



Arnoud Vossen
Secretary General
CEBS
Tower 42 (Level 18)
25 Old Broad Street
London EC2N 1HQ

9 July 2010

Deutsche Bank AG
Winchester House
1 Great Winchester Street
London EC2N 2DB

Tel: +44 20 7545 8000

Direct Tel +44 20 7545 7471
Direct Fax +44 20 7547 4179

Dear Mr Vossen,

Consultation paper on CEBS's Guidelines for the joint assessment of the elements covered by the Supervisory Review and Evaluation Process (SREP) and the joint decision regarding the capital adequacy of cross border groups (CP39)

Deutsche Bank (DB) welcomes the opportunity to respond to CP39. We broadly support the guidelines as set out in the consultation paper and are encouraged to see a standardised framework developed for joint assessments and decisions. DB strongly supports a move towards supervisory colleges having a concrete decision making role. There is still significant progress needed to achieve this and CP39 is an important step in the right direction. It is crucial that the joint assessment and decision are binding on members of the supervisory college and form the basis for on-site inspections.

While CP 39 provides for a theoretically sound framework, we are concerned that it will be challenging to ensure the guidelines are followed in practice. The EBA must take a strong role in that regard, and in monitoring consistency in how different banking groups are treated.

Common templates and scoring scales are a practical tool to improve the communication process between supervisors and banks. It is a matter of practicality that feedback and ongoing dialogue should be explicitly built into the guidelines. However, the CP includes little mention of the role of the banking group in the joint assessment process. A robust dialogue with senior management and technical staff is essential to explain the reasoning behind the template and rating system. There should be an explicit requirement in the guidelines for all results to be shared with the bank so that feedback can be taken into account. It is the only way to ensure that the assessment is based on a shared understanding of the business model, strategy and risk management of the group. A lack of effective feedback to the group on supervisory outcomes has made it difficult in the past for the institution to facilitate the joint assessment efficiently.

DB's response to CP34 gives a detailed view of our position on supervisory colleges. There is a certain degree of overlap between the two consultation papers. It is worth emphasising key themes in relation to joint assessment and decisions:



- As outlined in the CP, the consolidating supervisor must play a central role. We believe that the approach should be top-down with the consolidating supervisor providing the first assessment and then taking host country feedback into account in a second step.
- Participants in the assessment process must have sufficient seniority and authority to act on behalf of their organisation.
- Third country supervisors of major jurisdictions should be included in the joint work for it to be relevant. More emphasis on this principle in the guidelines would be welcome.

More specific comments on the draft guidelines are attached.

Yours sincerely

A handwritten signature in blue ink, appearing to be 'A. Procter'.

Andrew Procter
Global Head of Government & Regulatory Affairs
Deutsche Bank AG



General Comments

The following high level issues should be taken into consideration when redrafting the guidelines:

- The reference in a number of areas of the paper to alternative supervisory tools is welcome. We are concerned that there is an overemphasis at the moment on capital and liquidity requirements as the only means of addressing deficiencies. This point should be highlighted more clearly in the paper and should come before text around the determination of capital add-ons.
- In order for the decision-making process in the college to work efficiently, meetings should be structured by the consolidating supervisor with a clear thematic agenda based on the initial group assessment. This has not been the case to date.
- Requiring the lead/consolidating supervisor to provide a group overview upfront would minimise host supervisory requests for information on group processes and methodologies and reduce the workload for all parties. Such a structured approach would help to give host supervisors the necessary comfort on group diversification and non-local hedging, and would reduce the potential for disputes and subsequent delays.
- There is currently a mismatch between the materiality of entities and the ICAAP approach taken by host supervisors. It is essential that the group approach to ICAAP by the consolidating supervisor take precedence. Host supervisors should be guided by clear principles of proportionality in feeding their approach into the consolidating supervisor.
- A “one size fits all” approach should be avoided. When identifying required outcomes, banks and their supervisors should have sufficient flexibility to be able to tailor mutually agreed solutions. In this context, it is important to recognise that a global group will allocate capital along business lines rather than jurisdictional lines or on a legal entity basis.
- The assessment of solvency of legal entities needs to adequately take account of solvency at a group level. An isolated assessment that does not take account of the support provided by the parent to the legal entity (capital, liquidity, management, and infrastructure) would inevitably lead to inappropriate results and supervisory outcomes. Joint assessments should prevent such isolated assessments taking place.
- The remittance dates and frequency of ICAAP submissions should be effectively coordinated. This is not currently clear in Chapter 2 of the CP.

