

# EBF NEWSLETTER

THE VOICE OF EUROPEAN BANKS

*EBF 50th Anniversary*



## EDITORIAL

2010 marks the 50th Anniversary of the European Banking Federation.

It may not be the best of times for celebration. We are on the way to recovering from an unprecedented financial and economic crisis, with thousands of jobs at stake and political proposals that do not appear to meet citizens' expectations. As a trade Association, the EBF has just been through arguably, the three most difficult years of its existence, and tough times are still ahead.

Yet we feel that as the European banking sector representative, the EBF has developed a credible track record. It has established itself as the partner of choice in discussions with the European Institutions; it is frequently consulted by regulatory and supervisory bodies, whether global or European; it is the natural interlocutor of consumer and business organizations on financial services issues; and it is trusted by the media as the voice of European banks. This status is the outcome of the work of a dedicated team, and of the commitment of members over the years. I would like to thank them all.

As you will see in this issue of EBF News, we have been busy putting across our message to all stakeholders and continuing a dialogue, which is more crucial than ever. While we fully understand and support the need for regulatory revisions, our sector is facing a wave of measures, some of which, will dramatically impact our economy as a whole. This message may not be popular, but we must continue to make our point before measures are implemented and banks are blamed for not supporting the economy. We have acknowledged some responsibility in the crisis and are actively trying to help find the appropriate remedies to prevent future crises. It is crucial that we are heard if we are to continue playing our role as funders of the economy and to maintain the competitive status of European banks in the global economy.

GUIDO RAVOET

## ASSESSING THE IMPACT OF REGULATORY REFORM

The European Banking Federation has long been concerned about the overall impact of some proposals for regulatory reform. In the EBF newsletter n° 20 of November 2009, an article entitled 'More capital needs further assessment' drew attention to the trade-off between solvency and lending capacity of banks, which all stakeholders around the regulatory arena should carefully consider.

The Capital Requirements Impact Assessment Task Force (CRIA TF) of the EBF was created in November 2009 with the nomination of 20 members from EBF national banking associations. The task force was given a two-fold remit: firstly, to conduct an assessment of the new capital requirement for the European banking sector and secondly, to estimate the impact on the real economy.

The first work was delivered under quite ambitious deadlines. The CRIA TF deployed an assessment exercise with the participation of more than 60 banks and came up, by December 2009, with a rough estimate of the new capital required if all the new measures were put in place. The outcome informed us that the huge amount of new capital required by the proposals, of several hundred billions of euro, could hardly be raised quickly in the market. It is worth noting that since then the studies of several financial analyses have estimated the impact to be in the same range, thus reaffirming the initial findings of the EBF CRIA TF.

The intensive work of the CRIA TF in 2009 provided the EBF with three valuable outcomes: firstly, the size of the new capital injection required by the Basel Committee proposals, secondly, the qualitative analytical contributions of the CRIA TF members, which served as the starting point in configuring the EBF response to the Basel Committee consultation and, finally, a wide network of collaborators among our member associations and banks who will be in a position to assess the plausibility of the results of the calibration exercise that the Basel Committee is known to be developing as a whole.

The EBF has now moved forward with the assessment of the impact on the real economy in collaboration with the Institute of International Finance (IIF). This institution has developed an economic framework for the simulation of regulatory change scenarios in five building blocks (Canada, the Euro Area, Japan, the UK and the US). The Extended CRIA TF is tailoring the framework to the Euro Area – the largest banking system in the world. The objective is to gain better understanding and to assess from a different perspective, the likely effects of the measures on the economy.

In striving to meet the new stringent prudential requirements, banks will have three main ways to achieve compliance: to raise new capital, to retain profits and to cut risk weighted assets. They all point to an increase of the lending spreads to the private sector, thus reducing credit availability to households and businesses and, consequently, limiting the GDP growth. Our goal is to measure the range of the expected shift and to estimate the breach between the base scenario – with no change – and the regulatory change scenario. The outcome of the study will be published when finalised.

The assumptions of the model will be revised as long as new and more accurate information is received from different sources. Data availability permitting, future enhancements could include new regions in the scope of the study. All in all, the economic framework is intended to be a living tool to take on board fresh considerations as they arise.

*Gonzalo Gasós*



## FINDING THE RIGHT BALANCE FOR THE NEW BASEL FRAMEWORK

**In mid April 2010 the European Banking Federation submitted its response to the Consultation of the Basel Committee on Banking Supervision on: 'Strengthening the Resilience of the Banking Sector' and an 'International Framework for Liquidity Risk Measurement Standards and Monitoring'. Robert Priester, Head of Department, Wholesale and Regulatory Policy, summarises the positioning of the EBF.**

The EBF acknowledges that the capital base of the banking sector needs to be reinforced. However, resilience should not be based primarily on enhanced capital and liquidity requirements but, should first and foremost rely on improved risk management and internal governance practices, better regulation and improved supervision. Moreover, a right balance needs to be struck between bank resilience and economic recovery as: one cannot simply ignore the consequences which the whole range of proposed capital and liquidity measures - if they are approved as proposed - will have on the economy in general, and bank lending. It would, more particularly, be totally inappropriate to overlook those negative consequences by merely claiming that they will be outweighed by the benefits that enhanced financial stability are expected to bring .

Key concerns for the EBF as to the new definition of capital are (i) the proposed restrictive treatment of minority interests in subsidiaries within a consolidated group, (ii) the required deduction of deferred tax assets; (ii) the deduction of defined pension fund assets from the common equity component and finally, (iv) double counting of insurance holdings.

The Federation is extremely critical of the proposed liquidity ratios which, if they were to be implemented as proposed, may have a significant and negative impact on financial stability as well as on the economy. Moreover, those proposals made, contradict the main message which the Basel Committee had conveyed merely one year ago, i.e. that liquidity and funding risk management cannot boil down to merely applying a range of funding risk metrics. We agree that the proposed Coverage Ratio (LCR) covering the short-term liquidity may be a useful metric provided the LCR buffer includes central bank eligible assets. We are more critical and worried, by contrast, about what is being proposed concerning the long-term Net Stable Funding Ratio (NSFR), which needs to be reconsidered in a comprehensive way.

Furthermore, the counterparty risk involved in derivative transactions should be reassessed as their contribution to the effectiveness of the financial markets should not be ignored. In particular, the important role of over-the-counter (OTC) derivatives in offering efficient financial hedging to commercial transactions would be put at risk by the proposed measures. The EBF advocates placing incentives to the use of central counterparties (CCPs) without unreasonably penalising OTC derivatives, notably those linked to international commerce.

The EBF fiercely opposes, as a matter of principle, the proposed introduction of a leverage ratio. Whilst we support more stringent requirements in areas where the crisis has shown that risks were underestimated, we object to introducing a leverage restriction because such a measure is risk-insensitive by its very nature. It is particularly unfair that the most important victims of a leverage ratio will be banks that provide retail banking services and of which the lending portfolio mainly consists of well collateralised retail exposures carrying low risk which have in general been faring rather well during the crisis. A leverage ratio would be acceptable only if it were to be introduced within the Pillar II framework. Such an approach would enable supervisors to assess a bank's leverage in a more flexible way and, in particular, take into account each bank's business model and focus on how the ratio develops over time – which is likely to be a more relevant indicator than the (rather arbitrary) outcome of the ratio as such.

Although the Basel Committee is yet to elaborate further on the advisability of making systemically important financial institutions subject to specific constraints, the EBF believes that it is not size but other factors such as bad risk management and interconnectedness that have proven to pose risks of a systemic nature. Numerous regulatory remedies are already underway or are in place to address such systemic risks and need to be taken into account going forward.

The EBF sees a cogent need for a second consultation after the current calibration exercise by regulators. Despite the industry having dedicated huge resources to the analysis of the new proposals during the last months, the newness and complexity of the measures makes us think that further assessment is needed. Further to the quantitative impact study, more clarity would contribute enormously to the management of the expectations of market participants, rating agencies and the industry.

Transition periods and appropriate grandfathering of the existing stock of tier 1 capital should be provided for in order to allow for adaptation by banks to the new set of rules.

