



FEDERATION
BANCAIRE
FRANCAISE

*Banking supervision
And Accounting issues Unit
The Director*

Paris, August 8th 2012

French Banking Federation response to EBA, EIOPA and ESMA¹'s Joint Consultation Paper on its proposed response to the European Commission's Call for Advice on the Fundamental Review of the Financial Conglomerates Directive. (JC/CP/2012/01)

Dear Madam,

The French Banking Federation (FBF) is the professional body representing the interests of the banking industry in France. Its membership is composed of all credit institutions authorised as banks and doing business in France, i.e. over 450 commercial, cooperative and mutual banks operating in France. It includes both French and foreign-based organizations.

FBF banks welcome the opportunity to answer the Joint Committee Consultation Paper on its proposed response to the European Commission's call for advice on the Fundamental Review of the Financial Conglomerate Directive.

As a preliminary and very general comment, we would like to underline that the Financial Conglomerate Directive provides a robust and efficient regulatory framework which allows for the sound development and oversight of the bank-insurance model. The priority in our view lies first and foremost in the finalisation of the Basel3/CRD4 and Solvency II reforms, and their proper implementation.

../..

**Ms Linda van GOOR
Secretary to the European Financial
Conglomerate Committee
European Commission
Rue de la Loi 200
B-1049 Brussels**

¹ ESAs (European Supervisory Authorities)

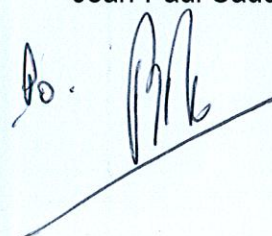
We support the proposed recommendations as far as they relate to the sources of risk specifically relating to financial conglomerates supplementary supervision (i.e. risk concentration, intra-group transactions, internal control mechanisms and risk management processes). They should not seek to address any potential sectoral issues, for which a specific supervisory regime already exists (e.g. CRD for banks and Solvency 2 for insurance groups).

You will find in the annex our answer to the questions raised in the consultation paper.

We thank you for the consideration of our remarks and remain at your disposal for any question or additional information you might have.

Yours sincerely,

Jean-Paul Caudal

A handwritten signature in dark ink, appearing to be 'J.P. Caudal', written over a horizontal line.

Annex

French Banking Federation response to ESAs Joint Consultation Paper on its proposed response to the European Commission's Call for Advice on the Fundamental Review of the Financial Conglomerates Directive.

As a preliminary and very general comment, we would like to note that current regulatory expectations as regard financial conglomerates, as the ones stressed in the Joint Forum "*Principles for the supervision of financial conglomerates*" (which set the trend for European legislation in this area), envisage a high level of accountability regarding to global risk management, group risk profile, group risk appetite, global liquidity or capital management.

Nevertheless, at the same time we note that the current proposed framework for D-SIBs, by setting capital allocation at the country level, would lead to added rigidity in group-wide risk and capital management for banking groups that have validly opted for such structure. The current proposed framework for D-SIBs is only one example. More generally, we are worried at observing an increasing gap between a trend toward national supervision ring-fencing and the current regulatory expectations towards financial conglomerates which, in this context, seems to be untimely.

Therefore, the search for "an ultimate responsible entity", even though understandable from your point of view, seems to us a bit at odds. In the current economic environment, the priority should be to avoid adding incremental layers of regulation without a preliminary in-depth impact analysis.

Q1 – Perimeter of supervision

The ESAs suggest a broader definition of financial conglomerates. In this prospect, the definition of financial sector would be enlarged to include insurance ancillary services undertakings and all special purpose vehicles / entities. In addition, the ESAs contemplate including Institutions for occupational retirement provision (IORPs) in the perimeter of supervision, in a similar manner to the inclusion of Alternative Investment Fund Managers (AIFM) and Asset Management Companies (AMC).

1. In the case of financial conglomerates headed by a supervised entity, the perimeter of supplementary supervision should consist of entities which are subsidiaries consolidated at the highest level of the group as well as the entities in which the parent undertaking or its subsidiaries own a participation (i.e. exert significant influence) reflected in consolidated accounts. In the case of mutual and cooperative banking groups, this perimeter would include entities consolidated in the balance-sheet of the central body, as well as the regional banks and their subsidiaries (which is already the case today, at least in France).

