From: **The European Mortgage Federation**

Issue: Position Paper on CEBS Consultation on supervisory Review Process

To: **Committee of European Banking Supervisors**

Summary: Overall, the EMF welcomes the opportunity to comment on the practical aspects of implementing a workable and effective Pillar 2 regime across Europe. We welcome also the high level principles set out in the consultation document, in particular the concept of proportionality, but we would stress that Pillar 2 should not automatically result in an increased capital requirement to the credit and operational risk requirement under Pillar 1. Moreover supervisors should, where practicable make use of the full range of tools at their disposal, not just a capital surcharge.

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EUROPEAN MORTGAGE FEDERATION POSITION PAPER ON THE APPLICATION OF THE SUPERVISORY REVIEW PROCESS UNDER PILLAR 2

General Comments

1. The EMF very much appreciates the opportunity to comment on the CEBS paper on the application of the Supervisory Review Process under Pillar 2, however we feel the paper could have more usefully been issued following the publication of the Basel and Brussels documents.

2. The European Mortgage Federation agrees with the high level principles set out for the supervisory review process (SRP), but would emphasise that the SRP should not automatically result in additional capital requirements or in prudential measures being imposed on institutions. A clear additional risk should be identified, such that institutions which are well managed and have sufficient capital to cover their regulatory requirements under pillar one should face not further surcharge.

3. Additionally increased capital requirements should not be the sole tool used by supervisors to address Pillar 2 risks. A requirement for a mitigating measure or a change to an institutions risk and controls system could equally serve to reduce the level of risk. Increasing an institutions capital requirement would simply negate the risk rather than reduce it.

Consolidation

4. In the context of the FSAP discussions, it is important that wherever possible the RCD is implemented consistently and transparently. It is therefore important for European supervisors to develop coordinated and practical approaches to supervision whilst at the same time not imposing too heavy a burden on financial institutions. EMF believes that a consistent approach will only be obtained through supervision applied at the consolidated group level and with a coordinating lead supervisor. The EMF believes that any other approach would be difficult to implement practically, would place an unnecessary regulatory burden on the industry, would not serve the aims of convergence and the FSAP, and would, most importantly, not result in an accurate measurement of the risks faced by an institution at the group level.

Concept of Proportionality

5. EMF welcomes the concept of proportionality for both the ICAAP and SREP, and agrees with the further detail provided on this subject in Internal Capital

Adequacy Assessment Process (ICAAP) high level principle III (a).

ICAAP Review Period

6. Reviewing ICAAP on an annual basis should not be a mandatory requirement. A flexible, well developed system put in place in a low risk institution may not require an annual review. The review period should be determined by the supervisor in line with the institutions risk profile. This would embody High Level Principle VII making ICAAP risk based.

List of Risk Factors

7. The European Mortgage Federation believes that the risks and controls enumerated in annex 1 should not be presented as an exhaustive list for supervisors to check off when going through the Supervisory Review and Evaluation Process (SERP). Many of the risks listed overlap with each other and will be difficult to assess independently. In addition this categorization is likely to conflict with the institutions categorization of the risks in its ICAAP. ICAAP High Level Principle VIII (b) clearly states that there is 'no standard categorization of risk types'.

Risk Correlation

8. The EMF welcomes ICAAP High Level Principle VIII (g) which we interpret as allowing portfolio effects between different risks, and avoid double counting of certain types of risk.

Trigger-Target Capital Requirements

9. Further discussion of the Basel Committee principle 3 could usefully take place, specifically looking into how it would be applied. Under the proposed new regime, credit and operational risk would result in a capital requirement which can then be augmented under pillar by the supervisor, however under principle 3 a further buffer is then required above the minimum capital requirement. Further discussion of the trigger and target system should take place to ensure consistency of application, as well as to preserve the transparency of the capital requirement calculation.