



Fédération Bancaire Européenne
European Banking Federation
Le Secrétaire Général

FBE Letter 0433

NF/UW
E-mail

Mrs Danièle Nouy
Chairman
Committee of European Banking Supervisors
Floor 18, Tower 42
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Brussels, 16 June 2006

Subject: Questionnaire on Market Practices on Large Exposures

Dear Mrs Nouy,

Chère Danièle,

The European Banking Federation (FBE) welcomes the opportunity to comment on the Committee of European Banking Supervisors' (CEBS) questionnaire on market practices regarding Large Exposures (LE). We believe that the current LE rules should be aligned with the spirit and the practices of the Basel II rules. To ensure that this is appropriately done the review ought to be extensive, and it should especially take into account that concentration risk in general is treated under Pillar II.

The FBE has decided to focus its response on the regulatory questions. We note that the wide use of national discretion across the EU has lead to considerable divergences. A review should therefore also address level playing field issues. Furthermore, in some countries firms experience substantial reporting requirements. Requirements which only serve regulatory rather than prudential purposes should be reduced as much as possible.

Please find our response enclosed. For any questions, please don't hesitate to contact either myself or my colleague Uta Wassmuth (u.wassmuth@fbe.be).

Yours sincerely,

Guido Ravoet

Enclosure: 1



Response to CEBS' Questionnaire on Market Practices on Large Exposures

1. The European Banking Federation (FBE) welcomes the opportunity to respond to CEBS' questionnaire on the Large Exposures (LE) rules in the EU. The LE review in the EU will be an important piece of work that must be based on a thorough understanding of the practices used by supervisors and market participants alike. We therefore also welcome the stock take released by CEBS on supervisory practices regarding LE.
2. As far as CEBS' questionnaire is concerned, the FBE has chosen to focus its response on the regulatory environment. Individual institutions and some of the FBE's member federations will respond to the technical questions posed by CEBS.
3. Given the scope of the task faced, we expect that it will take several years before a new regime can be put in place. Whilst we acknowledge that the European Commission is asked to submit the review by year-end 2007, we believe that within this time frame appropriate proposals can only be general and high-level. In addition, it has already become apparent that the implementation of the CRD will absorb banks' resources for a significant period of time. Substantive new pieces of regulation should as far as possible be avoided before the CRD and other important pieces of legislation impacting on financial institutions have been well integrated into institutions' management. However, there might be scope to reduce major sources of competitive implications in a shorter time frame.
4. We note that banks' overall implementation burden of the new Basel II rules makes it difficult to respond in the detail commensurate with the expected scope of the LE review. Institutions are responding on a best-efforts basis, trying to deliver as much information as possible. However, we call on CEBS to consider this questionnaire as an initial measure in an ongoing exercise, and to be open to additional industry input going forward.
5. Whilst we appreciate CEBS' stock take on supervisory practices, we note that there is some scope to deepen and broaden the aspects considered. In particular, we believe that a more granular view on the comparative aspects would allow for a more meaningful analysis of the potential factors of competitive distortions. For example, we assume that there might be significant differences regarding whether or not, and to what extent, temporary breaches of the limits are tolerated in each jurisdiction.
6. Furthermore, in an increasingly global financial environment competitive implications have gained significance throughout the last years. We therefore believe that at least non-EU members of the Basel Committee on Banking Supervision should be taken into account on a best-efforts basis.
7. With regard to the stock take, we also wish to point out that there are indications that major divergences exist in the treatment of credit derivatives across the EU. Whilst this aspect was not considered in the stock take on supervisory practices, it should be explored whether this issue can be addressed through quick, straight-forward adaptations of the regulatory framework.

8. We understand the stock take as a test case for the Supervisory Disclosure Framework and against the objectives of sound governance and convergence of supervisory practices defined by CEBS itself. We find the overview a helpful starting point but would encourage CEBS, with regard to the future use of the framework, to give particular attention to the practical application of the written rules. We also encourage CEBS to include the findings of the present overview in its Supervisory Disclosure Framework with a view to regularly updating it.
9. Given the basic nature of some of CEBS' questions, the FBE is concerned about the timing of the concentration risk parts of CEBS' CP 11. Institutions' responses to the questionnaire should inform the supervisory guidance. We would therefore suggest that CEBS only publish the principles themselves in CP 11, and defer the additional guidance until the responses have been sufficiently analysed.
10. With regard to Question 16, we note that the LE regime has so far proven effective in addressing the key risks inherent in LE. However, the Basel II framework changes risk management to the core. The LE rules ought to be aligned with the spirit and the methodologies of this new framework. Banks have developed different approaches to monitor and manage their LE for internal management purposes and use internal limits fitted to their own business and risk profiles. The review should take account of the work carried out in this area, which treats concentration risk in a holistic approach under Pillar 2. This concerns in particular the 800% limit for the total of LE. In this context, mitigation also plays a major role and we look forward to CEBS' report on these instruments.
11. Most divergences within the current regulatory environment result from the wide use of national discretion across the EU. In fact, there are significant differences in the written rules and in their practical application as regards both the limits to individual counterparties and the kind of limits covered by the LE regime. We therefore believe that a review of the current regime should also address level playing field issues, as well as bring about more consistency and convergence of supervisory practices.
12. Regarding the introduction of additional limits, we believe that new legislation should only be introduced where a market failure has been identified. On an initial analysis, this does not appear to be the case. We would call on CEBS and the European Commission to provide evidence of the need for regulation before recommending or issuing new proposals.
13. In terms of impact on business decisions, the current limits for Intra-Group Exposures have been identified by a number of institutions as constraining. The FBE would also question the prudential purpose of these limits, given that risk management is carried out at group level. In addition, some large cross-border groups have seen their activities restricted as a result of the national discretion now included in Article 111.2 of the CRD.
14. With a view to inconsistencies of the current regime with internal management practices, we note that large, cross-border groups manage LE at group level. This is as opposed to the application of the CRD not only at group level but also at sub-consolidated level, which can moreover lead to supplementary and unnecessary capital requirements. To allow for compensation effects to be taken into account, LE should be measured at group level.
15. We furthermore point out the regulatory burden imposed on banks by the extensive reporting requirements in place in some jurisdictions. Regulation should serve a clear prudential purpose, and any additional rules should be kept to a minimum. In addition,

the different rules that are currently in place also have competitive implications. A more streamlined reporting regime that focuses on the material risks identified by the institutions themselves would lead to more consistent, and thereby competitively neutral, requirements.

16. As a consequence of the fact that the LE were largely left unchanged, some of the exemptions included in the CRD foresee that LE continue to be calculated on the basis of – sometimes weighted – outstanding amounts. This is at odds with the determination of exposures for credit risk under the new rules and may lead to a situation where banks have to run a dual system for the calculation of normal exposures on the one hand, and LE on the other hand. A review of the LE regime should strive to allow banks to use the same IT system for the measurement of LE as for other exposures.