

14 May 2009

## **Minutes of the Consultative Panel meeting on 17 February 2009 in London**

### **Opening of the meeting**

1. The fourteenth meeting of the Consultative Panel (CPL) was held at CEBS premises, London, UK.
2. Mrs. Kerstin af Jochnick, CEBS Chair, welcomed Consultative Panel Members and Observers and Mr. Lucca Tullio who replaced Mr. Davide Alfonsi (Intesa SanPaolo) and Mrs. Kristelle Maouad who replaced Mr. Christian Lajoie (BNP Paribas).
3. Mrs. Kerstin af Jochnick informed the Panel about the finalisation of CEBS work programme that is now published to CEBS website and expressed her appreciation to the industry representatives for the positive feedback received during the prioritisation exercise. As CEBS's work programme was submitted to the EU institutions (European Commission, Parliament and Council), Mrs Kerstin af Jochnick stressed the importance of keeping a certain level of flexibility so as to follow the market developments and to meet the challenges of priority 1 and 2 issues.
4. CEBS's Chair debriefed the CPL members about the revised Decision establishing CEBS published at the end of January and the non-exhaustive list of tasks that CEBS is requested to perform. Mrs. Kerstin af Jochnick also referred to the de Larosière report expected to be published at the end of February and the very constructive dialogue that CEBS held with this high-level group ("the Group") chaired by Jacques de Larosière. Finally, CEBS Chair invited the Panel members to appoint representatives to the newly established industry expert group on large exposures.

### **Current Crisis Situation**

#### **a. Report on national plans for the stabilisation of markets**

5. CEBS's Vice Chair, Mr. Giovanni Carosio, presented to the Panel the report on national rescue plans. In general, the involvement of supervisors seems to be satisfactory, however differences in bank recapitalisation had effects on the level playing field, altering competitive conditions and raising prudential concerns.

Furthermore, there are concerns that some banks will not be able (or would not be willing) to receive government support, a scenario that could adversely affect the credit supply and lead to pro-cyclical effects. The harmonisation of rules has also been affected by the implementation of "de facto" prudential standards.

6. Further work on this field would be undertaken by CEBS's expert group on prudential regulation (EGPR) in two main aspects: a) quantity of capital; similar approach should be followed within the EU and adequate capital buffers to be defined by following a common methodology (i.e. stress tests) and b) quality of capital; instruments that have the highest quality in terms of loss absorption and flexibility of payments to be classified as core tier I for regulatory purposes.
7. Following the presentation of the paper, an extensive dialogue was held regarding the capital add-ons, the stress tests exercises, the various definitions of tier I capital in Europe and the non comparability of capital instruments. Mr. Giovanni Carosio cited that CEBS work is focused on the overall assessment of banks' capital buffers and not on creating a link between stress tests results and capital-add-ons. Mrs Kerstin af Jochnick concluded that there are currently different supervisory practices used to assess/determine capital buffers, while there is an absolute need to have in place adequate capital buffers for the future and a common approach on the level and quality of capital.

#### **b. Risk assessment**

8. CEBS's Chair informed the panel about the work undertaken by CEBS on risk assessment. CEBS is expected to perform risk assessments twice per year while possible overlaps should be avoided since work in this field is undertaken by other external parties. CEBS has set up a risk assessment framework and the exercise performed is based on the list of topics developed by CEBS and the WGMA of the BSC, focused on home host issues. The consolidating supervisor is in charge in organising the assessment and to provide answers to the topics raised. The exercise is currently limited to the 17 SON banks, but the aim is to extend this group to all 41 colleges that should be in place till the end of 2009.
9. The paper was welcomed by the Panel. However, Consultative Panel Chair stressed the need to avoid ending up with a list of statistics and to involve practitioners in this process, while the quality of the figures used was also questioned.

#### **c. Pro-cyclicality**

10. Mr. Giovanni Carosio presented CEBS's proposal and objectives on mitigating possible cyclical effects. The main objective is to have capital that is more stable, while it was explicitly cited that the proposal illustrated is in the context of the supervisory review and evaluation process (SREP). The idea is to use a scaling mechanism between current PDs and recessional PDs. This scaling factor could be calculated under three different options; on rating grade basis, on cohort basis or on portfolio basis. A first meeting with the industry has been already held in January 2009.
11. While the approach was presented by CEBS's Vice Chair as a Pillar 2 tool, some members of the panel argue that it is rather Pillar 1 tool. In addition, members

stressed the need to have a rather global solution and not solutions agreed on bilateral basis, between banks and supervisors.

