



## European Banking Industry Committee

---

European Banking Federation (EBF) • European Savings Banks Group (ESBG) • European Association of Cooperative Banks (EACB)  
European Mortgage Federation (EMF) • European Federation of Building Societies (EFBS)  
European Federation of Finance House Associations (Eurofinas)/European Federation of Leasing Company Associations (Leaseurope)  
European Association of Public Banks (EAPB)

LDR 0559/2009

Mrs. Arlene McCarthy  
Economic and Monetary Affairs Committee  
European Parliament  
B - 1000 Brussels

To: [arlene.mccarthy@europarl.europa.eu](mailto:arlene.mccarthy@europarl.europa.eu)  
Cc: [ole.christensen@europarl.europa.eu](mailto:ole.christensen@europarl.europa.eu)  
[klaus-heiner.lehne@europarl.europa.eu](mailto:klaus-heiner.lehne@europarl.europa.eu)  
[othmar.karas@europarl.europa.eu](mailto:othmar.karas@europarl.europa.eu)

Brussels, 1 December 2009

***Re: EBIC Comments on the legislative proposals for amending the Capital Requirements Directive as regards the trading book and for re-securitisations, and the supervisory review of remuneration policies ("CRD 3")***

Dear Mrs. McCarthy,

The European Banking Industry Committee (EBIC) brings together European banking associations with a mandate to provide advice, assure a comprehensive consultation of market participants and ensure representative industry views on all policy aspects related to banking activities, in particular during the process of drafting, adopting and implementing EU financial legislation.

EBIC wishes to congratulate you to your appointment as the Rapporteur for the Proposal for a Directive amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies ("CRD 3"). EBIC wishes you every success in this challenging task and takes the opportunity to express its willingness and availability to contribute with views and expertise to the forthcoming discussions

Through this letter EBIC would like to convey to you the main common concerns of its Member Associations in relation to the CRD 3 proposal. More detailed EBIC views on the European Commission's proposal and the Council compromise from 28 October 2009 are reflected in the note which is attached to this letter.

EBIC's main messages on the CRD 3 proposals should be read in the light of EBIC's general support for the announced regulatory programmes of the European decision-makers and the Financial Stability Board to address and repair the current shortcomings in the prudential framework. Furthermore, the remarks should take into account EBIC's firm belief that there is a strong need for aligning EU legislation with international regulatory standards adopted by the Basel Committee on Banking Supervision. In this context EBIC welcomes the fact that the final CRD 3 proposal put forward by the Commission in July has reduced the important discrepancies that existed between the measures initially envisaged by the Commission and the proposals discussed in the Basel Committee.

1) Need for an overall Impact Assessment

EBIC strongly believes that there is a need to undertake an overall assessment of the cumulative impact entailed by the wide range of proposals that will reshape the regulatory landscape. Such an impact assessment should be undertaken prior to the coming into force of new regulations and should not be limited to selected aspects. EBIC strongly believes that it would be even more important to ascertain in advance how the new regulatory requirements will influence (i) the capacity of banks to lend to the economy, (ii) the availability of other financial resources to the wider economy and, ultimately, (iii) economic growth.

2) Remuneration Policies and Practices

EBIC agrees that there is a need to align compensation incentives with the institutions' long term interests. Remuneration principles should target those functions and staff categories which have the potential to expose financial institutions to excessive risks and should be applied in a proportionate way to smaller credit institutions. The proposals of the European Commission in this respect are in line with decisions taken by the Financial Stability Board on a global level. EBIC therefore supports these proposals and urges EU decision makers to make all efforts to maintain the international level playing-field and avoid creating distortions through further, more prescriptive guidelines.

3) Prolongation of Basel I floors

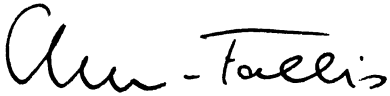
EBIC regrets the decision to extend beyond 2009 the transitional floors calculated according to the Basel I methodology, which has been taken without any consultation with the stakeholders. EBIC believes that this decision is not an appropriate measure for ensuring better capital adequacy. Furthermore, it is particularly burdensome for institutions to continue calculating capital requirements according to two different methodologies whilst being obliged to implement a whole range of new prudential rules. Taking into consideration also the declarations by Spain and France accompanying the Council compromise on the Commission's proposal for CRD 3, EBIC invites you to challenge the transposition of the Basel Committee's decision to extend Basel I floors into EU legislation and to question whether it would be appropriate for the EU to follow-up on it.

