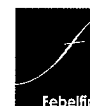
BELGIAN FINANCIAL SECTOR FEDERATION



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Mrs Kerstin af Jochnick
Chair
CEBS
Committee of European Banking Supervisors
Floor 18, Tower 42
25, Old Broad Street
London EC2N 1HQ

Brussels, 19 February 2008

By e-mail: cp16@c-ebs.org

Dear Mrs af Jochnick,

Large Exposures (CP16) : comment of Febelfin

Febelfin, i.e. the Federation which regroups four trade associations from the Belgian financial industry[1], welcomes the opportunity to express its views on the consultation paper mentioned above. The following remarks are communicated subject to the final decision to be taken by our Board on this matter on 22nd February 2008.

Generally speaking, we support the CEBS point of view on the Large Exposures (LE) regime being a backstop scheme. Consequently, we propose to keep this regime principles-based and fully consistent with the Pillar II requirements on concentration risk. For the purpose of allowing institutions to use the same systems and of simplifying data comparison, we would like to advocate a full convergence (e.g. in the field of exposure valuation, collateral eligibility and valuation) between the minimum capital requirements and the LE regime. To the extent some articles in the Capital Requirements Directive (CRD) would be considered inappropriate for Large Exposures, then both the CRD and the LE regime would in our view have to be adopted or modified to ensure that a single set of rules will continue to apply.

In accordance with our general approach on prudential supervision, we are furthermore of the opinion that the consolidated level is the appropriate level for a follow-up of large exposures. After all, a default by a large counterparty could damage a banking group, regardless where the credits may have been booked.

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[1] The following trade associations are part of Febelfin: the Belgian Bankers' and Stockbroking Firms'Association (ABB/BVB); the Professional Association of Credit Providers (UPC/BVK); the Belgian Association of Asset Managers (BEAMA); the Belgian Leasing Association (BLA).

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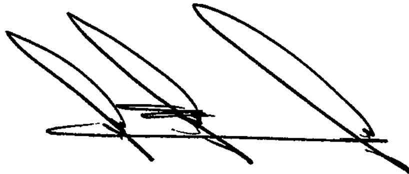
Febelfin

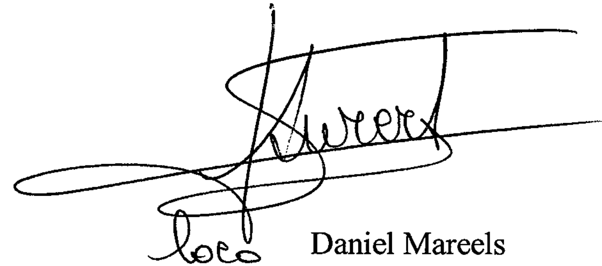
Intra-group exposures and short-term interbank exposures should furthermore in our view be exempt from the LE regime. As for the latter, we are also of the opinion that interbank markets have a credit and liquidity providing function which might be different by nature and such characteristics ought to be taken into account.

Finally, we would like to mention that the LE regime, in our opinion, is not the appropriate prudential instrument for necessarily bringing a solution to the problems caused by the liquidity crisis. We strongly would like this aspect to be dealt with within other frameworks such as liquidity management, crisis management, burden sharing, etc

We hope our remarks might get be taken into account. We are and remain evidently at your disposition for further questions and comments you may have.

Yours sincerely,





Michel Vermaerke
Chief Executive Officer

loco Daniel Mareels
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Enc.

cc. David Wright, Deputy Director General, DG Internal Market, European Commission.

J-P. Servais, Chairman of the Banking, Finance and Insurance Commission.

Large Exposures CP16, comment of Febelfin

Febelfin, i.e. the Federation which regroups four trade associations from the Belgian financial industry[1], welcomes the opportunity to express its views on the consultation paper mentioned above. The following remarks are communicated with reservation to the decision to be taken by our Board on these matters on 22nd February 2008.

1. General comments

We understand that regulators are now willing to use all the tools available to increase the resistance of the market against liquidity crises similar to the one we saw in the wake of the subprime crisis. We have noticed that this state of mind clearly has left its marks in the paper on large exposures. However, we are not convinced that the large exposures regulation is an appropriate solution for sheltering the market against this type of liquidity crisis and so, we do not support this approach. In our comment, we have given special attention to liquidity issues in our response as for the treatment of intragroup exposures and interbank exposures.