12. Mr. Giovanni Carosio concluded by stating that undoubtedly there is a need for dynamic provisioning. In addition, under this Pillar II approach, dialogue between the banks and the supervisors should be intensified, while supervisors should assess the accuracy of the calculations made by the banks. The Consultative Panel members were invited to continue providing valuable input on this.

#### **d. Risk management**

13. A Task Force on Risk Management has been established in order to perform the work on this field linked to the G20 recommendations and Action Plan. A lot of work on this topic has been made while CEBS was working on the implementation of the CRD. CEBS paper on risk management principles will be discussed in the next CEBS plenary meeting and also submitted to the EFC, while no major changes are expected compared to current guidelines and no need for more regulation has been identified; however there is obvious need for more focused discussions.
14. Mr. Andrew Cross mentioned the report prepared by the Senior Supervisor Group that was published in March 2008 and includes detailed self-assessments and proposed that CEBS should take it into account. He also proposed to compare the IIF recommendations to CEBS guidelines, something that could give a tangible evidence of what banks are implement in terms of risk management.

#### **e. Remuneration**

15. CEBS report on remuneration is also linked to the G20 recommendations and action plan and it is undertaken by the Internal Governance Task Force. It was also mentioned that the report will be published for one month consultation.
16. The report was subject to criticisms, since some of the consultative panel members stated that the remuneration policies were not the cause of the crisis and that CEBS, at least, should stay rather rational on this issue and regulators should reform the financial architecture to the right direction. They also declare that there is no correlation between the high compensation and high risk taking. Mr. Thomas Huerta also referred to the IIF recommendations and mentioned that the remuneration practices followed had a role in contributing in the crisis and the call to have changes in the remuneration policies isn't just a political reaction to huge salaries. Furthermore, he clarified that CEBS recommendations are not argue for low salaries. Mrs. Kerstin af Jochnick concluded that CEBS work on this field would not go in much detail; however, CEBS would try to produce a view among supervisors and deliver this view to the EFC while the main objective of this work from CEBS's perspective is to rebuilt market confidence.

#### **f. Transparency**

17. CEBS's Chair presented the work that CEBS is undertaking in this field that is expected to be completed at the end of the second quarter of 2009. Mrs Kerstin af Jochnick stressed how important is to have improvements on this area and debriefed the panel about the work that has been carried out till now. Following the June good practice disclosures, a follow up report has been published in

October 2008, concluding that 80% of the banks included in the sample provide adequate quantitative disclosures on the impact of market turmoil and on exposure levels. However, no improvement has been made regarding qualitative disclosures (i.e. business models). CEBS will not assess the 3<sup>rd</sup> quarter disclosures, but the last quarter 2008 and the preliminary year end disclosures. Further work would be also undertaken in respect to banks' audited annual reports, not focused only to the CEBS best practices but also to the Pillar 3 disclosures.

18. Following this update, an extensive dialogue was held focused on the efforts that the industry has made in order to improve transparency disclosures. However, some members of the panel expressed concerns that even if improvements have been achieved, no great interest has been expressed by the users since some of them they are not really familiar with the accounting rules. Mr. Arnoud Vossen, Secretary General of CEBS, concluded the discussion by arguing that the answer to this dispute is not more transparency but more focused transparency.

#### **g. Valuation**

19. CEBS work on valuation was presented by Mrs Kerstin af Jochnick. Following the June report on issues relating to complex and illiquid assets and the dialogue that CEBS held with standard setters, a follow up work is currently undertaken by CEBS in order to assess to what extent the issues raised in June report have been addressed by the industry and other stakeholders. The general feeling is that some of the issues raised have been taken into account, as the classification and reclassification aspects of many instruments. However, there are still issues to which further improvement should be reached.
20. The consultative panel members agreed that valuation is a fundamental issue and that there are two basic rules that the industry should follow; the fair value option should be given only for the liquid products that are easily accessible and for which market prices are available while the amortised cost option should be followed for i.e. complex equity and other derivatives. It was also cited that deviations from these fundamental rules affect banks' transparency. Finally, the Panel members stressed the need to re-orient banks' balance sheets and questioned the role of supervisors in this field.