International coordination and synchronisation of the implementation of all these measures is indispensable. Regulatory arbitrage should be avoided and to that effect, all G20 countries should implement the package at the same time and under a homogeneous set of accounting standards.



## REGULATORY REFORM IN THE US IS MOVING FORWARD

Policy-makers and the financial services industry agree on this: international consistency of regulation is key for a successful reform of the financial markets. The European Banking Federation has long been a strong supporter of the G20 process and the work of the Financial Stability Board and the international standard-setting bodies. Of particular significance for European institutions are the developments in the United States: many European banks have subsidiaries or branches in the US, and vice versa. Also, institutions that are not directly represented in the US may on occasion become subject to US regulation, when dealing with US counterparties.

The EBF therefore closely monitors the regulatory developments in the United States. In doing so, it cooperates with the New York-based Institute of International Bankers, which represents the specific interests of non-US headquartered firms active in the US. In addition, the EBF maintains direct contacts with US policy-makers and supervisors. An EBF delegation visited Washington in December 2009 for a series of high-level meetings with the Treasury, Congress and supervisory agencies. Members of the EBF's Executive Committee are again meeting US policy-makers and supervisors in May, as part of a delegation of the International Banking Federation. Additional contacts regularly take place in Brussels.

These contacts serve in particular to highlight the potential effects of divergent regulatory approaches on internationally active banks. In addition, level playing field distortions may indirectly impact on regionally active banks. As a prominent example, the EBF has raised questions over the approach and timelines for the implementation of the Basel II and Basel III rules in the US. For the most part, the Basel rules do not need Congressional approval but can be implemented directly through the supervisory agencies. It is however still not entirely clear to which institutions they will apply, and from which point in time.

In other areas, coordination between the European Union and the United States has already led to close alignment. The respective regulatory proposals for Over-The-Counter derivatives, for example, have so far been marked by a high degree of consistency.

At this stage, the timetable and final outcome of the regulatory revamp in the US are however still open. The House of Representatives agreed on a set of comprehensive reform proposals last December, but discussions in the Senate have proven difficult. The main points of disagreement between Democrats and Republicans are of a primarily US-internal nature, in particular regarding supervisory structures. Nevertheless, there are strong indications that the two parties are now moving closer towards agreement within the Senate. Once a Senate bill is passed, it has to be reconciled with the House bill. In order to avoid additional political complications arising in the run-up to the mid-term elections in November, policy-makers aim to finalise this process before the summer recess.

*Uta Wassmuth*





## POST-TRADING IS TOP OF EUROPEAN AGENDA

Since the turn of the millennium, there have been numerous developments in the post-trading environment. Although the financial crisis has demonstrated how resilient global clearing and settlement systems and infrastructures were, regulatory pressure has not diminished. On the contrary, the financial crisis has given the legislator more incentives to closely look at the functioning of the financial system. Consequently, areas that were previously consigned to the back shop of public authorities are now regularly addressed by the main economic newspapers and give rise to numerous public conferences and seminars where practitioners rush searching for information.

From a regulatory perspective, clearing and settlement is now thus firmly on the agenda of the European institutions, both in Brussels and in Frankfurt. The European Commission is rushing to deliver, before the summer break, a draft proposal on a piece of legislation that is initially targeted to regulate over-the-counter (OTC) derivatives but will eventually encompass the governance of market infrastructures such as Central Clearing Counterparties (CCPs) and Trade Repositories (TRs), not only in the OTC area but also for other asset classes. Better known as EMIL (European Market Infrastructures Legislation) the proposal will be subject to a very short public consultation period, probably in July (see more detailed article on page 20).

Another proposed directive that will also have operational impact on intermediaries as part of the post-trading value chain, in the context of cross-border securities transactions, is the Securities Law Directive (SLD). Initially foreseen to follow a parallel route to EMIL – which has been prioritized by the Commission to materialize the commitment taken by the G-20 leaders and to meet the deadline of 2012 - the SLD will naturally include the Central Securities Depositories (CSDs), which have been taken out from EMIL despite a reference to this crucial market infrastructure in the first discussion paper from the Commission. It is currently unclear whether the SLD will address the role of CSDs in exercising the rights flowing from securities only or whether it will also encompass safety and soundness, similar to the requirements for CCPs in the context of EMIL. The SLD will be subject to a second public consultation next autumn. In this respect, collaboration is already taking place between the EBF Legal Committee and the Financial Market Committee, to bring together legal experts and experts from the operations.

Finally, the Target2-Securities (T2S) project is gathering momentum, even though the initial ‘go-live’ date of June 2013 will be postponed, possibly to the first quarter of 2014. This ambitious initiative, led by the European Central Bank, will create a single platform for settlement in Europe. The main objective of T2S is to reduce the cost of cross-border settlement, thus indirectly challenging some of the barriers identified in the Giovannini reports of the early 2000s. While T2S will benefit the intermediaries as end-users, it remains a public initiative owned by the ECB, thus with limited access in terms of influence on the decision-shaping and making. The European Banking Federation is closely working with its members to ensure banking institutions are well represented in the advisory body of the programme, so that they can bring their expertise and voice their concerns if not suggest practical solutions, as the settlement instructions are ultimately initiated by the banks.

## REMUNERATION POLICIES AFTER THE CRISIS

Still lingering, the global financial crisis has increased the focus on the compensation policies of financial institutions. European Banks have, however, learned from the crisis and are taking measures to regulate remuneration in the banking sector.

The European Banking Federation recently published a report entitled 'Remuneration Policies after the Crisis', which gives a country by country overview of the range of initiatives being put in place in most financial markets globally. The report has been put together by the EBF Task Force on Remuneration Policy and, it shows that the sector is moving in the right direction, as confirmed by the peer review report of the Financial Stability Board last March. Nevertheless, it is essential to maintain a level playing field and to ensure the competitiveness of Europe at global level.

A large variety of legislation and guidelines on remuneration have already been introduced, both by international and national institutions. Initiatives by individual financial institutions have also been introduced.

In the last year(s), banks have reviewed their policies, procedures and practices, and have taken measures whereby long-term and non-financial metrics and targets play an important role in diminishing behaviour perceived to be excessively risky. In this context, the European Banking Federation has strongly supported the principles of the Financial Stability Board (FSB), which could contribute to a level playing field across financial services, if implemented consistently and simultaneously.

The competitiveness of the European Union through a level playing field is a priority for the EBF, including with regard of remuneration policies. Non-G20 countries should also implement the FSB standards, especially those that are becoming significant financial centres.

In its report on remuneration, the EBF has included a comparative table which details the measures that have been taken by both international and national institutions.

The report shows that in their vast majority, banks support remuneration principles. Banks in Europe in particular support a principles-based approach towards remuneration policies with the aim of aligning remuneration policies to sound risk management.

Moreover, banks agree that measures should be taken to correct any existing misaligned incentives due to remuneration policies. They believe that their risk management should be aligned with their long-term objectives. Remuneration must not be excluded from the scope of risk management.

It is essential that firms are given the opportunity, as well as sufficient time, to implement changes to their reward practices that have been reviewed and evaluated over time, and which are appropriate to their business models, rather than implementing any short term changes that may inadvertently cause unintended consequences in the long-term.





*From left to right:*

*Sébastien de Brouwer, EBF  
Giancarlo Durante, ABI  
Fons Stoelinga, Ambassador of  
the Netherlands to Italy  
Enrico Granata, ABI  
Wim Mijs, NVB  
Elie Beyrouthy, EBF*

The EBF stresses the importance of a level playing field to preserve the competitiveness of the European Union.

Two different level playing fields have to be considered:

- First, at global level: there is fierce competition amongst financial centres; and regulation has become a competition tool (among others; tax law, labour law, softness of financial supervision). One of the purposes of the G20 group of nations should be to reiterate that even if the competition between financial centres is not blocked, some common principles need to be applied equally across the world.
- Second, the cross-sector level playing field: remuneration of risk takers is not only a banking issue but concerns also the entire asset management area (classical funds, pension funds, alternative and hedge funds) and insurers.