Detailed comments

- **Additional levels of capital: Guideline 22.** At the Public Hearing on 3 June, CEBS pointed out that, where additional levels of capital above the Pillar 1 requirements were to be imposed, there should be an emphasis on loss absorbing Tier 1 instruments. We firmly believe that hybrids and contingent capital should be included as loss absorbing Tier 1 instruments (pending further harmonisation in the definition of capital at EU level and work in the Basel Committee on contingent capital).



- The investor base for bank equity will not be sufficient given the levels that will need to be raised in the coming years (estimated at €700 billion by McKinsey). Banks need investments such as hybrids which attract investor groups other than equity investors. DB supports a material position for hybrids including contingent capital at 20% of Tier 1.
- Contingent capital is one of the most important tools to quickly restore Equity Tier 1 capital and Additional Tier 1 capital in stressed situations, to mitigate procyclicality and ensure survival. In order to ensure a sizeable market for contingent capital instruments, banks will need some flexibility in tailoring instruments, including triggers which we believe should include some level of management discretion. In this context, we would also emphasise the importance of existing contingent capital instruments and the subordinated debt market.
- **Liquidity requirements: Guideline 3, Element 5, paragraph 54.** Global cross-border firms currently face a multitude of similar but distinct liquidity reporting requirements. Colleges could be instrumental in eliminating multiple liquidity reports by commonly selecting one set of relevant liquidity data requirements for individual cross-border banks and jointly monitoring and sharing these with other college members.
- There should be an explicit reference in the CP to the CEBS guidelines on the Liquidity Identity Card published in June 2009. Our understanding was that by implementing this Liquidity ID Card, liquidity related reporting for supervisory purposes would be harmonised as far as possible. Supervisors in their colleges should agree on a common format and data set for a bank.
- Based on historical evidence over the last two years (i.e. since the crisis started and liquidity risk moved up the agenda), we have not seen any meaningful harmonisation or coordination of regulatory information requirements in respect of liquidity risk.
- **Stress testing:** CP39 should not duplicate the guidelines of either CP31 or CP32. A reference to other CPs is welcome but should be sufficiently generic so that any change to other CPs would not materially impact CP39. It would be sufficient to refer to CP 32 and require institutions to assess their entire stress testing programme against the criteria laid out in those guidelines.
- **Guideline 9.** An explicit requirement to carry out capital planning stress tests is unnecessary. We also pointed out in our response to CP32 that capital planning stress tests should not be used to assess capital buffers, either on a group or subsidiary level.
- We suggest rephrasing **Guideline 9** as a general stress testing guideline without particular reference to capital planning: ***“The college members should discuss the adequacy of the stress testing programme and its integration into the risk management system. The stress testing programme should be proportional to the risks in the respective (sub-) portfolio. The evaluation of the stress testing programme has to consider risk management processes on the local and global level.”***
- **Guideline 19.** There are existing rules regarding the calculation of own funds and the outcome of stress testing on its own is not meaningful when deciding on capital adequacy. We refer to our response to CP 32.



- The proposal to allow for an additional macroeconomic stress test under **paragraph 116** should be treated with caution. This should be the exception rather than common practice. There is already considerable strain on resources between the internal stress testing process mandated by the banks management, and often conflicting external stress testing requirements. The increasing pressure on resources in this area will inevitably reduce the quality of output.
- **Paragraph 117** should be deleted as this should be covered in CP 32.
- **Local capital requirements: Guideline 18, paragraph 113c** refers to the allocated capital, net of group diversification benefits. Isolating the group diversification benefit from internal capital requires standalone Economic Capital models. To build these would be extremely burdensome for global institutions, and it would be practically impossible to calibrate local models to a satisfactory level of quality (e.g., for Market Risk and Operational Risk).
- Non-recognition of hedges for local legal entities by host supervisors is a key concern as the institution could potentially be over hedged. This may lead to conflicting risk management actions being taken on a home and host basis.
- **“Living Wills”**: **Guideline 3, Element 1, paragraphs 31 and 32** touch on the group legal and functional structure. It is not clear here whether the intention is to address the current debate around “living wills”. It is essential that global cross-border groups are not confronted with a variety of local standards and requirements in this area. A variety of local “living wills” uncoordinated with a group’s “living will” which is managed on a centralised basis would be unmanageable.
- **Business models: Guideline 3, Element 4, paragraph 46** talks about the appropriateness of the organisational structure in relation to the business model. Although it is clear that the intention here is not to interfere in the business model itself, it is a fine distinction. It will be essential for the EBA to ensure that no college strays into a discussion of the business model which is a purely commercial issue and should not be subject to any form of supervisory mandated change.