The perimeter of supplementary supervision may exclude entities whose inclusion would lead to inappropriate figures, subject to approval by the competent authority on a case-by-case basis (e.g. temporary holdings).

Banking groups already consolidate their material risks. Indeed, according to the current accounting standards (IAS27/SIC12), and even more with the new principles (IFRS 10), the controlled SPV are included in the accounting consolidation perimeter.

As the accounting principles are based both on power and on exposure to risks and rewards, the conglomerate's consolidation perimeter is aligned with their exposures to risks.

2. We consider that the application of supplementary supervision to non-regulated special purpose vehicles and IORP pension funds should follow the general principle set out in point 1 above in order to define the scope of supplementary supervision. It should also be noted that IFRS 12 will require disclosures on material SPV / SPE which wouldn't be consolidated in the IFRS 10 standard and that IAS 19 will require more detailed disclosures on asset plans.

3. As regards IORPs², the net asset value or the net liability value of an IORP that manages a defined benefit pension plan is accounted for in the consolidated balance sheet under IAS 39. Moreover, net defined benefit pension fund assets are deducted or risk-weighted under CRR I. In this context, it would be worth clarifying which specific risks IORPs would pose to a financial conglomerate which do not exist at sectoral level, justifying specific requirements in the context of financial conglomerate supervision.

4. Unregulated entities and regulated entities interactions within a financial conglomerate should be taken into account as "environmental" factors as part of the Pillar 2 Supervisory Review and Evaluation Process of banks and as part of the Own Solvency & Risk Assessment of insurers (i.e. without strictly extending the regulation to unregulated entities). Unregulated entities should not be regulated differently because they are part of a financial conglomerate in comparison to unregulated entities which are part of other regulated financial groups.

5. We believe that supervision should not create an uneven level playing field. As unregulated entities have rightly been recognized as an important focus by the G-20, the Financial Stability Board and the Joint Forum, we appreciate the emphasis put on such entities in the context of the supervision of financial conglomerates. But it does not mean that this issue has necessarily to be fixed by an extension of the existing regulation to all kind of unregulated entities within conglomerates. This would create an uneven playing field issue for these entities when being part of a wider group.

Q2 – Responsible legal entity for compliance with group wide requirements

The ESAs consider that supervisors should be entitled either to require the creation of an intermediate financial holding responsible for all the entities subject to supplementary supervision (tool 1) or to designate one single "point of entry" at the top of the unregulated entities such as a specific team or division or a member of the Board of the parent entity (tool 2) or to designate a specified regulated entity as point of entry (tool 3).

6. First of all, we strongly object to the implementation of "tool 1" and the possibility which could be given to a supervisor to influence the legal and organizational structure of a financial conglomerate. It would be a too far-reaching power which would enable the authorities to unjustifiably interfere in the governance of the company. At the European level, the CEBS has recognized as a general principle that supervisory authorities should "not interfere in an institution's strategy and the way it runs its business". This is all the more valid when the shareholding structure incorporates minority shareholders (cf. example below).

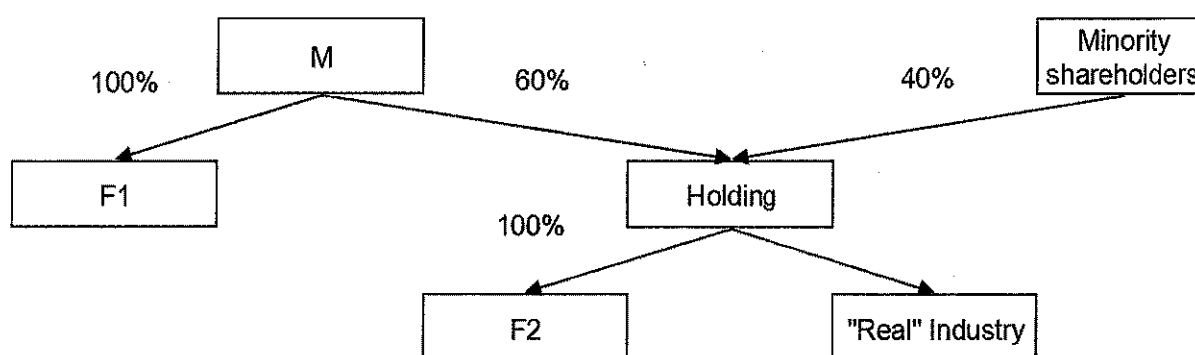
7. Regarding the point of entry for supervisors, there is no issue where the top entity is a regulated entity (bank, insurance company or MFHC); this entity is also the natural point of entry for supervision. This calls for two remarks:

- in the context of mutual and cooperative financial groups, this responsibility would fall to the central body as defined by national laws;

² Institutions for occupational retirement provision.