With the aim of a level playing field in mind, the FSB should monitor implementation going forward on an annual basis to ensure that all G20 members stick to their commitments.

Banks face numerous challenges in implementing Remuneration Principles. Notably :

#### **Subsidiaries and branches**

A potential concern is the rules that apply to internationally active firms. A case of double regulation could lead to a conflict of rules and/or an unnecessary burden on banks.

#### **Individual and collective labour agreements**

For many banks, the new initiatives alter the bank's existing remuneration policies. In view of the new initiatives, these differences could be problematic from a legal perspective.

Consequently, remuneration principles should only cover a very limited number of employees/risk takers and should only be taken from a corporate governance perspective.

The report - Remuneration after the crisis - can be found on the EBF website at [www.ebf-fbe.eu](http://www.ebf-fbe.eu)

*Elie Beyrouthy*



## MEPs EMBARK ON ADOPTING STRONGER EU SUPERVISORY REFORM PACKAGE THAN PROPOSED BY COMMISSION AND COUNCIL

Members of the European Parliament Economic and Monetary Affairs Committee (ECON) positioned themselves very clearly towards ambitious EU financial supervisory reforms by adopting on 10 May 2010, the Reports on a European Banking Authority (EBA), a European Securities and Markets authority (ESMA), a European Insurance Authority (EIOPA) and a European Systemic Risk Board (ESRB).

### A highly political context

The four main political parties (EPP, S&D, ALDE, Greens) supported the positions proposed in the draft Reports, thus sending a signal of parliamentary unity for ambitious reforms to the European Council and strengthening the European Parliament's position in inter-institutional negotiations. So-called 'trilogues' have now started between MEPs, the European Council and Commission to find a consensus between the co-legislators; but negotiations are likely to be tight.

MEPs have endorsed the framework proposed by the Commission and supported by the Council : creation of the ESRB for macro-level supervision and of three European Supervisory Authorities (EBA, ESMA and EIOPA) for micro-level supervision of financial institutions in tandem with national supervisors and colleges of supervisors for cross-border groups.

But the ECON Reports go beyond the red lines drawn by the Council by extending the scope of powers of the ESAs and reducing the room for Member States not to apply a decision by an ESA in situations of emergency and disagreement (see below for more details).

To achieve the initial goal of having the new Authorities set up in 2011, the legislative package should be put to a vote at the European Parliament's June plenary session for adoption at first reading.

### A quasi-umbrella supervisory authority?

The ECON Reports propose that the sectoral European Supervisory Authorities (EBA, ESMA and EIOPA) are located in Frankfurt with the European Central Bank (ECB) and the ESRB.

The three authorities would work together through a stronger Joint Committee, which would become a fourth European supervisory authority.

### Direct supervisory powers and two new funds

The adopted texts include a power to supervise directly systemically-important cross-border financial institutions, whereby national supervisors would act as agents of the EU authority. The Commission's proposal for a binding mediation power in the event of conflicts between national supervisors was also adopted.

Institutions directly supervised at EU level would be obliged to contribute to a European Deposit Guarantee Fund and a European Stability Fund. Contributions would be risk-based and both funds would be able to issue debt to boost their resources if needed. The European Stability Fund would provide private financing to resolve or to bail out one of these institutions if it ran into difficulties; the European Deposit Guarantee Fund would guarantee depositors' interests. A Resolution Unit within each sectoral Authority would be responsible for the crisis management and resolution of ailing systemically-important cross-border financial institutions.

Particularly relevant for ESMA, the ECON Reports provide for the possibility to impose temporary bans on very risky financial products. ESMA would also be expected to advise on the supervision and regulation of credit rating agencies and clearing houses.

### Additional powers

As proposed by the Commission, the EBA, ESMA and EIOPA would be empowered to draw up draft technical standards, which could then be made legally binding by the European Commission, thereby creating a single rulebook.

The European Supervisory Authorities would also have the power to address decisions with legal effect to national authorities and, *in extremis*, to individual financial institutions to ensure (i) compliance with EU laws and (ii) action is taken to address an emergency situation.

## EBF Members call for an improved supervisory framework as of 2011

The EBF has long been a strong advocate of the reform of the organisation of supervision in Europe, and indeed expressed its strong support to the European Commission proposals.


Furthermore, the Federation has lobbied MEPs in favour of an evolutionary approach to reforming the supervisory framework in Europe in a bid to adequately address the political, legal and practical challenges that are associated to this type of fundamental reform.

Members of the ECON Committee have nevertheless set high ambitions, which might be premature both technically and politically. The EBF agrees that 'more Europe' is called for, but the Commission seems to have arrived at the right tone with its proposals.

The main concern of the European Banking Federation at this stage is therefore that the important differences in objectives between the Council and MEPs will jeopardize the timely adoption of the Proposals and therefore the implementation of an enhanced, efficient and sufficiently strong European supervisory framework as of 2011.

For EBF Members, an improved supervisory framework will indeed be instrumental to ensure the upcoming regulations are applied correctly and consistently to produce their full effects and preserve fair competition.

*Noémie Francheterre*



ECON reduces the latitude for a Member State to invoke the 'safeguard clause' whereby it may not implement a decision of one of the European Supervisory Authorities if it considers that the decision impacts on its fiscal responsibilities. The Member State would be required to provide an assessment of how the Authority's decision creates budgetary problems for it. The European Commission would also be required, after three years, to evaluate the use of the safeguard clause.

The ECON Reports would grant the EBA, ESMA and EIOPA new powers to conduct together with the ESRB stress tests on financial institutions. The EBA would also be specifically empowered to evaluate the accessibility, availability and cost of credit to households and small and medium-sized enterprises.

### **European Systemic Risk Board: a greater role in risk assessment**

The ECON text makes provisions for the ESRB to be chaired by the President of the ECB and that it should be empowered not only to warn of a risk building-up (as proposed by the Commission), but also to declare the existence of emergency situations

As proposed by the Commission, the ESRB would not have a legal personality.

The ESRB should also develop a common set of indicators to assess the risk profile of cross-border financial institutions and thus determine which cross-border institution should be supervised directly by the ESA (see above). ECON furthermore calls for the ESRB to establish colour-coded grades to reflect different risk levels. The colour grade should then determine the level of risk in a warning or recommendation by the ESRB.

## CUSTOMER MOBILITY – THE EBIC COMMON PRINCIPLES ON BANK ACCOUNT SWITCHING

Since 1 May 2010 the Common Principles on Bank Account Switching have passed the half-way point between national implementation and the review process.

The Principles on Bank Account Switching were elaborated by the European Banking Industry Committee (EBIC) in 2008. These Principles, which are designed to facilitate domestic current account switching, create a common benchmark for increasing customer mobility in the European Union.

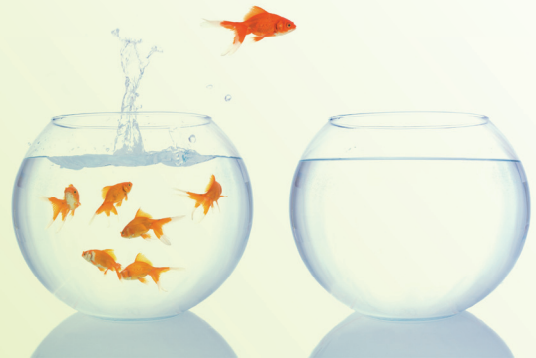
Further, the Common Principles ensure that bank account switching is not onerous for the consumer and that mobility is not constrained by unnecessary delay or cost; or by a lack of support from banks. They are also increasing the consumer's awareness of switching-related services and are expected to reduce consumer apprehension with regard to bank account switching.

With an official implementation date of 1 November 2009, the Principles have now been implemented in all 27 Member States. The legal instruments used for implementation at national level take the form of industry codes, recommendations, guidelines or legislation.

