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Internal Market and Services DG

**FINANCIAL INSTITUTIONS**

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**Subject: Request for advice on information required to be exchanged under Article 42 CRD**

Dear Ms. af Jochnick, *Dear Kerstin,*

At the meeting of the European Banking Committee ('EBC') on 5<sup>th</sup> March, it was agreed that the Commission would write to you with a formal request for the advice of CEBS on the classes of information that competent authorities are required to exchange under Article 42 of Directive 2006/48/EC ('the Capital Requirements Directive' or 'CRD').

As you are aware, the context for this request is the ongoing work of the Commission and the EBC on the supervision of branches by the home and host competent authorities and, more broadly, the Commission's proposed White Paper on tools for early intervention to prevent a crisis that is scheduled for publication in June.

The purpose of this request is to increase certainty and a shared understanding among supervisors about the information that home and host competent authorities are required to provide, or are entitled to receive, in relation to credit institutions that carry on activities in a Member State other than their home State through a branch. A shared understanding of the information covered by the obligation in Article 42 is necessary for the effective cooperation between home and host authorities in the supervision of credit institutions that operate through branches in one or more Member States, and to ensure that host authorities are in a position to take precautionary measures in a timely and effective way in appropriate cases.

## **1. BACKGROUND**

### **Ongoing supervision of branches**

The Capital Requirements Directive allocates responsibility for the ongoing supervision of credit institutions with one or more branches between the competent authorities of the home and host Member States (as defined in Article 4 CRD). Under this framework, general

responsibility for prudential supervision of a credit institution and its branches falls to the competent authority of its home State, and home State rules apply, except in those areas that are specifically allocated to the authority of the host State of a branch.

The **home** State supervisor of a credit institution is responsible for:

- internal governance arrangements, internal controls, administrative and accounting procedures (Art 22 CRD);
- own funds, solvency, large exposure lending limits and participations in the non-banking sector (prudential supervision - Art 40 CRD);

in relation to the legal entity as a whole (including its branches in other Member States).

The competent authority of the **host** State is responsible for the supervision of the following aspects in relation to the branch and its activities within the territory of that State:

- a) Conduct of business and market transparency rules (Art. 32(7) MIFID);
- b) Monetary policy (Art. 41 CRD);
- c) Liquidity, "in cooperation" with the home competent authority (Art. 41 CRD). Host supervisors are permitted to impose the same liquidity requirements on branches from other Member States as apply domestic banks.
- d) Statistical reporting on the activities of a branch (Art. 29 CRD). This permits host authorities to require branches to provide the same information that they require from domestic banks for statistical purposes.
- e) Non-prudential host State rules that are "adopted in the interests of the general good" (Art. 31) in areas that have not been harmonised or coordinated in EU legislation. In some cases, rules have been specified as such by the Court of Justice, e.g. rules relating to advertising<sup>1</sup> and protecting the integrity of the financial sector.<sup>2</sup>

### **Host powers of supervisory intervention**

In addition to the responsibilities allocated under the general framework for ongoing supervision, the CRD confers additional powers of intervention on the competent authority of the host Member State in specific circumstances.

Article 30 CRD permits host State intervention in cases where a branch is in breach of the prudential rules that remain under host country control (monetary policy and liquidity). The host State supervisor can request the branch to remedy the breach. If the branch fails to do so, the host supervisor must then inform the institution's home State supervisor, which must take appropriate measures to ensure that the institution rectifies the irregularity. If the violation continues in spite of any measures taken by the home State authority, the host supervisor is then permitted to intervene directly to prevent or punish further violations.

Article 31 CRD confirms the power of host Member States to take appropriate measures to prevent or punish the breach by a branch of host country rules that have been adopted "in the interests of the general good".

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<sup>1</sup> 'Mediawet' case (C – 148/91)

<sup>2</sup> 'Alpine Investments' case (C – 384/93). Article 37 CRD also expressly recognises branches must comply with host State rules governing the content and form of advertising that are adopted in the general good.

Article 33 CRD permits the host Member State, in the event of an 'emergency', to take "any precautionary measures necessary to protect the interests of depositors, investors and others to whom services are provided" by the branch, without having to follow the procedure laid down in Article 30 CRD. The host State is not required to inform the home State authorities before acting, although it must inform the Commission and the competent authorities of the Member States concerned at the earliest opportunity.

Lastly, Article 34 permits host States generally to take appropriate measures to prevent or punish irregularities committed within their territories.

#### **Article 42: Cooperation and information**

Article 42 requires the home and host supervisory authorities to cooperate closely in the supervision of the activities of a bank and its branches, and to exchange all the information that is necessary for effective supervision:

*The competent authorities of the Member States concerned shall collaborate closely in order to supervise the activities of credit institutions operating, in particular through a branch, in one or more Member States other than that in which their head offices are situated. They shall supply one another with all information concerning the management and ownership of such credit institutions that is likely to facilitate their supervision and the examination of the conditions for their authorisation, and all information likely to facilitate the monitoring of such institutions, in particular with regard to liquidity, solvency, deposit guarantees, the limiting of large exposures, administrative and accounting procedures and internal control mechanisms.*

The Commission Services consider that the requirement for regulators to exchange information under this Article should not be interpreted narrowly. A wide interpretation is necessary to ensure that the provisions cited above which allocate responsibilities and powers to competent authorities have their intended effect. As Article 42 makes clear, home and host supervisors must provide each other with (i) all the information that is likely to facilitate the proper exercise of the supervisory responsibilities allocated to them by the CRD, and (ii) all information likely to facilitate the monitoring of credit institutions and their branches both generally and with regard to the particular regulatory aspects that are specified.