4) Implementation

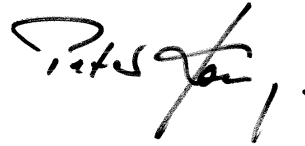
Given the significant increase of capital charges envisaged in CRD 3, EBIC would like to point out that an early implementation of such rules in the EU is likely to put European banks under excessive pressure to deleverage and may have adverse effects on lending. Furthermore, it risks putting EU banks at a considerable competitive disadvantage in relation to their counterparts in non-EU countries, especially in the US. Therefore, EBIC calls for the implementation date for new capital requirements foreseen in the CRD 3 proposal to be aligned to the implementation in non-EU countries, particularly the US, of the corresponding the Basel Committee's rules, as well as for the inclusion of a grandfathering clause for existing resecuritisation positions, as currently foreseen in article 122a CRD.

EBIC stands ready to discuss this matter further with you. The EBIC Secretariat remains at your disposal for any questions you may have in relation to these issues and would be glad to meet with you personally in order to explain our main concerns.

Yours sincerely,



Karl-Peter SCHACKMANN-FALLIS  
EBIC Chair



Peter KONESNY  
Chair EBIC Working Group on  
Supervisory Practices



## European Banking Industry Committee

---

European Banking Federation (EBF) • European Savings Banks Group (ESBG) • European Association of Cooperative Banks (EACB) European Mortgage Federation (EMF) • European Federation of Building Societies (EFBS)  
European Federation of Finance House Associations (Eurofinas)/European Federation of Leasing Company Associations (Leaseurope)  
European Association of Public Banks (EAPB)

1 December 2009

### **EBIC Comments on the Proposal for a Directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies (“CRD 3”)**

**The European Banking Industry Committee** brings together European banking associations with a mandate to provide advice, assure a comprehensive consultation of market participants and ensure a representative industry view throughout the process of drafting, adopting, implementing and enforcing EU-financial legislation and thereby provide input for the European institutions and their relevant sectoral committees. It is amongst the declared aims of EBIC to advise the Commission on relevant legislative banking and cross-sectoral initiatives and any developments at Community level affecting the banking and financial services activities associated with the establishment of a European Single Market for financial services.

EBIC has been established by the main banking industry federations: the European Banking Federation (EBF), the European Savings Banks Group (ESBG), the European Association of Cooperative Banks (EACB), the European Mortgage Federation (EMF), the European Federation of Building Societies (EFBS), the European Federation of Finance House Associations (Eurofinas) / the European Federation of Leasing Company Associations (Leaseurope), and the European Association of Public Banks (EAPB).

EBIC, hereby, would like to convey some important messages of the banking industry in relation to the legislative proposal for amending the Capital Requirements Directive as regards capital requirements for the trading book and for re-securitisations, and the supervisory review of remuneration policies – the so-called “CRD 3 proposal”. These messages reflect significant common concerns of the industry and complement the individual positions of the EBIC Member Associations.

### **1. Cumulative impact of proposed regulatory changes and the need for a thorough impact assessment and appropriate calibration**

The banking industry generally agrees that there have been deficiencies in the prudential treatment of complex financial instruments, as well as of the trading book and that there is a need to remedy such shortcomings. However, EBIC would like to underline that whereas the proposed amendments to the CRD may have a strong rationale when looked at individually, their effects need to be considered in the broader context of the overall regulatory reforms that are envisaged.

The banking industry is currently faced with an “avalanche” of regulatory proposals targeting mainly the capital requirements framework. Each of the envisaged regulatory changes (e.g. capital requirements for trading book exposures, prudential treatment of resecuritisations, the definition of eligible Tier-1 hybrid capital instruments, stricter loan-to-value requirements for mortgage lending, dynamic provisioning, capital requirements for mortgages denominated in a foreign currency, liquidity buffers, stricter treatment of large exposures) would entail a significant increase in the level of capital required for banks. Moreover, other measures that the Basel Committee is known to be considering (e.g. leverage ratio, counter-cyclical capital buffers, a stricter definition of capital, Pillar-2 add-ons, capital surcharge, contingent capital) would put higher strain on the industry. Nevertheless, none of the institutions involved in the regulatory process has made an attempt to assess the magnitude of the cumulative effects which the proposed changes are likely to produce. Taken together, the impact of the numerous regulatory proposals could prove extremely harmful. Therefore, EBIC urges decision-makers to pay due consideration to the potential overall impact of the envisaged changes, which are likely to substantially reduce the banking sector’s capacity to lend to the real economy.