1.1. Large exposures (LE) regime vs. concentration risk

- We fully share CEBS' vision on the LE regime as a safety net or backstop scheme. We understand that supervisors need a supervisor-driven backstop scheme or safety net, as large exposures are widely being recognised as a source of potentially high systemic risks. However, the LE system in itself still must be principles-based and fully consistent with the Pillar II requirements on concentration risk. More importantly, it must not replace nor duplicate the concentration risk regime.
- Large exposures concern concentration on a credit counterparty (single name or connected names). The concentration risk on the other hand covers concentration on a credit counterparty but also goes beyond. It has a much broader scope : concentration on segments, countries, products, collaterals, etc.
- We notice that the concentration risk regime is the institution's own responsibility and a process proper to the institution. This system also is the primary tool for managing credit risk concentration. At least for large banks, the system is more sophisticated, more granular and more embedded in the bank's risk management. Last but not least, it

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is one of the key elements of the ICAAP, SREP and the dialogue between bank and supervisors.

1.2. Level of application

- The consolidated level is generally being recognized as the appropriate level for the follow-up of large exposures. The failure of a counterparty - large exposure could damage a banking group, no matter where the credits are booked and consequently can cause systemic damage.
  The recent financial turmoil has proven that the stand-alone level of the legal entities does not reflect the real risks and does not allow to take corrective measures in due time.
- At least in those cases where the bank is organized so as to take care of the follow-up of the risk on a credit counterparty at group level, the primary level of application of LE is the consolidated level.
- Although we agree that the Capital Requirements Directive also applies on an individual basis, we think that centrally organized institutions should be exempt of the stand-alone level, provided they have proven to their consolidating supervisor that the appropriate policies (such as risk policy, capital policy, contingency plans) and processes are in place.

1.3. Full convergence between LE and minimum capital requirements (better regulation)

- The LE regime should be fully integrated in and form part of the CRD.
- As the concentration risk regime is the major tool for concentration risk management, including large exposures, the backstop regime for LE should be simple, comparable and applicable to all institutions (from small local institutions or niche players to large cross-border banks).
- We strongly advocate the use of one single set of rules. The backstop system should be simple and complementary to the CRD, i.e. based on the same rules and methodologies as the CRD. The institutions would welcome further convergence between minimum capital requirements (Pillar 1) and the LE regime in the field of exposure valuation, collateral eligibility and valuation. This would allow them to use the same systems and make it easier to compare data, whereas different measures may throw the market into confusion. Despite any theoretical arguments in favour of differentiated treatments, in practice, the additional cost involved would be too high. If some of the articles in the Capital Requirements Directive are considered to be inappropriate for large exposures, then both the CRD and LE will have to be changed together to ensure that the single set of rules is maintained.
- We strongly oppose the use of national options or discretions. We advocate the use of one single LE regime without national goldplating, divergent interpretation or implementation. Furthermore, CEBS' proposal should not be built upon national discretions that are to be left out.
- There should be no duplication with the concentration risk regime, such as for instance duplication of reporting on the same risks.

- We also propose to reduce the administrative burden for institutions which have enough capital to make sure that the LE limits will be taken into account.

1.4. Scope

- The scope should be strictly in line with the purpose, i.e. providing a backstop or safety net.
  - The LE regime must not be seen as an opportunity for renegotiating the current Capital Requirements Directive. In our opinion, a better regulation principle would be that institutions can use one system for calculating normal and large exposures. Only when the provisions of the Capital Requirements Directive do not seem to be appropriate for the calculation of large exposures, will both the CRD and LE have to be changed.
  - The LE regime must not be a remedy for the problems an ailing institution is confronted with, for these are part of other domains such as capital and liquidity management, crisis management; burden sharing, etc.

1.5. Transitional measures

- A transitional period is necessary, so as to offer the institutions enough time to adapt to the new regulations.

2. Detailed comments

CHAPTER 1 : KEY FINDINGS IN PART 1

Q1 : CEBS would welcome respondent's views on the high level impact assessment of the policy options

- The relationship between the LE regime, as a supervisor-driven backstop, and the institution-driven concentration risk regime should be made clearer.
- The shortcomings of the concentration risk regime which justify the introduction of an extensive LE system should be described more into detail.