Accordingly, the information that is required to be exchanged between home and host supervisors under Article 42 is not limited to information on those areas where host supervisors have prudential responsibilities (i.e. liquidity supervision).<sup>3</sup> In order for the provisions on supervisory intervention by the host State, and in particular Article 33 on 'emergency' intervention, to have their intended effect, host State authorities should receive the full range of information that they need to assess the regulatory compliance of credit institutions that have branches in their State, and risks to interest of their domestic depositors, investors and others that receive services from those institutions.

Moreover, the Commission Services take the view that the scope of the information covered by the requirement in Article 42 should not be restricted by any distinction between information that is 'essential' and that which is merely 'relevant' to the supervisory tasks and powers mentioned in that Article. It is true that this distinction is made in Article 132 in the context of the supervision of subsidiaries, to distinguish between information that must be exchanged automatically and this which must be provided on request. Article 42 does not

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<sup>3</sup> In this regard, it is worth stressing that the liquidity of a branch will be difficult to address in isolation. The financial soundness of a credit institution directly impacts liquidity positions, including those of its branches.

of information between the home and host supervisors concerned with the supervision of a particular institution are legal requirements under Article 42. In terms of application, this means that home State authorities must provide the host State supervisor with any information which, in the assessment of the host supervisor, "*is likely to facilitate the monitoring of such institutions*".

## 2. ADVICE REQUESTED

Taking into account the need to ensure that home and host supervisors have all the information necessary to enable them to perform their supervisory responsibilities and exercise their powers of intervention in a timely and effective manner, CEBS is kindly requested to provide advice on the following questions.

1. The categories of information that are covered by the requirement to exchange information under Article 42.

If possible, it would be helpful if CEBS could compile a list of the information that "is likely to facilitate the monitoring", by home and host State authorities, of credit institutions that operate in other Member States through a branch or branches. We appreciate that it may not be possible to provide a comprehensive list, since specific information requirements may vary according to the particular circumstances of the individual case, but would ask that the indicative list should be as full as possible to reduce to a minimum any uncertainty or disagreement among supervisors about what information can be expected under this provision.

2. Any distinction between information required by the home and by the host supervisors.

Article 42 requires the flow of information in both directions: from home to host supervisor, and from host to home. CEBS is therefore asked to specify (i) the information that the host should supply to the home authority for the purposes of its supervisory activities, and (ii) the information that the home should apply to the host authority to enable it to carry out its particular supervisory responsibilities and powers in relation to branches, if there is any difference between the two categories.

## 3. TIMING

You are aware of the urgency of these questions for the work of the Commission and the EBC on the supervision of branches and on early intervention measures, and have kindly agreed to provide the advice in an accelerated time frame. We should be grateful if CEBS could provide a final response to the questions specified above by Friday 15<sup>th</sup> May. However, we would also invite CEBS to use best endeavours to provide us with its preliminary views on these questions by the end of April if that is possible. The advice on the scope of Article 42 is needed for the purposes of the Commission's White Paper on crisis intervention which is scheduled for publication in June, as well as for the further deliberations on supervision and intervention in the June meeting of the EBC. The cooperation of CEBS in working to a very tight deadline is much appreciated.

#### 4. ANTICIPATION OF AMENDMENTS TO CRD

Finally, it was also agreed at the EBC meeting of 5<sup>th</sup> March that CEBS should anticipate some of the amendments to the CRD concerning cooperation between supervisors of credit institutions with branches that are currently being concluded by the European Parliament and the Council.

Article 42a, if adopted, will enhance the cooperative framework between home and host regulators in respect of 'significant' branches. Paragraph (2) of that new Article will home State supervisors to provide the host supervisors of significant branches with information concerning any adverse developments in the credit institution concerned or in other members of the consolidated group and major sanctions and exceptional measures taken in relation to that institution. The proposed amendments will also enable, in appropriate cases, the participation of supervisors of significant branches in meetings of the supervisory colleges for the relevant institution.

This letter also constitutes a formal request to CEBS to anticipate, to the extent possible, the changes to the CRD by the end of 2009, so as to identify the host regulators of significant branches, and to include them in the relevant colleges that have been established by that date. Similarly, CEBS is requested to arrange for early effect to be given as far as possible to the enhanced information requirements in proposed Article 42a, so that host supervisors of significant branches receive information about adverse developments in relation the bank (such as a deterioration of the bank's capital position) which could seriously affect that institution, and about any major sanctions and exceptional measures that may have been imposed.

These measures should reinforce the supervisory framework at this critical time. Importantly, they will increase the confidence of host authorities that they have access to all the information necessary to enable them to carry on effective branch supervision in accordance with the Directive, and that risks to depositors and investors, or to financial stability generally, will be brought to their attention at a sufficiently early stage to facilitate effective intervention.

I am therefore very grateful for your support in giving early effect to these measures, and look forward to continuing productive collaboration between CEBS and the Commission Services.

Yours sincerely,



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