Against this background, EBIC invites regulators to carry out a thorough impact assessment before taking any final decisions on the proposed regulatory changes. Such impact assessment should accompany any future regulatory proposals and not be conducted in a second phase, after preliminary decisions have already been taken. It is imperative that the impact assessment looks at all the consequences entailed by the measures put forward or considered by the EU decision makers and the international regulatory bodies (the Financial Stability Board, the Basel Committee). Moreover, the impact assessment should analyse the effects of regulatory changes on the lending capacity of banks and as a consequence on economic growth and on the availability of other financial resources to the wider economy. A proper, comprehensive impact assessment of all envisaged regulatory changes - including the increase of capital requirements for the trading book and for re-securitizations proposed in CRD 3 - could help avoiding imposing an excessive level of

overall capital requirements. There is a need for a balance to be struck between solvency and lending capacity, thus enabling the industry to keep on playing its funding role to the real economy.

EBIC is aware that the Basel Committee will carry out an impact assessment at the beginning of 2010. However we fear its scope might be not wide enough, as it might not consider the overall measures that the FSB will take on board according to its working programme. Moreover, the impact assessment should not be limited to the capital requirement measures, but explicitly examine the broader effects and unintended consequences.

Depending on the outcome of those impact assessments, there should be mechanisms available to enable legislation to be adjusted and the new measures to be properly calibrated.

The banking industry stands ready to provide any assistance needed by regulators when conducting such assessment.

## **2. Remuneration policies and practices**

EBIC is generally supportive of the envisaged provisions on remuneration policies entailed in the CRD 3 proposal. EBIC takes the view that all financial institutions need to pay close attention to the alignment of compensation incentives with the institutions' long term interests.

EBIC agrees that the inappropriate remuneration policies of some banks were one driver of the current financial crisis. However, it must be underlined that, on the whole, the role played by remuneration policies in the crisis is less significant than other factors. It is therefore important not to overemphasize the importance of measures tackling remuneration policies, as compared to other more urgently needed regulatory responses geared at enhancing the overall corporate governance of banks.

Remuneration policies are very institution-specific and the responsibility for remuneration policies rests mainly and ultimately with the financial institutions themselves. Therefore, remuneration principles developed by public regulators for addressing weaknesses should remain high-level. It is important that prescribed public guidelines be not too prescriptive and flexibility is preserved, in view of avoiding a one-size-fits-all approach. It may be difficult for some financial institutions to measure the individual performance of directors independently from the overall performance of the credit institution. It depends on how staff are assessed and even the culture of the organisation. Some firms do not promote a "star" culture, preferring a more team-oriented outlook or overall perspective.

EBIC welcomes the additions made by the Council which emphasise that the principle of proportionality should be carefully observed in the case of small credit institutions and investment firms in the contexts of effective risk alignment and non-cash variable remuneration. Against this background, EBIC acknowledges and supports the proposal to impose a binding obligation on banks and investment firms to have remuneration policies that are consistent with effective risk management.

Furthermore, remuneration principles should target those functions and staff categories which have the potential to expose financial institutions to excessive risks. This is imperative given that the vast majority of staff of financial institutions, in particular those involved in activities such as retail banking, do not perform tasks or take decisions which are relevant to the level of risk taken by the institution. EBIC would like to highlight that it is of utmost importance to have at all times clarity about the categories of staff that will be subject to remuneration-related measures. It needs to be clearly ascertained what is understood by "risk takers" and "control functions". Therefore EBIC

welcomes the limitation of the applicability of the provisions on remuneration policies in the CRD 3 to those categories of staff, including senior management, whose professional activities have a material impact on the credit institutions risk profile. This is particularly important in view of avoiding conflicts between remuneration principles and national labour legislation and regulations, as well as with the principle of contractual freedom and confidentiality obligations with regard to firms' business strategies.

With regard to CEBS mandate set out in Article 22 paragraph 3 of the discussed proposal, EBIC fears that further guidelines by CEBS in support of the principles on remuneration policies risk ignoring the diversity of existing remuneration policies and are likely to turn the principles (included in the reviewed CRD) into prescriptive norms proposing inappropriate one-size-fits-all remuneration structures. It is important that the industry be duly consulted on such guidelines.