- within this entity, if the supervisor feels necessary to designate more precisely point of entry, it cannot be a member of the Board. We draw your attention on the fact that the Board is a collegial body. The Board can entrust missions to the one of its members but these missions are fulfilled only to the Board benefit. The Board determines the orientation of the company's activity and oversees its implementation. Executive management is provided by the Chief Executive Officer ("CEO") who assumes the general management of the company under his responsibility and represents the company in its relations with third parties. Moreover, the reports drawn up following the controls carried out by the supervisor are provided to CEO or Chief Operating Officer or "*specific team or division*". It seems logical that the supervisor contacts CEO or Chief Operating Officer or "*specific team or division*" for all supervisory actions. CEO or Chief Operating Officer or "*specific team or division*" will, if necessary, provide the relevant information to the Board.

8. For more complex groups, we think it will be necessary to distinguish the point of entry from the "ultimate responsible" entity. This can easily be seen in the following example:



where F1 and F2 are two financial, regulated, entities.

In this example, F1 can be the point of entry but not the "ultimate responsible" entity. Actually, F1 exert no influence on F2. M is the only entity in this group which has a real influence on F1 and F2. If Holding had only a minority interest in F2, M could still decide to sell its participation in F2.

We also wish to underline that the difference between the concepts of "responsible entity" and "point of entry" is unclear when the two functions are filled by separate entities. We understand that the responsible entity is in charge of coordinating information flows, fulfilling reporting requirements and ensuring compliance with supplementary supervision, in which case the need for a separate entry point is unclear (as the responsible entity is likely to have more knowledge and expertise than any other entity, regulated or not).

Q3 & Q4 – Requirements imposed on this qualified parent entity and enforcement of the group wide requirements

In their recommendation 5, the ESAs suggest that the European commission should explicitly require the ultimate responsible entity to have a coordinating and directing role over the other entities of the conglomerate. In the recommendation 6, the ESAs suggest that the European Commission develop an enforcement regime toward the ultimate responsible entity.

9. We are particularly concerned by the ESAs' recommendation suggesting to the European Commission to explicitly require that "*the ultimate responsible entity to have... a directing role over the entities of the conglomerate*". We would like to remind you that supervision has to

take into account the framework imposed by the company law of the country. As such, this proposal is unreasonable as in many countries it would breach company law applicable to legal entities having legal personality, as well as other existing national legislations. We strongly oppose this suggestion which will create significant legal issues.

10. If deemed necessary, it may be clarified that the ultimate responsible entity shall take the necessary steps to ensure compliance with the financial conglomerate directive and shall be entitled to do so, in particular to implement, calculate, report to the coordinating supervisor and monitor group wide requirements, on behalf of all entities included in the supplementary supervision. It is worth noting that Art. 9 of the Financial Conglomerate directive already in force requires *"regulated entities to have, in place at the level of the financial conglomerate, adequate risk management processes and internal control mechanisms, including sound administrative and accounting procedures"*. In addition, Art. 14 states that *"Member States shall ensure that there are no legal impediments within their jurisdiction preventing the natural and legal persons included within the scope of supplementary supervision, whether or not a regulated entity, from exchanging amongst themselves any information which would be relevant for the purposes of supplementary supervision"*. Therefore, we don't see the need for an additional layer of regulation in this area.

Nevertheless, please remember that confidentiality of information is a legal issue and that the disclosure of confidential information is usually constrained by the law in force in a country. Notably for public companies for which information sharing between a large numbers of people raises delicate issues.

Q5 – Other additional empowerment of supervisors

In their recommendation 8, the ESAs suggest creating a minimum set of sanctioning measures and suggest the ESAs should be asked to develop guidelines or binding technical standards for a common reporting scheme on risk concentrations and intra group transactions.