CHAPTER 2 : DEFINITION OF LARGE EXPOSURES

Q2. Do you agree with the proposal and suggested interpretation of 'control' and of 'interconnectedness'? Do you find the guidance/examples provided in both cases useful? Please explain your views, provide examples. And where relevant provide feedback on the costs and benefits.

- We agree with the definition of large exposures as mentioned in § 71 of the document.
- The definition of a "group of connected clients" in § 78 contains two different elements: (a) control ; (b) interconnectedness.

- The first element is a well-known element of regulation ; the information is easily accessible (generally published together with the financial statements) ; data are straightforward (e.g. more than 50% of the voting rights).
  Data are easy to collect, handle and store through mass production.
  Control is rule-based and supervisor-driven.
- The second element supposes there is a fine-tuned case-by-case credit analysis. The conclusion is a matter of credit appreciation and will not be a simple black-and- white answer. The examples given in § 92 show that the degree of dependency may vary from non-existent or weak up to strong. Everyone will have its own appreciation. So, we believe that interconnectedness is a matter of appreciation and is institution-driven.

- Control means that the joint companies have to be considered as a group of customers, except when the institution can prove that there is no significant risk correlation between the companies => comply or explain.
- As LE is a backstop regime, the definition of LE will be a standard definition of exposures that are easily measurable and accessible as well as fit for mass handling. Consequently, the definition of interconnectedness must continue to be principles-based. So, only element (a) should be taken into account. Element (b) certainly can be useful in the concentration risk regime, where the approach is more fine-tuned and of a more granular kind.

CHAPTER 3 : EXPOSURE VALUE

- The LE regime should be strictly in line with the accountancy rules and with the CRD rules. Any kind of discrepancy between the building blocks of Large Exposures and CRD must be avoided.
- We would like to point out that the CEBS consultation paper does not mention the formula for calculating the LE amount to be compared with the own funds.
  In our view, the PD is not being used for the LE regime, because the latter gives a view of the risk linked to a particular position, independently of the PD of that position. However, the Credit Risk Mitigation (CRM) is taken into account. For the sake of full consistency between the CRD and LE regimes, we are of the opinion that LE should be calculated as follows :
  CRD EAD * CRD LGD * LE risk-weighting = LE exposure
  Where LE Rw = 0% for first-class sovereign risk
  maximum 20% for first-class banks (to be confirmed)
  100 % in all other cases.

- We are of the opinion that increasing the weight for interbank exposures from 20% to 100% would strongly impact interbank activity, and impede banks from effectively managing their liquidity.

Q3. In your view, how should exposure values for on-balance sheet items be calculated, gross or net of accounting provisions and value adjustments? Please provide examples to illustrate your response and feedback on relevant costs and benefits.

The calculation of the exposure value for on-balance sheet items has to be consistent with the Capital Requirements Directive. This calculation will depend on the approaches used :

- Standardized approach : Exposure value is calculated net of specific provisions
- IRBA : Exposure value is calculated gross of specific provisions.

A comparison must be realized between expected loss and provision, the difference impacts directly the own funds. The management of two definitions of the exposure (LE and CRD) is too burdensome for the industry.

Q4. In your opinion what could be the costs/benefits of applying a 100% conversion factor to the genrality of off-balance items?

Q5. Do you think that low risk items should receive a 0% conversion factor? Do you believe that there is room to apply conversion factors between 0% and 100 % in a large exposures regime? Which items could in your opinion receive a conversion factor different of 100%, and for which reasons? Please explain your views and provide feedback on the costs and benefits of such an approach.

- Full convergence between LE and minimum capital requirements: we support the proposition that the conversion factors must be identical to CRD without any divergence.
- In defining the conversion factors, one should also take into account the Solvency II-regime with a view to convergence between CRD and Solvency II.

Q6. In your opinion, how can a large exposure regime address the risk that credit institutions may not be able to exercise their legal right to cancel an undrawn credit facility?

