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BANCAIRE  
FRANCAISE

The Deputy Director General

Paris, 17 July 2008

**Public consultation on CEBS technical advice to the European Commission  
on liquidity risk management.**

Dear Madam,

The French Banking Federation (FBF) welcomes the opportunity to comment on the CEBS advice to the European Commission on Liquidity Risk Management and Supervision.

The recommendations of CEBS detail the fundamental principles that the Basel Committee is currently reviewing and propose concrete measures to improve the management of liquidity in banking groups. They take into account the consequences of the financial turmoil that we have been experiencing for nearly a year. Besides, they build upon the work done by the industry, particularly the IIF in its March 2007 report on the principles of risk liquidity management.

Generally speaking, we support the recommendations contained in the advice of CEBS. They highlight the best practices that should govern liquidity risk management in banking groups. Moreover, we appreciate that CEBS proposes relying on internal methodologies developed by banking groups in order to ensure prudential supervision of liquidity risk.

From our point of view, it could be useful to devise some points that are not clear enough, and that we will comment in the attached document.

However, we regret that the proposals of CEBS do not go far enough and do not mention the objective of establishing a common European framework for liquidity risk management and supervision. Furthermore, the issue of supervision of the liquidity position of national or cross border groups as well as foreign subsidiaries would be improved if it was developed with a greater emphasis towards consolidated supervision which fits the way banking groups manage their liquidity.

**Mrs Kerstin af Jochnick  
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The French Banking Federation is committed to building a level playing field in Europe that, we believe appropriate regulation can contribute to create. FBF remains at the Committee of European Supervisors disposal for any further discussion on these issues.

Yours faithfully,

A handwritten signature in black ink, appearing to read 'Lauzun', with a stylized flourish at the end.

Pierre de Lauzun

## Comments of the French Banking Federation

We are pleased to note that the CEBS, after having contributed to the implementation of the Basel II accord on capital requirements, has taken initiatives to propose guidelines and recommendations to improve liquidity risk management and supervision of European banks. CEBS after careful consideration has decided to take into account the consequences of the current market turmoil that has highlighted the importance liquidity risk.

The proposals of CEBS are in line with those of the Basel Committee which is reviewing the broad principles of risk management of liquidity. They examine and describe concrete measures to improve the management of liquidity by promoting internationally accepted standards and best practices. Besides, European supervisors build upon the work already done by the industry, particularly through the March 2007 International Institute Finance report on the principles of liquidity risk management, which report French banks actively took part in.

French banks support the efforts of CEBS to improve the management and supervision of liquidity risk and underline the excellent work done.

As cross-border banks need to be able to manage their liquidity on a group wide basis, the level of the prudential supervision set in the proposals does not seem to be clear enough for us. It could force banks to manage their liquidity with two regulatory sets of rules (consolidated and solo) even for subsidiaries located in the same country. We are pleased to note that CEBS has left each banking group free to organize LRM (centralized or decentralized, management intra-day or long-term funding). However, supervisory requirements should not lead to question this principle within a country or for cross-border banking groups even if the issue of free transfer of assets exists.

In fact, an increasing number of banking groups manage their liquidity on a group wide basis. Local supervisors will keep the right to impose local requirements even if specific exemptions are provided for and if internal methodologies are used by the consolidated supervisor to monitor LRM. We believe that the CEBS recommendations should focus more clearly on consolidated supervision that fits the way banks manage their liquidity. We believe this is more in line with principle 6 of the document of the Basel Committee on Banking Supervision on liquidity.

It seems necessary for us to distinguish more clearly between banks under the standard approach and those relying on internal methodologies as supervisory tools to assess the level of liquidity required. Regarding the last ones, the question is how will buffers be calculated? Our understanding, to be confirmed, is that the level of liquidity buffers will depend on the results of the stress tests. For institutions using the standard approach, if the underlying stress scenario is already including liquidity buffers the supervisor won't need to require additional buffers.

In general, we support the recommendations contained in CEBS document. Nevertheless, it might be useful to specify or propose another wording for some recommendations which do not seem to be clear enough in our point of view.

**RECOMMENDATION 1:** Depending on the organizational structure, the board of directors or the executive committee will be responsible for defining strategies and policies for managing liquidity risk. In any case, the board of directors will be informed of the decisions taken by the executive committee (cf. Principle 3 of the BCBS document and footnote 4 on page 7).

