FEDERATION BANCAIRE FRANCAISE

RESPONSE TO
PUBLIC CONSULTATION ON THE CAPITAL REQUIREMENT DIRECTIVE ('CRD IV')

French Banking Federation (FBF) welcomes the "*Public Consultation on the Capital Requirement Directive ('CRD IV')*" (CRD IV PC) and supports the efforts that would lead to a global level playing field in a strengthened financial system.

This paper does not duplicate our response to the Basel Committee on Banking Supervision Consultative Paper on liquidity and resilience (BCBS CP) that is attached. It focuses on CRD IV.

FBF fully concurs with CRD IV PC's goal to build a homogenous regulatory zone in European Union (EU). This will greatly help avoiding regulatory fragmentation in the EU whose end result would be the fragmentation of liquidity risk management and would deny the free flow of liquidity in EU.

Section I Liquidity standards

General Comments:

Liquidity risk metrics should be applicable to *no smaller scope than* pools of entities which are active in the zone when the following criteria are met:

- **actual liquidity risk management is global to the pool of entities;**
- **capacity to transfer liquidity;**
- **legally binding commitments between the entities.**

Subject to those criteria, a host supervisor should liaise with the college of supervisor, potentially by being a member of this college, to address liquidity issues: **no host regulation should be required to any specific entity, or group of entities, within the pool of entities that meet those criteria**. There should be an automatic waiving process: CRD IV PC §17: "application to individual firms *could* be waived", should be substituted by "application to individual firms *should* be waived"

Certainly, this will require clearly articulated a governance between the supervisors, notably in EU. Even though the CRD IV PC refers to governance issues[1], they need to be detailed to make sure that the CRD IV PC suggestions will actually work.

FBF concurs with CRD IV PC's suggestion to adapt standardized overlay factors (runoff and rollover assumptions) **to European jurisdictions** so that they fit jurisdictions' evidenced-specificities.

Hard-wired BCBS CP suggested overlay factors should be neither minimum (for runoff and liquidity assumptions) nor maximum (for rollover assumption) if evidence leads to different factors. **Adapted standardized overlay factors should be able to depart from BCBS CP suggestions.**

FBF welcomes the possibility that European authorities will be able to depart from the too narrowly defined assets that qualify for LCR-liquidity buffer, through establishing a list of assets that would be central bank eligible. **As LCR is market-wide stress-based, FBF considers that central bank eligibility should be a criterion *per se* to qualify for LCR-liquidity buffer.**

More generally, **European authorities should be in a position to depart from the BCBS one-size-fits-all approach to**:

1. **cancel out any remaining flaws**;
2. **make sure that Europe is not at comparative disadvantage** vis-à-vis other regions of the world that would depart from BCBS recommendations;
3. **mitigate the adverse consequences for the economy in the transition period**: European authorities should be in a position to choose the transition process (period, progressive thresholds for LCR and NSFR…). This is all the more important as analyses done so far have all concluded that the transition to the LCR and NSFR, as they are, would have massive consequences for the whole economy.

As articulated in our response to BCBS CP, **FBF considers that the one-size-fits-all LCR and NSFR assumption sets** in the BCBS CP, potentially adapted to each jurisdiction in Europe, should be the default measurement framework (*standardized regime*) that **could be**

[1] Example: the waiver governance needs to be detailed.

substituted by bank-specific LCR- and NSFR- assumption sets (*advanced regime*), reviewed and validated by the College or Supervisors. This advanced liquidity measurement regime would be adapted to bank specificities (business model, diversification of activities, funding sources…).

FBF is looking forward to constructively working with the European Commission on improving CRD IV.

Remark:
- some answers refer to the FBF's response to BCBS CP that is attached.
- additional comments on each PC paragraph are Appendixed

Question 1: Comments are sought on the concept of the Liquidity Coverage Requirement and its likely impact on institutions' resilience to liquidity risk. Quantitative and qualitative evidence is also sought on the types and severity of liquidity stress experienced by institutions during the financial crisis and – in the light of that evidence – on the appropriateness of the tentative calibration in Annex I. In particular, we would be interested in learning how the pricing of banking products would be affected by this measure.

Please find detailed comments in the FBF response to the CP.