- First, we are of the opinion that this issue should be dealt with outside the LE regime. Consistency between the LE regime and the CRD prevails.
- Nevertheless, we agree that real exposures and credit lines offered to (a group of) counterparties must not exceed the backstop level which has been laid down (i.e. 25% of own funds). This is a logical consequence of the existence of a backstop regime: it does not make sense to offer credit facilities that would put banks at risk of breaching their large exposures limit. However, the existence of such a regime should be sufficient to make sure that banks will not incur any commitments which may put their compliance with the large exposures limit at risk. In practice, banks indeed take their (potential) large exposures into account when determining their internal limits. So, there seems to be no need for introducing additional rules for (uncommitted) credit lines.
- If CEBS considers pleading for (uncommitted) credit lines to be included into the large exposures system, a clear distinction should be made between facilities which are committed, those which are uncommitted but advised and those which are uncommitted and unadvised. As for facilities which are neither committed nor advised, reputational considerations would not play any role; it would be no problem to block

the line when one has doubts about the counterparty's financial health. Consequently, those lines should be kept outside the LE regime. Reputational impact also would be limited – though it may arise - in case of advised but uncommitted lines. If CEBS were to conclude that those lines must be included under the LE regime, this would mean that the current treatment under the CRD is inappropriate and that the CRD also has to be modified. However, referring to our general position, we are not in favour of introducing into the LE regime specific provisions which may be in contradiction with the CRD.

- In any case, short-term interbank activities should not fall within the scope of the regime, since they are aimed at providing funding liquidity and allow the banking process to function well. See also question 33.
- Please note that CEBS' proposal should aim at being internally consistent. There is a danger that consistency will be lost, if there is a plea for including undrawn credit facilities as well as intragroup exposures. Indeed, it would be inconsistent to assume on the one hand that institutions live up to the expectations of their non-group counterparties for reputational reasons, and on the other hand that they may fall short of their intragroup commitments.

Q7; CEBS would welcome comments on the proposed set of principles. Are they appropriate for allowing AiRBA institutions to use their own exposure calculations ? (...)

Q8. In the context of schemes with underlying assets, do you agree that for large exposures purposes it is necessary to determine whether the inherent credit risk stems from the scheme, the underlying assets or both? Do you agree that the proposed principles are appropriate to identify the relevant risk in a large exposures back stop regime? Are there other relevant criteria that you wish CEBS to consider? Please explain your views and where relevant please provide feedback on the costs and benefits.

- Referring to our general remarks, we agree that for the determination of the concentration risk, the principle laid down in § 119 should be taken into account, which also implies that, whenever appropriate, institutions should be able to identify the underlying risks of funds and/or structured products. However, we do not think this should be part of the LE regime.

CHAPTER 4 : CREDIT RISK MITIGATION

Q9. Do you agree that for large exposures purposes there can be cases where it is justified to treat mitigation techniques in a different way from the treatment under the minimum capital requirements framework? Please explain your view and provide examples. And where relevant, please provide feed back on the costs and benefits.

- Definitely not. The benefits a differentiated definition may have for the LE regime will be largely lost due to the cost of overlapping systems and data warehouses and due to

the lack of transparency and efficiency of a complex and overlapping set of rules for which there is no need.

- We also advocate more consistency with the Solvency II regime.
- The LE CRM rules and CRD CRM rules should remain strictly identical. We refer to our general comment and would like to point out that, either the CRD rules are appropriate and can be copied into the LE regime, or they are not appropriate and then the rules have to be amended simultaneously and consistently for the two regimes. We do not support a renegotiation of the CRD in this respect. The current proposals should be limited to the integration of the LE regime into the CRD framework.
- We refer to § 57 and § 59 : the LE exposure aims at identifying and limiting large single name exposure. In our opinion, the way in which failures as for this kind of exposure must be dealt with, has nothing to do with the LE regime but rather with fields such as liquidity management, crisis management, winding up, etc. Introducing differentiated definitions of " timely" (§ 130) between the CRD and the LE regime, in our opinion is unjustified, because solvency is already concerned by the certain and timely recovery.

Q10. Do you agree that the three alternatives set out for the recognition of CRM techniques are the relevant ones? Do you think there are other alternatives CEBS should consider? Please explain your views and provide examples. And where relevant, please provide feed back on the costs and benefits

- Only proposal 1 meets the requirement of full consistency between LE and CRD, which we support. Here also, we plead for more consistency with the Solvency II regime.
- The liquidity risk of positions is dealt with in Pillar II, so there is no need for an overlap in the LE regime.

Q11. Are there costs/benefits that have not been identified? Are the costs/benefits identified correctly assessed? In particular could you provide CEBS with more information on the impact of each of the alternatives on the institutions' and collateral market's behaviour?