#### **Developments at the EU level, especially on the CRD**

21. The representative of the European Commission (EC) provided an update of the work that is currently performed. The basic challenge will be to move further based on the de Larosière proposals. Mr. Patrick Pearson also mentioned the intention of the Parliament to stress the importance of colleges and the need to have colleges for 41 major banking groups till the end of the year. In addition, EC is currently dealing with the proposed changes in the CRD and in particular with the: i) securitisation, ii) large exposures, iii) non-risk based matrix, iv) framework on impaired assets, v) remuneration and vi) home- host issues.
22. Following the debriefing from Mr. Patrick Pearson, an extensive dialogue was held mainly focused on the non-risk based approach and on the home-host issues. As regards the first topic, the consultative panel members expressed their concerns about the objective and the design of this approach as well as about

the proposed timing that will be implemented. EC representative stressed that the basic idea behind such an approach is not to replace the current one but to act as a supplementary measure.

23. As regards the home-host issues, Mr. Mick McAteer cited that the objective of the work on this field should be to ensure more, better and timely exchange of information and the legal right of the host supervisor to intervene when this is regarded as important.

#### **Discussion on the work of the de Larosière group**

24. Mr. Patrick Pearson informed the Panel about the main issues that would be raised from the Larosière Group, such as i) the harmonisation of the present regulatory framework in Europe, ii) inadequacy of the peer review mechanism iii) the need to enforce binding mediation mechanism so as to resolve cross border disputes iv) the implementation of qualified majority voting in the decision process of the level 3 Committees v) the establishment of colleges for all major cross border groups within 2009, and vi) the importance of comprehensive risk assessments.
25. In this context, Mr. Patrick Pearson also mentioned the constructive dialogue that CEBS had with "the Group" and that the major issues/problems raised by CEBS will be taken into consideration. As regards, whether the de Larosière report could lead to a revision of the Treaty, he mentioned that if this is the case then the normal legitimate process should be followed.

#### **Functioning of colleges of supervisors**

26. Mrs Kerstin af Jochnick informed the Panel about the discussions held at CEBS December plenary meeting on colleges and the decision to have an action plan for the setting up of colleges for all major cross border banks in Europe.
27. CEBS work on colleges was well received from the Panel and was commented as a good starting point. The main challenge that should be met in this respect is the desirable convergence of supervisory practices and the process followed in order to resolve possible disputes. The latter is directly related to CEBS role and could be managed through the implementation of the mediation mechanism. Mr. Arnoud Vossen concluded the discussion by stating that the establishment and successful operation of colleges is a two-folded process and requires both the supervisors' and the industry's commitment.

#### **Micro loans given by non credit institutions from the risk management and supervisory perspectives**

28. This topic was raised by Dr. Herbert Pichler (Austrian Federal Economic Chamber) who expressed his concerns on the lack of regulation and supervision of all financial market participants. Mrs. Kerstin af Jochnick stated that this is a rather political issue and that in some countries there is extensive dialogue between supervisors and governments on this issue.
29. The majority of the consultative Panel members agreed that the regulation of these non credit institutions can't be addressed under the CRD and it is a topic that could be raised by the Parliament.

### **Discussion regarding government intervention, level playing field and normalisation of the banking industry**

30. The Consultative Panel Chair, Freddy Van den Spiegel, raised this issue that was briefly touched upon. The main question raised was whether CEBS could take this issue on board, but it was generally agreed that this is mainly a political driven issue.

### **Public consultation and informal dialogue**

31. Under this session, Mrs. Kerstin af Jochnick briefly presented other areas of CEBS work such as i) custodian banks, ii) large exposures, iii) liquidity risk management and the review of Financial Conglomerates Directive. Some of these issues will be extensively discussed in the next consultative panel meeting.

### **Participants**

32. The following members and observers of the Panel were present: Freddy van den Spiegel (Chair), Herbert Pichler, Klaus Willerslev-Olsen, Berstrand de Saunt Mars, Kristelle Maouad (replacing Mr. Christian Lajoie), Michel Bilger, Klaus-Dieter Kremkow, Demetrios Lefakis, Tullio Lucca, Zygierewicz Mariusz, Jose M Mendez Alvarez-Cedron, Peter Knutsson, ~~N~~ Richard Desmond, Andrew Cross, Hugo Banziger, Mick McAteer, Stephen Sanders, Volker Heegemann, Walburga Hemetsberger, Wilfred Wilms, Nicolas Jeanmart