To ensure transparency and accessibility, the EBIC Integration Working Group, under the leadership of the EBF (and chaired by Enrico Granata from ABI), has prepared an 'Implementation Report on the Common Principles'. The report aims to provide an overview of certain aspects of national adaptation and provides some additional and explanatory information. Accordingly, it covers the processes foreseen at national level for:

- Information on switching
- Banks' support in the switching process
- Facilitation of switching
- Implementation
- Monitoring

In addition the report includes more detailed information on the national information campaigns, conducted ahead of the implementation date, as well as references to the online versions of the national adaptations of the Common Principles.



Furthermore, as of June 2010, the report will be enhanced by a section which refers consumers to alternative dispute resolution schemes available in their country, which could be addressed in a case of complaint. The said table is available online both on the EBIC and EBF website.

Through on-going dialogue with the European Commission and the European Consumer Association, BEUC (Bureau Européen des Unions de Consommateurs) the representative view of other stakeholders on this issue is ensured. A review of the Common Principles by the European Banking Industry Committee is envisaged for November 2010. Until then, a first evaluation will be undertaken at national levels, the results of which will be gathered by EBIC. The European Commission has also declared its intention to launch a monitoring exercise in 2010 to complement the industry evaluation.

The success of the exercise is considered a hallmark for self-regulation in retail financial services. The European Banking Federation has closely followed the previous achievements and is fully committed to ensuring that the implementation at national level is appropriately reflected in practice.

*Alexa Steinmetz*



# TOWARDS A EUROPEAN RETAIL FINANCIAL SERVICES MARKET

The European Banking Federation will shortly publish a report which maps the Federation's vision for further integration of retail financial services in Europe.

The report was produced by the Consumer Affairs Committee, chaired by Eric Leenders at the request of EBF Executive Committee. It sets out the Federation's position and policy strategies vis-à-vis current retail financial services issues.

Aimed at outlining the EBF's retail priorities and establishing the areas in which a more (pro)-active attitude should be adopted, a clear image on how the creation of a competitive, single European market can be advanced is created. At the emerging signs of economic recovery, bearing in mind that the restoration of trust in the banking industry must be driven by sound and sustainable banking practices, the EBF also considers the role of the European institutions in this process.

A strong supporter of the vision of an integrated European retail financial services market, the document also establishes EBF's strategic view on the progress in the creation of this market, in particular in a post-crisis environment.

Both horizontal, as well as specific issues are considered. Notably, topical issues such as potential initiatives announced in the area of responsible lending and borrowing, product tying, packaged retail investment products (PRIP's) and financial inclusion are covered; but also industry initiatives, such as the Single European Payments Area (SEPA) and the EBIC Common Principles on Bank Account Switching are mentioned. Further, comments on existing pieces of legislation, such as the Consumer Credit Directive and the Distance Marketing of Financial Services Directive, are incorporated.

The document generally highlights the Federations policy focus and goes hand in hand with the creation of a specific page dedicated to consumers – 'Banks & Consumers' on EBF website – [www.ebf-fbe.eu](http://www.ebf-fbe.eu) – with the possibility of serving as a basis for further enhancing the dialogue between the stakeholders on relevant issues.

*Alexa Steinmetz  
Sébastien de Brouwer*



## EBF TURNS 50

# EBF 50th Anniversary

On 4 February 2010, the European banking Federation launched its 50th Anniversary.

The year will be marked by a number of events which will help reinforce the visibility of the Federation, and the dialogue between the Federation and all stakeholders in the field of financial services, be they policy makers, regulators or representatives of other industry and civil society sectors.

A panel debate, followed by a press conference, marked the occasion. Alessandro Profumo, President of the EBF and CEO of Unicredit, seized the opportunity to stress the legitimacy of the Federation as the European banking sector's representative, including – and particularly - in difficult times.

The panel was very well attended by representatives from all sides of the financial services spectrum and interested parties, focused on supervisory issues, and crisis resolution and prevention mechanisms. Members of the panel included Eddy Wymeersch, Chairman of CESR (Committee of European Securities Regulators), Burkhard Balz, Member of the European Parliament, and David Wright, Deputy Director General, Internal Market, European Commission.

On this occasion, the EBF launched its nine principles for a successful future of banking in Europe', in which it highlights the industry's recommendations to standard setters and decision-makers at this crucial time; presenting a set of principles which, if followed, should help to promote the health, safety and vitality of EU banking in the coming years.



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1. Alessandro profumo, president of EBF & CEO of Unicredit

2. From left to right: Burkhard Balz, member of the European Parliament; Alessandro Profumo; David Wright, Deputy Director General, DG Markt, European Commission; Eddy Wymeersch, Chairman of the Committee of European Securities Regulators.

*EBF - 50 Years of Sound Banking Representation*



## EBF REINFORCES PRESS RELATIONS

Relations between EBF and the press and media were further reinforced earlier this year when communications staff held a press lunch for a handful of selected journalists from the Brussels press corps.

The lunch took place in one of the restaurants at the Residence Palace, Brussels, which is an administrative centre where a number of journalists have their offices.

Chair of EBF Executive Committee, Ariane Obolensky, welcomed journalists and outlined the EBF's recent publication 'Principles for the Successful Future of European Banking', before opening the floor to questions, which she answered together with EBF Secretary General Guido Ravoet.

This exercise was the first of its kind for the EBF and was aimed at establishing a more regular and more systematic contact between representatives of the banking sector and the press.

Ariane Obolensky, who is also CEO of the French Banking Federation, declared: "The main objective was to give journalists background information and a better grasp of current issues facing the sector. And judging from the follow-up in the press, this objective was certainly reached."

It was a communications initiative, she said, which should "definitely be repeated."





# LIFE UNDER THE PSD

## THE STORY SO FAR

The Payment Services Directive (PSD) is still being implemented across the European Economic Area (EEA); we will take a look at practical experiences in the market since 1 November 2009 and examine the ongoing activity of the banking industry's PSD Expert Group, as established by the EBF in 2007.

### Implementation Update and Practical Experiences

All 30 countries of the EEA were required to have implemented the requirements of the PSD into their national legislation by 1 November 2009. To-date, this implementation remains outstanding in four countries, all of which hope to complete the task by the end of 2010: Sweden (target 1 July), Greece (target Q3/Q4), Poland (target Q4), Iceland (target Q4).

Meanwhile, banks and their clients are continuing to have to cope with the fact that differing legal regimes remain in place, albeit in the case of Sweden the impact has been reduced by the positive industry initiative to adopt a number of core PSD principles in advance of transposition (in line with the PSD Expert Group's recommended approach).

In the few months since the PSD went live in most EEA countries, a number of practical issues have emerged as banks and others have started to put their new processes into action. It is too early to say for sure which of these are a lasting trend and which are temporary 'teething problems' as banks and their clients adjust to the new environment. However, several issues which started emerging in the first month after the PSD went live are still being experienced in some cases, such as:

- Inconsistent usage - and handling - of charging options due to differing interpretations of the PSD's requirements.
- Significant and/or unexpected deductions/lifting fees applied by beneficiary banks without seemingly having agreed such deductions in advance with their customers.
- New 'non-STP'<sup>1</sup> fees and 'SHA-claims'<sup>2</sup> being levied by some beneficiary banks, along with some confusion concerning post-PSD interbank charging principles in the intermediary bank space.



## Next steps of the PSD Expert Group

Whatever the real explanation behind such issues, it is clear that continued dialogue within the banking industry at a European level to promote common interpretations of key PSD principles, identify best practices and ensure a positive and consistent end-customer experience remains critical.

One of the original objectives of the PSD Expert Group (PSD EG) was to record and formulate practical PSD implementation guidance for banks based on the outcome of the PSD EG's constructive dialogue with the European Commission Services and national authorities. This was initially achieved by the publication of Version 1.0 of the document 'PSD Guidance for the Implementation of the Payment Services Directive' in August 2009.

Since November 2009, the PSD EG has continued to be active, monitoring closely the ongoing implementation process across EU/EEA Member States and engaging in identifying solutions to issues emerging in the market as a consequence of the PSD going live, such as the examples highlighted above. To this end, the PSD EG has just finalised an addendum to Version 1.0 of the Guidance Document. The goals of this addendum are to:

- Reinforce core PSD concepts and scope where there is evidence pointing to a lack of consistent understanding.
- Reiterate and where necessary elaborate on existing market best practice with regard to various PSD-related topics
- Provide the results of the PSD EG's work to collate an overview of derogation usage and gold-plating on a country-by-country basis.