**RECOMMENDATION 3:** French banks agree to segregate clearly operational and monitoring functions. As specified, it has to be done according to the organizational structure of the banking group.

**RECOMMENDATION 5:** ALM services are increasingly using front office tools to measure liquidity risk and prepare their reportings. The need of a necessary reconciliation with accounting is often difficult. Liquidity risk could be partly monitored with front office tools, and not with accounting tools as it is currently. The ALM function should not develop its own tools if they already exist in the bank.

**RECOMMENDATIONS 7 & 8 :** French banks agree on the recommendations even though they are difficult to implement in practice. It is very tough to manage particular clauses such as covenants within the IT system to reduce the documentation risk.

**RECOMMENDATION 11 :** This recommendation raises a strong concern from French banks as it would force them to manage their intra-day liquidity on a gross basis whereas many payment and settlement systems are working on net basis (eg TARGET 2). This change from the current situation would increase costs.

**RECOMMENDATION 14 :** French banks are in favor of stress tests as wide as possible from which they should draw the consequences to adjust their internal policies and contingency plans. They are ready to do their best in order to improve the quality of these tests and would deem useful that the national supervisor harmonizes the types of scenarios they could work with.

**RECOMMENDATION 16 :** Liquidity buffers must be gauged by an institution to enable it to resist for a period of survival without requiring changes to its business model. Without changing fundamentally their business model, institutions must remain free to adjust or modify their lending and financial policies in stressed time. It's up to every firm to adapt itself to the circumstances. The length of the survival period should be specified and fitted each institution. Supervisors should check the harmonization of periods of survival chosen by institutions having similar risk profile and business model.

**RECOMMENDATION 18 :** French banks are not opposed to disclose information on their liquidity risk management. Nevertheless, they wish to draw attention to the risks that may create such disclosures. Extensive disclosures are very sensitive and may be misunderstood by market participants. They might have devastating consequences on the integrity and stability of the market and might jeopardize the liquidity position of an institution. Inappropriate disclosures could be at odds with the objective of mastering liquidity risk. Moreover, if IFRS 7 only applies to consolidated accounts, there is no use for extending these disclosures to individual or sub-consolidated levels. In the end, French banks are in favor of a more complete dialogue with supervisors but they are against increasing the volume of quantitative information disclosed to the markets.

**RECOMMENDATION 25 :** We have noted with satisfaction that the supervisors could accept to rely on internal methodologies as supervisory tools. We appreciate that the recommendations of the supervisors remains principle based and thus allow every bank to use its own methodology

methodologies to satisfy supervisory reporting needs.

**RECOMMENDATION 29** : French banks encourage supervisors to increase and promote exemptions for foreign subsidiaries and to include them in the legal text in a more formal way. They are in favor of close coordination between supervisors regarding liquidity issues. They insist upon the central part that the consolidating supervisor should play in the college to supervise liquidity risk at the consolidated level and for the different entities of the group.

Finally, we regret that the proposals of CEBS do not go far enough and do not mention the creation of a European common framework for LRM. We are aware that legal obstacles exist, but, in the case of capital requirements, authorities were able to overcome them and it is a pity that, regarding liquidity, they could not achieve the same result. We also regret that their recommendations do not advocate for the implementation of a homogenous regulation within every state of the European Union. The CEBS recommendations will create a unlevel playing field between European banks established in different European countries. This will result in multiple constraints for cross-border firms requiring them to retain trapped pockets of liquidity in some entities and will increase regulatory burden through a duplication of tasks. Moreover, to insure a level playing field in Europe, it would seem appropriate that the regulatory constraints lead to the same level of requirements implying equivalent liquidity costs throughout Europe for institutions having the same risk profile. This requires a better harmonization in the national rules applied to the calculation of liquidity ratios.

**Large exposures:** The responses of banks to the consultation of the European Commission on the CRD potential changes clearly highlighted industry concerns about the proposed rules for interbank exposures. The proposals are going to create serious issues regarding liquidity risk management, especially for banks managing liquidity in a centralized way. French banks would like the Commission to review its proposal to lower the riskweight of interbank exposures. The Commission cannot maintain its proposal of a 100% riskweight for the first euro and from the first day on. It requires appropriate impact studies (cost, liquidity and contingency plans in a more severe regulatory framework) before passing changes in the CRD.