have to sit around the table and decide who pays the bill. In my view it is very likely the role of supervisor."

Mr Lajoie responded to the question: do 'friends and family' Colleges work? "Yes, up to a point. We have a big issue here because we are in Europe and we need a legal framework, a legal basis to make these colleges work. At the same time banks are global and these colleges need to have among them non-EU supervisors.

"If you need to make a decision, some consensual decision, even though you have the last say then you must organise the colleges in a flexible way, and in the case of a cross-border bank you probably need to have a two-tier structure. We should give the home supervisors the flexibility to organise the colleges according to the structure of the banking groups, because they are not all organised in the same way." He cited Fortis Bank, which had three main national supervisors.

On mediation, he said it could be important, but there should not be suspensive mediation. "Mediation should not be a way to push forward and not to decide, otherwise the system will be blocked."

Ms van den Burg responded to a question about the inclusiveness of colleges. "We have tried in our report for the European Parliament to give some principles. There are two elements; one is the decision-making, the other is the stage of information, particularly confidential information." There could be a difference between core and other members in the colleges according to the importance of the group in the different Member States, she said.

On decision-making, Parliament had tried to indicate what could be the criteria. She said you needed to respect the perspective of the group, where the main assets were, and that of the host member state, where the group may have a very minor part of its total assets, but nevertheless may have a large proportion of the savings in that (small) Member State and pose systemic risks. Regarding third countries, she said there might be a problem in the exchange of confidential information, if the third country is not bound by the same European rules and if there is not a reciprocity in the requirements for exchange of information.

She also addressed the issue of accountability and liability. "You take the decision inside a legal framework, and you cannot afford to leave this to those who are not liable in case there will be procedures. I agree that this is complicated in the present structure and important to take into account. There are already court cases against supervisors who made wrong decisions so it should be clear who's liable. Nevertheless we shouldn't make this problem prohibitive to find solutions for binding mediation and conflict resolution"

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