To give an example of the contents of the addendum, on the topic of the continuing confusion surrounding the use of charging options, the PSD EG is looking to propose as a best practice that SHA should be seen as the default approach for all payments falling under the PSD, even where there is a currency exchange (thus mirroring the forward-looking approach adopted in the SEPA schemes on this point).

Additionally, it is proposed that it would be appropriate for banks to provide a 'health warning' to their payers in cases where the OUR option is still being offered as deductions on the beneficiary side cannot be guaranteed to be excluded.

In terms of the next area of focus for the PSD EG's work, it has become clear that certain pre-PSD interbank principles and conventions, whilst no longer valid, are still being cited by banks in some cases. Accordingly, the intention is for the European banking industry to shortly establish a new work stream, leveraging the broad representation of the PSD EG, with a view to reviewing these conventions in the context of the PSD and Regulation 924/2009 now being in force and potentially defining a revised set of high level inter-bank principles to take their place as necessary.



Ruth Wandhöfer  
Chair, PSD Expert Group  
Head of Payments Strategy & Market  
Policy, EMEA, Citi Global Transaction  
Services

<sup>1</sup>non-STP: non Straight-Through-Processing;  
<sup>2</sup> SHA-claims: "sharing", i.e. both sender and beneficiary pay charges to their respective bank

## TYING, BUNDLING AND OTHER COMMERCIAL PRACTICES UNDER SCRUTINY

On 18 January 2010 a study launched by the European Commission on the impact of tying and other commercial practices on customer mobility was published and submitted to public consultation until 14 April. As announced in the 2007 White Paper on Integration of Mortgage Credit Markets in the EU, following the results of the Retail Banking Sector Inquiry, this study was due to analyse the usage of various selling practices and their effects on consumers, from both a quantitative and a qualitative point of view.

The study identified a number of selling practices based on the assumption that, insofar as they bind consumers to a particular financial services provider, they may restrict mobility and thus competition. By covering the sectors of banking, insurance and investment services, the authors tried to assess the spread of tying and other practices across the EU-27 as well as their potential effect in terms of foreclosure of competitors and unfairness towards customers.

The study defines ‘tying’ as the practice whereby two or more products are sold together in a package (e.g. a mortgage loan and a life-insurance) and at least one of these products is not sold separately, while ‘bundling’ is described as selling two or more products together although each of them can also be purchased separately on the market (e.g. a consumer credit and a current account). To tying and bundling (jointly ‘cross-selling practices’), the authors of the study associate also ‘conditional sales’ where either the purchase is submitted to an action undertaken by the customer (e.g. having the salary paid into an account with the provider) or the provision of better contractual conditions to existing customers are subject to their specific behaviour (e.g. allowing variable fees on a credit card depending on the level of usage). A number of ‘aggressive commercial strategies’ as unsolicited offers are also covered by the study.

In the cost-benefit analysis of the practices under scrutiny, the study concludes by stressing both the potential unfairness and anti-competitive nature of cross-selling practices, but benefits like the quality of service and comprehensive advice are neglected. This disregards the ‘natural’ trend towards long-term bank-customer relationships due to the fact that financial services are not merely a matter of price but also of quality.

The European Banking Federation is of the opinion that the practices under scrutiny, with the exception of aggressive commercial strategies, are not per se detrimental to consumers and/or competitors in the retail financial services market. Only a case-by-case approach can allow a correct assessment of any anti-competitive nature and/or unfairness vis-à-vis consumers. A more balanced assessment is necessary including the benefits that exist for both providers and consumers.

The EBF believes that the study’s methodology does not allow a comprehensive and correct picture of the market to be delivered. On the other hand, the assumption inferred from the 2007 Retail Banking Sector Inquiry that the low level of switching in the internal market would conclusively demonstrate the existence of barriers and potentially abusive behaviour by financial services providers vis-à-vis consumers is not supported by evidence. The switching level should not be taken (in isolation) as a mere parameter of lack of consumer choice, rather it is mainly an indicator of customer satisfaction.

In the EBF’s opinion, the existing (hard and soft) legal framework, both at national and EU level, does provide sufficient protection to consumers as long as comparable, understandable and complete – but not overwhelming – information is provided to them. In particular, the Unfair Commercial Practices and the Unfair Terms Directives have been conceived as flexible tools and are already adequate to deal with situations where consumers are unfairly or misleadingly deprived of free choice or where anti-competitive situations arise, so that any further layer added at EU level at this stage does not appear justified.

The EBF has consistently argued in favour of ensuring a level playing field in the retail financial services market. However, the industry does not agree that product tying and bundling is an area where a level playing field is under threat.

*Arianna Mellini Sforza*



## EBF IS HAPPY TO SUPPORT THE 8TH EUROPEAN BUSINESS SUMMIT: PUTTING EUROPE BACK ON TRACK

The European Business Summit (EBS) is organised by BUSINESSEUROPE and the Federation of Enterprises in Belgium, in close cooperation with the European Commission and the EU Presidency. After seven editions, the EBS has truly become Europe's key meeting place for business leaders and decision makers.

With the theme 'Putting Europe back on Track', more than 100 speakers will debate how to build a more competitive and sustainable European Union. Annually, the EBS attracts 2 500 participants including CEOs & Top Executives, (Prime) Ministers, European Commissioners and media.

The two plenary sessions, the President's Debate and the twelve interactive sessions of this EBS will focus on topics such as economic recovery, financial regulation, trade for growth, the place of Europe in the world, new skills for new jobs, climate change and energy, innovation, clean-tech, Europe's digital agenda and the future shape of the EU's socio-economic model.

This year's edition will be more innovative and more interactive. A major novelty is that the EBS 2010 will present a CEO Survey collecting the views of business leaders on what Europe needs to get back on track. The 2010 EBS wants more than ever to contribute to new and sustainable growth in Europe.

We are looking forward to meeting you on Wednesday 30 June & Thursday 1 July 2010 at TOUR & TAXIS in Brussels, Capital of Europe!



▶▶ THE EUROPEAN  
BUSINESS SUMMIT



## EBF IDENTIFIES CENTRAL QUESTIONS FOR THE MiFID REVIEW

In 2007 when banks were in the process of implementing the new Markets in Financial Instruments Directive (MiFID), compliance officers took some comfort from the thought that this major work effort would be followed by a few years of regulatory stability. Three years on, work in the European Commission is sufficiently advanced to already propose a review of MiFID.

Inspired by experiences from the financial crisis and by general market developments, the Commission has (re-)opened a large number of questions to prepare legislative proposals by the end of 2010 or in early 2011. It held a series of workshops over last December and January to collect evidence on the functioning of the markets. Issues that were considered in these workshops include transparency of the non-equities markets; dark pools and broker-dealers' crossing networks; best execution and conduct of business requirements; and the functioning of data consolidation for cash equities. These issues came in addition to a range of others which the Committee of European Securities Regulators (CESR) had already put under the microscope, such as the definition of non-complex products.