In a nutshell, the main points are:
- FBF concurs with the concept of the LCR, which is very consistent with the regulation that French Banks have had to abide by for more than 20 years;
- There should be consistency between the type of scenario on which the LCR is based and the assets in the liquidity buffer:
  - If market-wide-crisis based, central banks should be considered as managing stakeholders in a liquidity crisis management and central bank eligible assets should be part of the LCR-liquidity buffer;
  - If central bank eligible assets are excluded from the LCR-liquidity buffer, the LCR stress test should not be market-wide-crisis based;
  - A possible solution could be to set a limit to the portion of the liquidity buffer that is composed of central bank eligible assets that are not necessarily highly market liquid (ex: central bank eligible loans) and to define the LCR-stress test scenario as an idiosyncratic stress test combined with the beginning of the market wide crisis scenario.
- The LCR assumption set is too extreme:
  - The liquidity buffer is too narrowly defined:
    - Either the LCR stress test scenario is a market-wide stress test and the central bank eligible assets should be part of the liquidity buffer, or central bank eligible assets are not part of the LCR liquidity buffer and the LCR scenario should be idiosyncratic stress test-based (ie less severe a scenario).
    - The overlay factors that are applied to the corporate and covered bonds are too severe.
    - The securities that are not qualifying for the liquidity buffer are not recognized any liquidity value in the cash inflows: direct sales and repo rollover should be considered. This binary approach should be substituted by a more progressive approach with a broader range of liquid assets with their accompanying liquidity factors.

- Securities issued by financial institutions should not be singled out:
  - Assuming 100% runoff of all financial institutions deposits is too extreme and not evidenced, even by the recent crisis.
  - Financial institution is too broad a category. It should be broken down in smaller categories.
  - Stickiness factors are too narrowly defined and should apply to financial institutions too.
- The 100% drawdown assumption on liquidity lines is too extreme. It should be broken down by counterparts and revised down (notably in light of evidence observed during the crisis)
- Banking liquidity supervision should be consistent with legally binding commitments: revocable uncommitted lines should not be considered, owned liquidity lines should be given a liquidity credit (and not denied as is suggested in the CP), reputation risk is not a commitment, off balance sheet commitments cannot be extended beyond their contractual maturities (only transactions with residual maturity longer than 1 month should be considered in the LCR).

- FBF response to BCBS shows FBF suggestions for changes to LCR assumption set (cf Appendix E).

On a stand alone basis, the LCR would impact not only prices but the services offered by banks:

- Banks would have to buy, hold and trap the narrowly defined assets that qualify for LCR-liquidity buffer. This would result in less liquidity for those assets (which is exactly the opposite effect of the very reason for those assets to be selected as qualifying for the LCR-liquidity buffer in the first place!). The bid/ask spread for those assets would increase.
- The CP disincentives market-making on assets that are excluded from the LCR-liquidity buffer as they would require longer than 1 month term funding (repo on those assets are not assumed to be rolled-over and those assets are not recognized any value in the LCR-cash inflows). The assets not qualifying for LCR-liquidity buffer would become less liquid and their bid/ask spreads would increase.
- Banks would be led to compete for deposits that are recognized stickiness, which will most probably make them more expensive (to attract them from competitors) and finally more volatile.
- Banks would decrease the rates offered to deemed non sticky clients (notably financial institutions)
- Due to punitive 100% drawdown assumption of liquidity lines, liquidity lines would be reduced in amounts offered and their prices would increase. The end result would be reallocate funding risk outside the banking industry (clients would no longer be offered this service, or it would come from non banks). This would apply more generally to all off balance sheet commitments that are allocated a too high 10% drawdown assumption a 1 year horizon… even more so when their contractual maturity is lower than 1 year!
- As banks would need to increase their longer than one month borrowings, this would drive short term rates up: this increase will be passed to clients: short term rates will increase.

LCR and NSFR should be seen in combination: the impact on offered services to the economy and on pricing will result from this combination.

Question 2: In particular, views would be welcome on whether certain corporate and covered bonds should also be eligible for the buffer (see Annex I) and whether central bank eligibility should be mandatory for the buffer assets?

First, FBF considers that consistency should be ensured between the severity of the stress and the assets that can qualify for the LCR-liquidity buffer (cf answer to *Question 1* above).

Second, market liquid assets, notably corporate and covered bonds, but also equities and commodities, should be part of either the LCR-liquidity buffer or contribute to LCR-cash inflows with reasonable liquidity factors.

Provided that market liquidity is not denied in the LCR-cash inflows, central bank eligibility can be mandatory for the LCR-liquidity buffer. We suggest that this criterion is not an additional criterion on top of market liquidity criterion, but a LCR-liquidity buffer qualifying criterion *per se*.

Question 3: Views are also sought on the possible implications of including various financial instruments in the buffer and of their tentative factors (see Annex I) for the primary and secondary markets in which these products are traded and their participants.

Please refer to FBF response to the CP with the suggestion for changes to the LCR-assumption set, notably for the LCR-liquidity factors that should be allocated to market liquid assets (cf. Appendix E).