Although EBIC acknowledges the need for the introduction of enforceable rules on remuneration, we take the view that capital add-ons would be a disproportionate extreme sanction that should be employed only in the case of serious disincentives to sound risk management stemming from remuneration policies; in no way should minor breaches entail additional capital requirements. Generally speaking, competent authorities should be able to choose from an array of non-financial sanctions. Any such sanctions imposed by supervisory authorities must be used only as a last resort, i.e. after all other methods of ensuring compliance with the remuneration principles have failed.

In particular, it must be borne in mind that imposing capital add-ons and/or financial sanctions does not improve the compliance of the remuneration policy with the principles, nor does it reduce the associated risks. Instead, it should always be a priority to enforce the remuneration principles by requiring the necessary adjustments to the institution's remuneration policy and/or practices to be undertaken.

Furthermore, global and European alignment in terms of scope, rules and timetable for implementation is of the utmost importance to prevent regulatory arbitrage and an uneven playing field.

### **3. Prolongation of Basel I floors**

EBIC notes that the Council has added to the Commission's legislative draft on CRD 3 a proposal to extend the transitional provisions provided for in Article 152, paragraph 5, of Directive 2006/48/EC in respect of the Basel I floors. We understand that this proposal is intended to be in line with what has been agreed within the Basel Committee for Banking Supervision.

We fully understand the decision taken by the Basel Committee to extend the transition period beyond 2009 taking into account that the Basel II framework has not become operational in some countries as yet. However, we do not believe that it would be necessary or even appropriate for the European Union to follow-up on the decision taken by the Basel Committee. EBIC highlights that whereas the Basel II Framework explicitly permitted such prolongation, the CRD did not foresee it – and this for good reasons.

First, European banks have implemented the Basel II framework for some time now and have adapted the Basel II parameters to the financial crisis in the meantime. Under these circumstances, the banking supervisors from EU Member States have had ample opportunity to examine the impact of the Basel II framework on capital requirements in comparison to those imposed under Basel I.

Furthermore, the pressure exerted by financial markets has resulted in banks holding capital levels which are much higher than those now required by the Basel I floor. Consequently, the banking

industry does not believe that it would be realistic to hold lower capital, whatever EU regulatory capital requirements in this regard may be. This is being confirmed by the outcome of the stress-testing exercise conducted by CEBS, which indicates that *“the (European) banks’ aggregate Tier 1 capital ratios will be well above 9%, compared to the present Basel minimum requirement of 4%”* and *“and no bank would see its Tier 1 ratio falling under 6% as a result of the adverse scenario”*.

The envisaged discretionary prolongation of the Basel I floors, that were conceived merely as transitional measures, raises important questions about legal certainty in EU law. Also, EBIC notes that the decision to prolong Basel I floors has been adopted without any due process and was not part of the public consultation documents circulated by the Commission prior to its adoption of the legislative proposal on CRD 3.

The proposal to extend the Basel I floors is of major concern to the banking industry because of the administrative burden which may result from the proposed amendment as it would imply requiring Europe’s credit institutions to continue calculating Basel I capital numbers, with all systems and other resource implications that it brings along. EBIC sees no regulatory benefit that would justify imposing this additional burden on banks now that supervisors have publicly confirmed that their level of own funds is higher than the floor imposed by Basel I.

Under these circumstances, EBIC invites EU law-makers to refrain from amending the current transitory provisions and, therefore, to accept that the Basel I floors will expire on 31 December 2009. An extension would seem to be particularly inappropriate in situations in which a bank is able to demonstrate to its supervisor through objective reporting that it is operating above the minimum capital level.

#### **4. Concerns related to early implementation of higher capital requirements**

The CRD 3 proposals will lead to significantly higher capital charges for EU financial institutions. Much of the additional capital would need to be held against legacy positions which are illiquid and difficult to unwind quickly. Early implementation of these rules – end-2010, as currently envisaged by the Commission and the Council – is likely to put pressure on banks to deleverage and force them to sell parts of their portfolios at considerable losses, thereby triggering adverse effects on lending. Furthermore, these additional charges for the trading book and resecuritisation positions imposed on banks have a broader impact on the cost of doing business in Europe and are likely to place European banks at a considerable competitive disadvantage compared to their counterparts in countries outside the EU.

For these reasons, EBIC urges the European Parliament to make sure that the burdensome capital requirements proposed in CRD 3 are introduced in the EU only simultaneously to the implementation of the corresponding Basel Committee’s rules in non-EU countries (especially in the US). Hence, the implementation date of the CRD 3 should be such that it does not put at disadvantage EU banks. Furthermore, in line with the current article 122a CRD, CRD 3 should contain a grandfathering clause for existing re-securitisation positions.