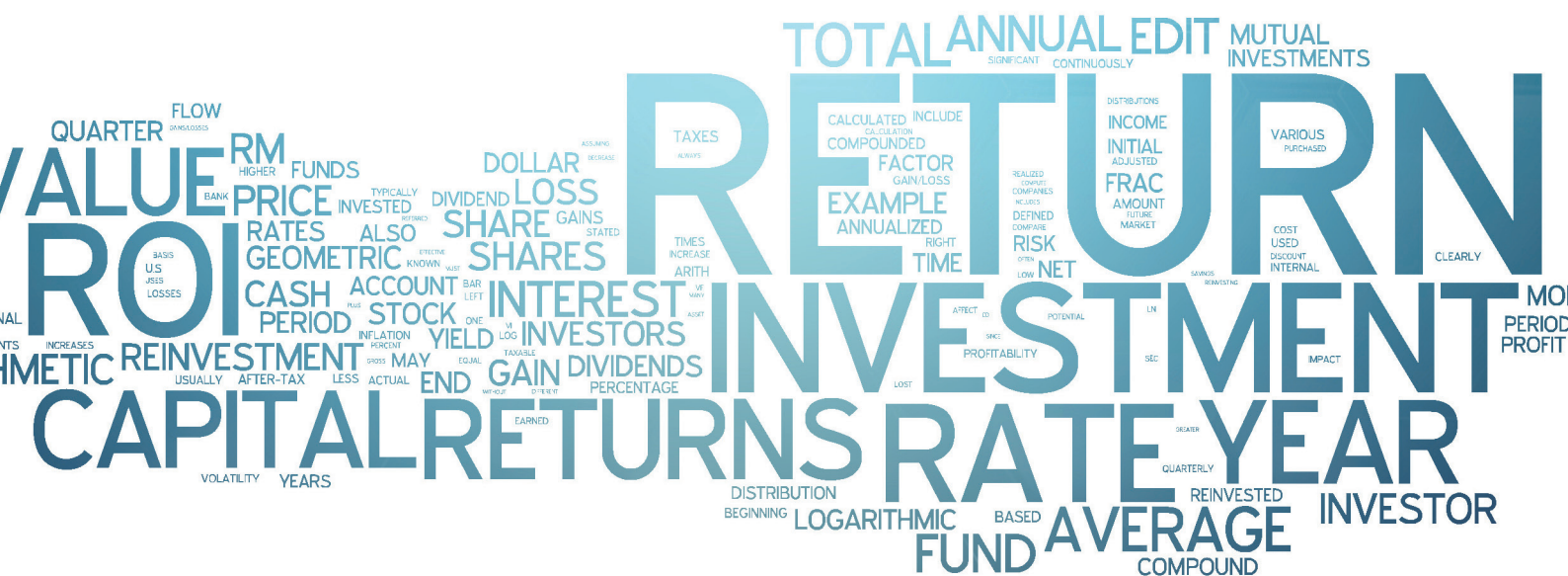
The European Banking Federation decided to review, for its part, all of these areas in a comprehensive manner. Over February and March, it held intense discussions within its Securities Working Group to identify the extent to which the questions brought up in the Commission workshops and other aspects of MiFID were perceived as problematic by banks.

Overall, these discussions confirmed banks' generally positive views of MiFID. Banks continue to believe that MiFID is the right regulatory framework and that it has generated important improvements in the functioning of the European equity markets. This is in particular with respect to the often-cited competition between trading venues. But positive evaluations were also made for other areas, such as the MiFID requirements in the field of investor protection.

The general view therefore was clear: modifications of the MiFID rules should be well-targeted and are only warranted in a limited number of areas. EBF members also agreed, however, on one key area where improvements are urgently needed. Post-trade transparency for cash equities is not working effectively. Steps must be taken to improve both the quality and the comparability of data. In a first instance, improvements should be sought through a combination of different measures such as the standardisation of reporting formats and possibly, the concentration of reporting venues. Only if these measures do not prove sufficient should further-reaching intervention be considered, such as the proposal of a publicly-sponsored consolidated tape.

CESR is currently working on a number of pieces of advice to the European Commission, on which the EBF is also providing input. The Commission plans industry consultation for the second half of the year.

*Uta Wassmuth*



## ALTERNATIVE INVESTMENT FUND MANAGERS: NEGOTIATIONS ARE PROGRESSING

Important progress has been made, over the past few months, in the negotiations of the proposed Directive on Alternative Investment Fund Managers (AIFMD). The Council held intense discussions first, in the second half of last year, under the Swedish Presidency, and then under the current Spanish Presidency. By March, near-agreement had been reached on most issues. These included in particular: to retain a broad scope of the Directive, covering a wide range of funds including hedge funds, private equity funds, real estate funds, and others, with an option for Member States to exempt small funds from most of the Directive's requirements; minimum capital requirements, depending on the fund's activities; stringent conduct of business requirements; requirements for sound remuneration policies; an independent risk management function; independent valuation; and extensive transparency obligations. In comparison with the European Commission's initial text, the industry generally considered these draft provisions a great improvement, especially in terms of practicability and legal clarity. The EBF particularly welcomes the clarifications made to the depositary requirements, even though a few questions remain open.

The Council nevertheless decided to delay the vote on the draft text in order to further review some parts of the text. This concerned especially the third country aspects, dealing with funds and fund managers located outside the European Union. Concerns had been voiced both from some Member States and non-EU countries that the respective draft requirements were overly restrictive.

In the European Parliament, the great interest in the AIFMD was evidenced by the almost 1700 amendment proposals. The rapporteur, Jean-Paul Gauzès, made a range of compromise proposals early April, which were generally perceived as well-balanced. Nevertheless, the EBF underlined remaining concerns around the proposed depositary requirements, especially with regard to liability arrangements. More generally, the EBF pointed out that work in the European Commission to make proposals for depositary obligations under the Directive on Undertakings for Collective Investments in Transferable Securities (UCITS) is currently ongoing. Rather than proposing to align the respective UCITS provisions with the AIFMD, flexibility should be allowed so that the conclusions of the Commission's work can be considered in the context of the AIFMD.

Votes in both the Economic and Finance Ministers Council and the Parliament's Economic and Monetary Affairs Committee are expected for mid-May.

*Uta Wassmuth*



## AWAITING PROPOSALS ON OTC DERIVATIVES MARKET INFRASTRUCTURES

Last October, the European Commission announced its future policy actions in the area of OTC derivatives. Three major pieces of legislation will be used to regulate OTC derivatives markets: (i) the Market in Financial Instruments Directive, MiFID; (ii) the Capital Requirements Directive; and (iii) the new proposals on Market Infrastructures.

With regard to MiFID, the Committee for European Securities Regulators (CESR) has started assessing whether greater price transparency for OTC derivatives might improve the resilience of the financial system and improve market efficiency. The outcome of this assessment will be factored in the Commission's proposals for the MiFID review that will be released by the end of 2010 or in early 2011 (see related article on page 18).

In the area of capital requirements, both the Basel Committee and the European Commission have just concluded a consultation on, among other things, the treatment of counterparty risk. The European Commission is considering the introduction of a clearer differentiation between capital requirements for CCP-cleared OTC derivatives contracts and others.

However, it is the area of Market Infrastructures where reform of OTC derivatives markets will be more profoundly felt. The introduction of clearing obligations for eligible OTC derivatives contracts and the regulation of the infrastructures operating in the market - central counterparties and trade repositories - is seen as the cornerstone to the proposals to make OTC derivatives markets more efficient, safer and sounder. Importantly, these proposals will not only cover OTC derivatives markets only but all securities business.

There is a joke in Brussels about the future European Market Infrastructures Legislation being referred to as EMIL, thus coinciding with the first name of the official in charge of this project in the Commission, Emil Paulis, Director for Financial Services Policy. Mr Paulis himself has jokingly declared that any resemblance should be considered as a measure of the high importance the Commission attaches to these proposals.

Indeed, the European Commission has worked very hard over the past few months to ensure that the European legislators are aligned to its policy thinking and that no significant divergences surface once the proposals are made public. Exchanges of views have regularly taken place with Member States within an ad hoc Derivatives and Market Infrastructures Working Group. Background papers have been produced for each of these meetings, covering essential aspects of the upcoming proposals such as clearing obligations for market participants and specifically for end-users, the treatment of foreign exchange derivatives, organisational requirements for Central Clearing Counterparties (CCPs), CCPs' authorisation and supervision, registration and oversight of trade repositories, etc.

With the Parliament, cross-fertilisation of ideas is clearly distinguishable in many of the amendments introduced to the own initiative report on OTC derivatives prepared by Dr Werner Langen (Member of the European People's Party, German) and that is about to be voted at the time of writing.

The EBF has closely monitored all these processes and actively participated in the presentation of amendments to the Parliament report. Views have also been exchanged more informally with Member States and the Commission. The EBF considers that, whilst acknowledging the benefits of CCP-clearing, no legal obligation to clear through CCPs should exist. The EBF also favours broadening the policy debate by highlighting other complementary alternatives for effective counterparty risk management, such as the strengthening of the legal security of bilateral credit risk reduction mechanisms (basically close-out netting and collateralisation).

