

**AECM Position Paper:**  
**CEBS Consultation paper on Implementation of Guidelines**  
**regarding instruments referred to in Article 57 (a) of Directive**  
**2006/48/EC recast**

Brussels, 30<sup>th</sup> March

**General Comments:**

AECM, the European Association of Mutual Guarantee Societies, is pleased to be able to provide CEBS with its position regarding its Consultation paper on the implementation of guidelines regarding instruments referred to in Article 57 (a) of Directive 2006/48/EC recast.

AECM's position takes place in the context of the general review of the Basel II framework and according revision of the Capital Requirements Directive, for which the 16 April has been set as deadline for comments. AECM will also comment separately to these two consultations.

AECM's Member organizations are mutual or cooperative entities, as well as public institutions, providing credit default guarantees for SMEs, who for lack of sufficient collateral could not otherwise access bank loans. According to provisional figures the **total volume of new guarantees issued in 2009**, AECM members issued over 853.000 guarantees with a value of over € 33 billion over the year. On 31<sup>st</sup> December 2009, AECM members held in their portfolios more than 2 million guarantees for a value of **€ 70 billion** to over **1,8 million customers**, which represent about 8% of all SMEs in the European Union; in some countries (for example in Italy) this percentage is even higher (about 25%). This underlines the important contribution guarantee societies have made to fostering SME access to credit.

AECM underlines that in many countries guarantee societies have a wide range of qualitative information about SMEs. This can supplement the evaluation of the bank, which is usually mostly based on the balance sheets of the loan beneficiary, and so to enhance the rating of the SMEs.

**Specific comments:**

Guarantee societies dispose of own funds, which are provided either by their shareholders (State, banks, industry associations, companies) or by the beneficiaries of the loans that they guarantee (companies).

These funds are either joint common stock shares, normally admitted in core Tier 1 capital, or cooperative and mutual shares, whose treatment under the current CRD status has been unclear hitherto and handled differently by supervisory authorities in the respective Member States.

The most common forms of shares issued by cooperative or mutual societies are on one hand the shares issued by cooperative or mutual societies underwritten by the beneficiary companies themselves and on the other hand certain forms of mutual guarantee funds paid in by the same companies or the shareholders.

They have specific features: the subscription of cooperative or mutual shares by the beneficiary is directly linked to the issuance of the guarantee as well as the proper execution of the loan obligations and the termination of the credit agreement; their reimbursement is also subject to the withdrawal of the beneficiary from the guarantee society. The individual paid in shares directly cover the corresponding individual loan guarantee commitments. These shares cannot be compared to shares issued by cooperative banks, which do not directly cover the individual assets, i.e. loans risks, of the bank. Rather, in the case of the cooperative banks, the capital ensures the institutions overall solvency.

The mutual guarantee funds paid in by the shareholders or beneficiary companies work the same way: they are paid in directly as the individual guarantee is issued and they cannot be reimbursed for the duration of the loan; moreover these funds cover the asset side of the guarantee society. They are in no way to be equated to normal deposits of banks, which the depositant may ask for back at whatever time.

These shares represent the most important item to determine the volume of guarantees they may issue both shares and mutual funds represent the most important item to determine the volume of guarantees they may issue (or grant).

Taking into consideration that they are directly linked to individual loan operations and that they are subject to strict reimbursement rules regarding the loan covered, other assets, liquidity situation, and that they involve the withdrawal of the beneficiary from the guarantee society, they should be treated as Tier 1 capital.

In this context, AECM welcomes the clarification as to their recognition as Tier 1 capital in CEBS CP33 consultation paper. In our view, the 10 criteria listed as guidelines for the interpretation of Article 57 (a), in particular as regards the conditions to be fulfilled by cooperative or mutual shares to be considered as own funds instruments are generally measured and adequate.

However, there is one comment to be made regarding the conditionality of redemption of cooperative and mutual shares (Criterion 4, page 11). The CP33 states that the owner of the instrument shall not have a put option or any other right to require unconditional redemption. In some countries, the holder does have a redemption right for his cooperative share, however only:

- after the specific guarantee for which the share has been issued has come to term
- at face value
- after deduction of pro-rata losses
- with no rights to reserves and/or dividends
- after the holder has required and has got the withdrawal from the guarantee society.

As explained above, the share is therefore directly linked to a specific financial asset's risk. Therefore, this case would warrant recognition of this type of own funds instrument, since it is directly and fully loss-absorbant for the time of the existence of the specific underlying risk over the time of its existence.

Furthermore we attract CEBS attention to the fact that in some countries, the shareholder of a limited company has the right to leave the company by a formal cancellation of the company with a perennial period of termination. In practice, the remaining shareholders decide the continuation of the company and have the option to take over the stake or not. We are convinced that this right of a shareholder of cancelling a limited company is no case of redemption or buy-back in the meaning of Criterion 4 or 5 (page 11 and 12), even if the share have to be assigned to another shareholder or a third party or have to be in case of need collected by the company.

The other provisions and interpretation in the case of cooperatives and mutuals as regards in particular the conditionality of redemption rights and pari passu treatment of loss absorbency corresponds to the legal and operational reality of our cooperative and mutual members.

AECM also encourages the Basel Committee and the European Commission to take the specific treatment of cooperative and mutual shares, proposed by CEBS, into consideration for their on-going work on the review of the Basel own funds regulatory framework as well as of the CRD.