- The cost of maintaining two set of rules for CRM is enormous for the institutions and exceeds the supervisory benefits by far.
- The risks and costs stemming from overcomplicated IT systems and data warehouses as well as from overlapping processes are highly underestimated, and the same goes for the growing gap between internal risk management and supervisory requirements.

Q12.Do you support CEBS' proposal that institutions that use the simple method should follow the minimum capital rules (substitution approach) instead of applying the haircuts included in the current large exposure rules ?

- We highly appreciate the proposal for bringing the LE regime into line with the CRD rules and for doing away with national discretions.

Q13.Do you agree that physical collateral should not in general be eligible for large exposures pruposes ?(...)

- Definitely not. As mentioned before, the CRD and LE CRM rules should continue to be consistent and identical.

Q14. Do you agree that the development of a set of principles or guidance to require institutions to take indirect exposures into account when addressing “”unforeseen event risk” is the best way ahead ? Which principles do you think are relevant ?(...)

- We think that the risk transfer principle is inadequate, for it is an amalgam of two categories of exposure which are incomparable by nature. Direct exposures are unconditional and de facto have been incurred by the institution and there can be no doubt about their being taken into account for the calculation of large exposures. Indirect exposures depend upon the default of other counterparties. Direct and indirect exposures would sum up only when the collateral user would default. And even then, not all indirect exposures would become direct exposures, but only one; bar a systemic crisis in which all collateral users would fail. Furthermore, direct and indirect exposures would only be realised if both the collateral user and collateral issuer would default simultaneously (double default).

- Furthermore, we think that any direct exposure is always mitigated by the use of collateral, except when the value of the collateral is correlated with the direct exposure (e.g. when the collateral taker and the collateral issuer belong to the same group, a situation which is not accepted under CRD). This means that the amount of direct exposure taken into account for the purpose of large exposures should decrease whenever collateral is used, even in the case of collateral from an issuer with a lower credit rating.

- We refer also to our answer on Q2. As for interconnectedness, “indirect exposures” supposes a fine-tuned case-by-case credit analysis. The conclusion is a matter of credit appreciation and will not be a simple black-and-white answer. Consequently, “indirect exposures” should be excluded from the LE scheme.

- We agree however that under Pillar II, the recommendation of § 162 is meaningful.

CHAPTER 5 : TRADING BOOK

No comment.

CHAPTER 6 : INTRAGROUP EXPOSURES

Q19. Do you have any comments on the market failure analysis on intra-group exposures?

- We do not support this analysis, since it is not in line with the group-based risk approach followed by institutions. Neither is it in line with the development of a single financial market.

Q20. Could intra-group large exposures limits give rise to other costs and benefits? Please explain your response.

- Regulators should not use the LE regime for solving the issue of burden-sharing, nor for the supervision of intragroup liquidity.
- We are of the opinion that intragroup exposures should be totally exempt within the European Union and the EEA, provided the institution meets a number of eligibility criteria :
  - The banking group is integrated with strong central functions.
  - The banking group has a group risk policy, a central risk management, a central capital policy and contingency plan.
  - The risk policy and capital policy of the banking group is to support their subsidiaries.
  - A formal guarantee should not be required. It should be sufficient that the parent company has committed itself (eg through its internal policy and/or a comfort letter) towards the supervisory authorities that it would support its subsidiaries should they need funding.
- Outside the EEA, intragroup exposures could be exempt on the basis of reciprocity and equivalent system.
- Including intra-group exposures could result in absurd situations. For example, a parent entity may give a guarantee to its subsidiary in order to take over the risks linked to credit granted at the request of the parent company to a specific (group of) clients or within the framework of an overall group approach. The set of exposures on customers will be replaced by a single exposure on the parent entity, at the risk of exceeding the 10% limit. This leads to a paradoxical situation in which a sound group policy is jeopardized by supervisory restrictions on intragroup exposures.
- The direct interference with liquidity management within the banking group is underestimated. Taking into account intra-group exposures might prevent banking groups to manage their liquidity centrally, and to allocate this liquidity efficiently among their different entities.

Q21. What are your views on the proposals/options for the scope of application of the large exposures regime?

- According to us, intragroup limits lie outside the scope of the large exposures regulations. Indeed, the large exposures regime is based on the principle that groups must be considered as a single entity for assessing exposures. Taking into account intragroup exposures would mean that exposures of other banks vis-à-vis entities of a banking group are determined on a basis different from that for exposures of any group member vis-à-vis its sister/parent companies.