Irrespective of the final tone and content of the proposals, a pressing concern is that the Commission, despite having extensively consulted with other EU institutions, is planning to only hold a brief open consultation sometime in June. This is sending a very strong but negative message to market practitioners: your views to guide regulatory action are not necessarily welcomed this time round. In fact, it seems that the proposals are already very much advanced (there is talk that the number of articles is in the 60 + area).

Against that background, the EBF is about to finalise a paper on the upcoming proposals on the European Market Infrastructures. The paper has been consulted extensively with members of the EBF's Joint Focus Group on OTC Derivatives and Market Infrastructures and is expected to be released by early June

*Enrique Velázquez*

# EURIBOR-EBF: AN OPERATIONAL MARKET STANDARDIZATION ARM OF THE EBF

Created in 1998, Euribor-EBF is a nonprofit organization, with both analytical and regulatory aims.

**Analytical:** To guarantee the development and support of market benchmarks activities such as EURIBOR, the EONIA and EONIA SWAP indices and EUREPO. These activities include keeping the benchmarks as accurate as possible, developing their visibility on the market, licensing those protected trademarks, answering market and institutions queries, and finally, reporting the relevant data to interested parties. The crisis has proved that Euribor is the reference in the world regarding the euro money markets, even used by the European Central Bank (ECB) to monitor its re-financing current operations.

**Regulatory:** To ensure the development of the STEP (Short Term European commercial Paper) programme, initiated in 2006 by both the ECB and Euribor-EBF/Euribor-ACI to standardize the Short Term Commercial Paper market. STEP is one of the leading European programmes for market transparency, with an outstanding amount of 404 Billion Euros to date. The STEP market Secretariat administrates the STEP label jointly with the ECB and National Central banks, providing the market with a common standard and a high level of transparency, enabling investors to limit their risk exposure and corporate companies to find treasury capacity on the market . In other words, STEP finances the real economy.

The STEP programme and Euribor-EBF benchmarks have taken such an important place in the financial markets' community that they have become a reference many seek inspiration from.

The Euribor-EBF strategy in the coming years will consist in finding the best types of organization and process to bring the highest level of service to its members, to the market and to the European Institutions.

*Cédric Quemener*



## EBF PROPOSES AN ALTERNATIVE IMPAIRMENT MODEL

In November 2009 the IASB (International Accounting Standard Board) issued an Exposure Draft (ED) on impairment of financial instruments as part of their wider project on IAS 39 replacement. The Impairment proposal applies to financial assets measured at amortized costs.

The IASB expected cash flow model would pose significant operational challenges due to its complexity and would require significant time and costs to implement due to the need to revise the methodology for the Effective Interest Rate (EIR) and define expected Cash Flows (CF) by time period whereas entities manage expected losses (EL).

The EBF, concerned with conceptual and operational difficulties of the IASB model has developed an alternative application of the concept of expected loss which is consistent with the general objective of financial statements, the objectives of the ED and reflects lending activities and credit risk management practices of financial institutions.

The IASB model mixes interest rate risk and credit risk in the calculation of the Effective Interest Rate (EIR). The model is based on the presumption that it is possible to accurately estimate the timing of future losses over several years. It treats initial expectations of future credit losses as if they resulted from contractual terms, whereas they actually result from a failure to comply with contractual terms. Separate methodologies for the recognition and presentation of interest income on the one hand and credit losses on the other would provide more useful information.

The EBF model does not change the calculation of the EIR, nor does it change the definition of amortized cost. The current calculation of EIR is based on identified and known components while the Expected Loss is a calculation of estimated future credit losses. It would be difficult for users to understand expected losses if these have been embedded into the EIR calculation, which as a result lacks relevance. The EBF model therefore keeps the current definition of the EIR under IAS 39, excludes the expected loss from the EIR calculations and shows it separately as an impairment expense.

The IASB proposed methodology is applied to individual loans or closed portfolios. The EBF methodology reflects the way portfolios are managed and is suitable for application on open portfolios where existing loans mature and new loans are added to the portfolio. The size and nature of portfolios may vary within and between entities, but it should however reflect the entity's business model for managing financial assets. The methodology is based on the Expected Loss over the Life of the Portfolio (ELLP), aggregating the future expected losses of each specified portfolio. The life of the portfolio is the average maturity of the loans in the portfolio weighted by the outstanding balance.

The ELLP is the measurement of the loss expected within a period, based on historical loss experience for assets with similar risk characteristics, which are adjusted first to reflect the effects of conditions that did not affect the period on which the historical loss experience is based and secondly, to remove the effects of conditions in the historical period that do not exist anymore at the reporting date. Entities that have no loss experience of their own (or insufficient experience) should use peer group experience for comparable groups of financial asset.

The ELLP should be spread in the Income Statement over the average life of the portfolio and reviewed and recalculated periodically at each reporting period to reflect adjustments due to the changes in the current or expected credit risk conditions and changes in the composition of portfolios

The IASB model introduces an artificial distinction in the accounting treatment of initial expectations and changes in those expectations increasing the degree of subjectivity and volatility into the recognition of interest income. There is no conceptual difference that would justify the significant difference in treatment between the initial expectations and subsequent revisions in expected losses. Full recognition in Profit & Loss (P&L) of the effect of changes in loss expectations in the period of the change creates a higher level of P&L volatility. This higher level is not justified by the economic impact of changes in expectations, because relatively small changes in expectations will have a much greater impact in the period of change than the initial loss estimation. It represents a recognition model that is highly volatile and sensitive to changes in economic conditions, a criticism which has been made of the incurred loss model.



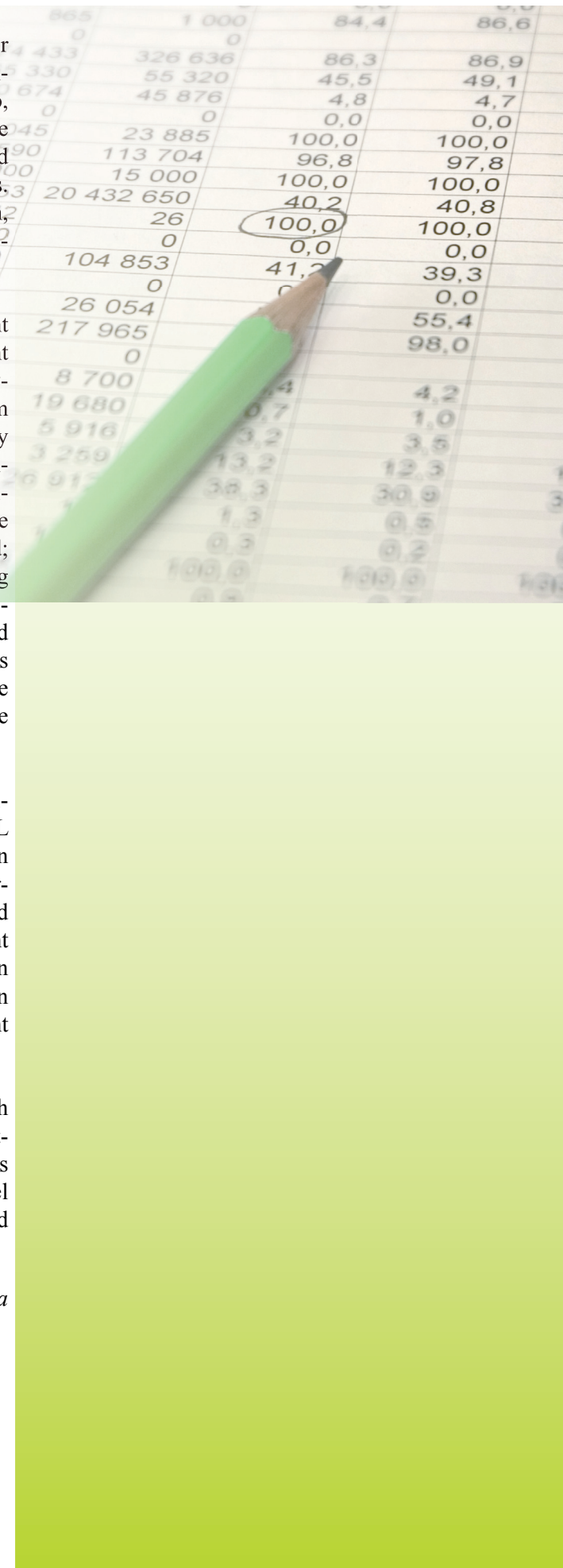
Therefore in the EBF model, all expected losses, whether initial or subsequent estimates, are recognised in the income statement through the average life of the portfolio, as is income on the portfolio. This is consistent with the principle that revenue from financial assets at amortised cost should be recognised over the life of the instruments. The EBF model results in more comparable information, because changes in expectations are recognised prospectively.