11. It is worth clarifying that sanctions should only be used to address infringements regarding sources of risk specifically relating to financial conglomerates supplementary supervision (i.e. risk concentration, intra-group transactions, internal control mechanisms and risk management processes). They should not seek to address any potential sectoral issues, for which a specific sanctioning regime already exists (e.g. CRD for banks and Solvency 2 for insurance groups).

In particular, the ESAs underline (on page 41) that *"currently, there are differences in regulation between the banking and insurance sector. CRD is more prescriptive than Solvency II. Moreover, the CRD IV proposal from the European Commission contains an important strengthening of the sanctioning regime and is more detailed in the sanctions that should be applied. Although these CRD IV proposals are still under discussion, this strengthening of the enforcement regime may create an unlevel playing field between financial conglomerates"*. FBF banks underline that the strengthening of the sanctioning regime applicable to financial conglomerates should not seek to address shortcomings in the insurance sector prudential regulation, as this would undoubtedly create an unlevel playing field between insurance companies, depending on their inclusion or not in the supervision of a financial conglomerate.

12. As regards the development of binding technical standards for a common reporting scheme on risk concentrations and intra group transactions, should the European Commission retain this recommendation, it would be advisable to carry out further analysis including a cost / benefit analysis on such reports so that they are actually implemented in cases and in a way which is really needed.

It is worth underlining that, in member States where financial conglomerates are already subject to intra-group transaction or concentration limits and restrictions, as well as supervisory reports, it is questionable whether far more detailed common reports on intra-group transactions and concentrations would bring significant benefit from a supervisory perspective.

13. The Financial Conglomerate Directive should be based on sectoral regulations and should only seek to address possible issues at the Financial Conglomerate level when they are not addressed in sectoral regulations. In this respect, we are particularly concerned by the detailed prescriptive requirements set out on page 36 with respect to internal controls while sectoral regulations already provide with detailed prescriptions in this area. We strongly advise against duplicating sectoral regulations in the Financial Conglomerate directive.

For example, the requirements pertaining to *"the definition of tasks and responsibilities of the various units assigned with the control of risks within the conglomerate"* and to the *"periodical information flows which allow the achievement of strategic objectives and the compliance with regulations to be verified"* seems to ignore the provisions relating to risks controls and compliance under CRD IV (as well as planned RTS in this area) and Solvency II. However the coordination duties at group level should include coordination of internal controls mechanisms.

14. Moreover, some of the requirements set out on page 36 tend to suggest there are currently severe deficiencies with respect to accounting procedures and systems within conglomerates, for example the following suggested provisions : *"mechanisms for integrating the accounting systems, also with the aim of ensuring the reliability of the registered items on a consolidated basis"* or *"highlighting and accounting procedures which allow the (intra-group) transactions between entities in the conglomerate to be checked, quantified, monitored and controlled"*. Not only the existence of such deficiencies in accounting procedures and systems within financial conglomerates still remain to be proved, but this is also questionable whether accounting procedures and systems issues should be dealt by the Financial Conglomerate Directive exclusively. The Art. 9 of the Directive in force already provides with the requirement of sound internal control mechanisms, including accounting procedures. If deemed necessary, it could be clarified that the accounting procedures referred to in Art. 9 include the registered items on a consolidated basis and intra-group transactions.

Specific questions summarised in annex H

Q1: How many additional conglomerates would be in the scope of the FICOD if
 a. IORP Pension funds were to be included?
 b. SPV/SPEs were to be included?

Q2: What characteristics would these new financial conglomerates have (size, type etc...)?

Q3: What would be the scale of additional capital requirements (and the differences in the quality of capital?) if
 a. IORP Pension funds were to be included?
 b. SPV/SPE were to be included?

Q4: Please provide some information on the potential additional compliance costs were your group to be identified as a conglomerate under these proposals.

Q5: Please could national supervisors provide an estimate of the additional resources required were the scope of supervision to be enlarged as envisaged in this proposal.

Generally speaking, the French Banking Federation is not in a position to respond to these questions. National supervisors may be best placed to provide information and data regarding the impacts associated with the proposals.