- We would very much welcome an alternative solution for the limiting of intragroup exposures. For example, when institutions comply with specific eligibility criteria as mentioned under Q20 , these companies could be exempt from limits.

Q22. Which treatment do you believe is the most appropriate for intra-group exposures i) to entities within the same Member State; ii) to group entities in different Member States and iii) to group entities in non-EEA jurisdictions ? Please explain your response.

Q23. What are your views on the high level principles to define intra-group limits?

- We advocate a single approach of intragroup exposures throughout Europe and preferably also on a global level. Different rules within Europe are rejected anyhow.
- We are in favour of a principles-based approach for defining intragroup limits. In any case, national discretions in this respect should be avoided.

CHAPTER 7 : SOVEREIGNS, …

Q26 What are your views on the proposal to remove the national discretion and to automatically exempting exposures to sovereigns and other international organisations (within Art. 113.3 (a –f), as well as some regional governments and local authorities ?

- We agree with the basic objective as mentioned in § 248. We also agree with the statement that "developed countries (…) are not subject to a plausible unforeseen event risk (…)" (§ 252) as well as with the general exemption of the exposures mentioned in art. 113.3 (a) to (f).
- For regional governments and local authorities, the LE regime should follow the CRD rule without any exception: whenever the competent national authority recognizes a regional/local public entity as being equivalent to an exposure on the central government (i.e. a zero risk weighting in the standardized approach), the exemption should be equally applicable under the LE regime.
- National discretions should be removed. The decision of the competent national authority to recognise a regional/local public entity as being equivalent to an exposure on the central government will automatically be recognized by the national authorities of the other Member States (Here we refer to the EBF response for the removal of national discretions from the CRD).

Q27 Please provide feedback on the costs and benefits that you consider would arise from the proposal

- As a result of the divergence between the LE regime and CRD rules, the institutions will have to double their systems and data. The cost for the institutions will be much bigger than the marginal interest for the supervisors.

Q28 Is there room for further exemptions ?

- In addition to the exemptions covered in question 26, intra-group exposures (as discussed under chapter 6) and short-term interbank exposures (as discussed under chapter 8) should be excluded from the LE-regime.

CHAPTER 8 : INTERBANK EXPOSURES

Q29. Do you consider that large interbank exposures of all maturities are associated with the market failures identified?

- We agree that the market failures described in the CEBS paper also apply to interbank exposures, whereby the chances of a bank failure leading to multiple defaults would increase significantly if other institutions are heavily exposed to that failing bank. However, we think that the chances of witnessing an unforeseen default are non-existent for very low maturities and highly rated counterparties, and that the cost of sheltering the banking sector from such an event would be too high as compared to the benefits.
- The management of interbank exposures is more closely connected with liquidity risk management than with the development of an LE regime.
- Given the prudential control banks are subject to, the overall risk of interbank exposures is lower than the exposures to other counterparties.
- A full harmonisation of the treatment of interbank exposures at EU level (removing national discretions), and an overall alignment with the CRD are absolutely necessary.

Q30. What do you consider to be the implications of the caveats set out above for the conclusions of the cost/benefit analysis? Do you have any other comments on the cost/benefit analysis?

- We value the attempt made by CEBS to quantify the impact of introducing a backstop at 25% of an institution's capital. However, we fear that the cost/benefit analysis will not lead to any firm conclusions. Its caveats are indeed significant, especially :

    - the fact that cost calculation is based on the assumption that all exposures can be collateralised. In practice, collateralisation of exposures is not always possible, especially when one is dealing with very short term (e.g. overnight) exposures. For this category of exposures, the introduction of a cap may cause a loss of business for banks (which in its turn could entail "disproportionate or inappropriate restrictions on banks' activities", as stated in the CEBS paper on page 63 of its advice), which is hard to quantify;

    - the assumption that "there is a sufficient number of creditworthy counterparties to enable banks to diversify unsecured exposures without significantly reducing the average counterparty creditworthiness" is not always true. Indeed, in some shallower markets, banks tend to rely on a limited number of well-known names. Institutions may well decide to call on less creditworthy counterparties in order to stay below the limit.

These caveats mean that anyhow, 89 milion EUR would be a lower bound for the cost. Since the benefits of the 25% limit lie within a range between 33 million EUR and 402 million EUR per year, one cannot draw any conclusion whatsoever about the net effect of the measure proposed.