Individually impaired loans are treated as in the current IAS 39, keeping the current definition of impairment and the methodology to calculate the impairment allowance. When a loan is impaired, it is distinguished from the performing portfolio and assigned with the necessary provision from the stock previously created. The remaining portfolio will continue to build up an impairment allowance based on the ELLP over the residual life of the portfolio. Impairment allowances are built to be used; therefore incurred losses are booked against existing impairment allowances. Any subsequent increase or decrease in incurred losses is booked against the expected loss impairment allowance account. When expected loss allowance is not sufficient to absorb incurred losses, the deficit in incurred losses is booked directly on the income statement.

It is not possible to have a negative EL impairment allowance account. The overall impairment allowance (EL + Incurred loss) is as a minimum equal to or higher than the incurred loss impairment allowance under the current IAS 39 model and as a maximum equal to expected loss of the portfolio plus the incurred loss impairment allowances under the IAS 39. If a non performing loan becomes performing again, it will be re-incorporated in the portfolio together with its corresponding impairment allowance.

The ELLP model developed by the industry is in line with the G20 objectives and the Bank for International Settlement's six principles to achieve sound expected loss provisioning. At the same time, it is believed, the model is easier for users of financial information to understand and for preparers to implement at reasonable costs.

*Denisa Mularova*



## MICROFINANCE WITHIN THE EU BANKING INDUSTRY: POLICY AND PRACTICE - AN EBF REPORT

Within the European Union private banks are among the main providers of microfinance. The EBF report focuses on the microfinance which EU banks are making available to borrowers within its borders. On the basis of observations on the commercial market for microfinance, conclusions are drawn as to the appropriate framework at EU level to accommodate diverse approaches and allow public and private supply to co-exist healthily.

Across the EU banking industry, microfinance usually refers to small loans ('microcredit' or 'micro-loans') and small commercial customers ('micro-entities'). The European Commission defines microcredit in the EU as loans under EUR 25,000 for business initiatives. Yet the lack of a consistent and commonly used definition of microfinance for banks' internal reporting impedes the collection of information on the activity. Reliable facts and figures for the volume of microcredit and related services, particularly for the EU as a whole, are elusive. Despite this, existing country-level data illustrates the diversity of national practices.

Banks' strategic approach to microfinance across the European Union is varied. A main point of difference is the extent to which the business is seen to be driven by economic and/or social objectives. Much microfinance from EU banks is undertaken in the context of Corporate Social Responsibility (CSR) policies. Incipient and small enterprises often face special difficulties when requiring small amounts of finance from external capital providers. The adverse cost/earnings ratio may mean that a microcredit is unprofitable for banks in the 'conventional' way of lending. What is more, the recent financial and economic crisis has made the assessment of risk more hazardous, and has led banks to rethink their strategies, restructure balance sheets, and improve profitability.

Taking into account the risks and uncertainties associated with this type of lending, the most influential single provider of microfinance within the EU is likely to be the public sector.

In conclusion, the activities of public and private providers should be complementary, with public support targeted at 'non-bankable' borrowers, helping to create – to the highest degree possible – enterprises that will be successful. Inside the EU, as clear as possible a separation between small loans supplied by a bank to 'bankable' borrowers, and the cases to be handled by a specialised Microfinance Institution or development bank, should be observed. At the same time it should be recognised that banks are also providing or supporting microfinance services to the non-bankable sector in certain markets. In light of the highly sophisticated level of regulation for bank providers of microfinance, there is no need for a dedicated regulatory framework. Nonetheless, in order to avoid distortions of competition and excessive risk-taking, it is vital that the principle of same business, same risks, same rules for lenders be respected. To sum up, the EBF's study of its members' approach shows that private and other providers frequently work together. What is more, the proposed European Microfinance Facility for Employment and Social Inclusion offers an undeniable opportunity to bring different skills and experience to bear. This said, improved understanding of the nature of the microfinance activity in the 27 Member States is to be encouraged.

<sup>1</sup> <http://ec.europa.eu/social/main.jsp?langId=en&catId=89&newsId=547&furtherNews=yes>

*Elena Letemendia & Alison Bell*

## NEW FACES



**Cedric Quemener**

Drawn by the dynamism of the EBF, Cedric Quemener sensed quickly that the EBF would be just the working environment that suited. Preceding his arrival in March, Cedric's professional career included, Inter alia, brokering at Credit Agricole, and developing equities at Thompson & Reuter for the Benelux. As Manager of the Euribor-EBF structure, Cedric's files include bench marks Euribor Eonia, Eonia Swap, Eurepo, and promoting the relatively unknown STEP project. Though Cedric's advent is recent, he has been able to add to his financial and commercial profile, thanks to the novel associative and lobbyist aspects of his new role. Last but not least, whilst an avid sportsman, Brussels is not La Bretagne, and for the moment sailing and kite surfing are on hold.



**Christophe Bonte**

Swiss-Belgian, Christophe Bonte joined the EBF in December 2009 as Adviser for Securities Infrastructures and Operations. With a degree in International Relations and European Integration, Christophe has lectured and researched on the subject at the Swiss Institute for Public Administration in Lausanne. A PhD in political science - on a topic of high interest for the European Banking industry, given the EU Savings' Tax Directive - brought him into contact with the EBF, through a series of interviews he conducted with its tax expert, in the early 2000s. As a market expert for settlement at the Bank of New York Mellon prior to arrival at the EBF Christophe finds his new role to be a perfect combination of past experiences, expectations, motivation, and interests. From the outset, Christophe became immersed in his files, given his involvement with the EBF Secretariat before joining. Not surprisingly, Christophe's interest in European Affairs is reflected in his hobbies. Stamp collector rather than philatelist, he is collecting stamps dedicated to European integration since 1950, a rare angle.





**Szymon Stellmaszyk**

Szymon Stellmaszyk's arrival at the Federation heralds the advent of the Polish EU Presidency and the grounding that the Polish Banking Association is preparing for the 2nd half of 2011. As a seconded Adviser it is both appropriate and appealing for Szymon to become more familiar with the EU mechanisms in Brussels. What is more, he is benefitting from close collaboration with EBF staff aside from gaining experience that should prove invaluable for the Polish EU Presidency. As a lawyer with experience and interest in journalism and international relations Szymon aims, while in Brussels, to continue his professional commitments at the Polish Banking Association by following new EU legislation and coverage on the financial sector in the international media. Necessarily, familiarity with the EBF structure, work-style and procedures will significantly benefit Szymon's future coordination work at national level.



**Sébastien Dieu**

Sébastien Dieu arrived at the Federation early 2010. As an outside consultant for the EBF prior to joining, he had become acquainted with the EBF surroundings. Drawn to the multicultural diversity and dynamic environment, becoming part of the EBF staff was the next natural step. Indeed, the role of IT Coordinator matched exactly what he sought, including as it did, the development of an IT project (Collaborative Solution); a combination enabling him to put his expertise in Communication and Marketing to use at the EBF. What is more, for Sébastien the importance given to the staff's well being - and the structures in place to help staff integration - was a real pleasure to discover. Outside the office Sébastien pursues several hobbies, not least, coaching a basketball team.

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