Q31. Given the market failure and costs/benefit analysis set out, what treatment would you consider appropriate for interbank exposures?

- We refer to our answer to Q33.

Q32. Would a 25% limit on all interbank exposures unduly affect institutions' ability to manage their liquidity? Should maturity of the exposure continue to play a role? CEBS would find any practical examples useful as aids to its thinking (CEBS would not disclose confidential information).

- Yes, a 25% limit could hamper the banks' liquidity-raising activities. The maturity of exposures definitely must be taken into account, for this would allow regulators to distinguish between funding liquidity and credit provision. See also our answer to Q33.
- Just as for intragroup limits, imposing stricter interbank limits would affect the liquidity management of credit institutions and would increase the probability as well as the potential impact of a liquidity crisis.
- For short-term maturities, we are in favour of sticking to the current approach, i.e. a reporting-only system, in which the national supervisory authorities are informed of counterparty concentration.
- As for maturities, most funding liquidity transactions have a 1 to 3 months timespan. We are in favour of maintaining the current 1-year limit, for this would encompass all liquidity-related transactions. Intraday and overnight-only transactions should be excluded from the regime, because they are driven only by funding liquidity needs.

Q33. If you believe there is a market failure but a hard 25% limit would not be appropriate, what would you consider an appropriate treatment for interbank exposures?

- Interbank markets have a credit and a liquidity providing function. These are different functions by nature. Credit activities involve medium to long-term exposures, which banks will accept voluntarily. Funding liquidity transactions are used for coping with short-term liquidity needs. The aim is to match today's needs with tomorrow's inflows. They are not incurred voluntarily but can be a side-effect of other activities pursued by banks. Consequently, these exposures are (very) short-term. We would welcome a differentiation which takes these specificities into account and which would be far less stringent for short maturities.

CHAPTER 9 : BREACH OF LIMITS

Q34. Respondents' views on the approaches to non trading book breaches of the limits would be welcomed. Please explain your views and provide examples and feedback on relevant costs and benefits.

(1) EU Top consolidated level

- At the consolidated level, and since the LE regime is supposed to be a backstop system, no breach whatsoever is acceptable (§ 299 = first option). However, we refer to our answer to Q33 for the calculation of this limit.
  The supervisor systematically must be informed of any breach or better said, any anticipated breach. The institution will explain the kind of action it has planned or taken in order to make an infringement undone. The supervisors will impose appropriate measures.
- The excess is deducted from the own funds.
  A penalizing deduction (deduction of the full outstanding exposure on the client) would make things more complicated and increase the danger of systemic consequences. This should be left out.

(2) Subconsolidated or solo levels

- A breach of limit by a subsidiary (at a subconsolidated or stand-alone level) which does not entail an overall breach at the consolidated level, is not a real issue. This concerns only the spreading of an acceptable risk position on group level among the members of the banking group.
  The breach can be maintained over a longer period of time (§ 301 = third option but without deduction of the excess from own funds).
- A breach at subsidiary level should not lead to a penalty being imposed, but must be the subject of a discussion within the college of supervisors.
- This is also in line with the principle we refer to in our general comment which states that the primary level of application of the LE regime is the consolidated level.

Overall, breaches should be considered acceptable (no capital to set aside) in the following, exceptional, situations:

- When they would result from the failure of a counterparty that would lead to the realisation of an indirect exposure – and the possible breach of large exposure limits. Such a situation would trigger the selling of that collateral, so that the exposed institution could reimburse the loss. The large exposures regime should take into account that, given the possible impact on the market, this might not be possible within a very short timeframe, and assume that the aim of the institution would be to sell the collateral and therewith to manage its exposure to the collateral issuer downwards.

- When they would be due to unforeseen events, eg operational errors at counterparties, and resolved within a short timeframe.

- Short-term interbank exposures – and breaches of limits - should be exempted from the large exposures regime overall, as argued under chapter 8 Interbank exposures.

CHAPTER 10 : REPORTING ISSUES

Q35. What are your views on the 3 reporting options? Please explain and provide feedback on the costs/benefits of CEBS' initial views.

- We reject including the large exposures reporting into the Pillar 3 reporting, for the following reasons :
  - Pillar 3 reporting should be market-driven. In theory, new items should only be added if deemed of used by the market. In practice, regulators should avoid adding new requirements before Pillar 3 implementation, which is very time-consuming for banks, is fully done.
  - Pillar 3 and the LE regime have different objectives. Pillar 3 reporting aims at informing the market about the overall exposures taken by the reporting institutions, their management of these risks, and the associated capital requirements. It has a long-term focus. The LE-regime aims at preventing banks to incur too large exposures on single counterparties. Breaches are (or should) be very limited in time. Reporting of breaches in Pillar 3 would be meaningless as by the time of publication they would have been resolved.
  - The bank's customer easily can be identified and this is in contradiction with the bank's confidentiality duty..
  - The customer is not concerned by the bank's obligation to stay within the limits.
  - There is a danger of causing a negative downwards spiral.

- The option "Reports defined by the supervisors" is not the best solution for the following reasons:
  - There is no such thing as a "one size fits all" reporting which could be used adequately for dealing with the situation of all institutions without becoming too detailed.
  - There is an overlap with the financial institutions' internal reports, which, at least as far as leading banks are concerned, are much more granular and much more accurate than the mandatory supervisory reporting.

- We propose the second option "Reporting to supervisory authorities based on financial institutions' internal reports". In practice, this corresponds with concentration risk reporting. The advantage for the institutions is that it prevents any overlapping of reporting, whereas the supervisors will gain better information and a high added-value SREP.

- Nevertheless, and more particularly as for small banks, "a report defined by the supervisors" will be a substitute solution for banks which do not have any internal report.

Q36. Do you support CEBS' thinking on the purpose and the benefits of regular reporting using predefined reporting templates ?

- The LE regime is a backstop and the institutions are drawing a more accurate concentration risk report, which is one of the elements of the SREP and which will be the basis for the dialogue with the supervisory authorities. So, we propose providing that only an "event reporting is required", especially as for LE. This will prevent any reporting overlap as well as LE "non event" reporting.
  In other words, institutions for which the chances of breaching the LE limits are small, will not have to report, as long as they stay below a fixed "warning limit", i.e. a percentage lower than 15% (for instance 10%).
  Institutions which go beyond the "warning limits", will have to report on a regular basis.

- If CEBS decides to impose a "standard prudential reporting defined by the regulators/supervisors" :

  - this should take the form of an additional COREP template, with a uniform format, truly identical in all of the Member States, without any national option or discretion, without any divergent interpretation or implementation.

  - with standard frequency and remittance dates being laid down.

  - the reporting requirement should be imposed only on the top consolidated level. Reporting on statutory level has no sense. Given the fact that the CRD applies to the consolidated as well as the statutory level, chances are that supervisors will require reporting of large exposures on a statutory and/or subconsolidated level. In that case, we should point out that reporting must be done on the same accounting basis.

  - Interoperability with current COREP templates : (a) the contents already to be provided in the current COREP templates should not be asked twice. (b) The exposure values should be calculated along the same lines as for the COREP templates.

Q37. What is your opinion on CEBS' initial thinking regarding the elements to be reported under the large exposures regime ?

- Reporting should be required only at EU top consolidated level.

- 1st and 2nd bullets : as stated under Q3 to Q7, the exposures reported should be fully in line with the accountancy figures (IFRS for large banks) and the CRD rules. Any specific LE rule should be left out.

- 3rd bullet : what is meant is the EAD minus the CRM, without any divergence from CRD (See our comment on Chapter 3)

- 4th bullet : to be deleted (See our answer to Q10)

- 5th bullet : Interbank exposures should be included into the first three bullets just like any other exposures. Intragroup exposures should be left out.
- 6th bullet : idem 5th
- 7th bullet : to be deleted
- 8th : to be deleted. This information is available by request : the information does not consist of figures, but rather takes the form of lists, organisation schemes, etc. This information is, however, not easy to gather, and any conclusions need to be based on a (partly subjective) credit assessment. Its format and subjective character make it improper for regular reporting.

CHAPTER 11 : CREDIT RISK MANAGEMENT

Q38. Do you agree with CEBS' views on the recognition of good credit management ?

- We agree that banks applying advanced risk management should not be exempt from the LE system.
- We agree that sound credit management must be rewarded and consequently, we would appreciate if the LE regime does not diverge from CRD thanks to additional restrictions for the LE regime.