Question 4: Comments are sought on the concept of the Net Stable Funding Requirement and its likely impact on institutions' resilience to liquidity risk. Quantitative and qualitative evidence is also sought on the types and severity of liquidity stress experienced by institutions during the financial crisis and – in the light of that evidence – on the appropriateness of the tentative calibration in Annex II. In particular, we would be interested in learning how the pricing of banking products would be affected by this measure.

Please find detailed comments in the FBF response to the CP.

In a nutshell, the main points are:

- FBF concurs with the concept of the NSFR, which is very consistent with French banks' practice;
- However, the NSFR suggested assumption set is too extreme:
  - In a 1 year long idiosyncratic stress test scenario, the bank cannot be assumed not to adapt its business models and keep doing business-as-usual: loan rollover assumptions (85% fore retail, 50% for corporate) are too severe. Loan origination scale-down assumptions need to be considered. Those assumptions are necessarily bank-specific as the businesses that could be scaled down are bank-specific. Capital market activities are among the easiest to scale down, as well as business that are exclusively asset oriented (ex: consumer loan business line, leasing activities…).
  - Market-liquidity criteria for an idiosyncratic stress test scenario should not be the same as for a market-wide stress test: market liquid assets that do not qualify for LCR-liquidity buffer should be recognized far more liquidity than the too low factors they are attributed.
  - Expected prepayment should be taken into account for what needs to be longer than 1 year term funded.

- The categories “all other assets” that are required to be fully funded at longer than 1 year horizon and “all other liabilities” that are recognized no funding value need careful attention. As an example, if applied to trading derivatives’ values in the balance sheet, it would not make sense: absent any netting it would require huge and unjustified amounts of funding which would not be manageable as the values of such derivatives can vary massively over time and switch from the asset side to the liability side (some derivatives such as swaps can be an asset at one time and a liability at another time).
- Banking liquidity supervision should be consistent with legally binding commitments: off balance sheet commitments cannot be extended beyond their contractual maturities.

On a stand alone basis, the NSFR would impact not only prices but the services offered by banks:

- The CP disincentives market-making on assets that are excluded from the LCR-liquidity buffer as they would require costly longer than 1 year term funding. Those assets would become less liquid and their bid/ask spreads would increase. This illustrates a flaw in the BCBS CP that consists in deriving NSFR-liquidity from LCR-liquidity, even though both the underlying scenarios (idiosyncratic + market wide stress for LCR vs. idiosyncratic for NSFR) and the horizons (1 month vs. 1 year) are different.
- Banks would be led to compete for regulatory-deemed sticky deposits, which will most probably make them more expensive (to attract them from competitors) *and* more volatile (ie: leading to exactly the opposite effect as the reason why those deposits are deemed sticky in the first place)
- Banks would decrease the rates offered to deemed non sticky clients (notably financial institutions)
- The rollover assumptions on loan (50% for corporate and 85% for retail) would require banks to fund loans on longer maturity than their contractual maturities! This would decrease the amount of offered loans and would increase the rates of those offered loans. The increase in prices would be even more material as the loan would be short. As an example, a 1 month long loan would need to be partially funded on maturity longer than 1 year: the 1 year liquidity cost would have to be passed to 1 month long borrower!
- The 10% drawdown assumption on all off balance sheet commitments, be they liquidity related or not, would increase longer than 1 year term funding, additional cost of which have to be passed to clients.

LCR and NSFR should be seen in combination: the impact on offered services to the economy and on pricing will result from this combination.

Question 5: Comments are in particular sought on the merits of allowing less than 100% stable funding for commercial lending that has a contractual maturity of less than one year. Is it realistic to assume that lending is reduced under liquidity stress at the expense of risking established client relationships? Does such a differentiation between lending with more and with less than one year maturity set undesirable incentives that could discourage for instance long term funding of non-financial enterprises or encourage investment in marketable securities rather than loans?

The BCBS CP assumption that a bank would not adapt its activity during a 1 year long stress test scenario is too extreme. As FBF suggests in its response to BCBS CP, it would make more sense to breakdown bank’s business lines between those that can be stopped (no or very low rollover assumption) and those that can be scaled down (far lower than 100% rollover assumption). As an example, a business line that would be fully loan origination oriented, to clients that the bank has no other relationships with, could be stopped quickly if a

liquidity stress was to occur. The FBF response to BCBS CP illustrates how extreme the loan rollover assumption is.

Question 5 clearly formulates one of the asymmetries that the BCBS CP is full of: a loan would be subject to a required rollover assumption whereas the very same lending, legally structured as a security, would not require any rollover assumption: these asymmetries should be cancelled out in the liquidity regulation.

Rollover assumptions will clearly disincentive banks from short term lending, and encourage investment in securities, marketable or not, since no rollover assumption is applied to securities.

Question 6: Views are sought on possible implications of inclusion and tentative "availability factors" (see Annex II) pertaining to various sources of stable funding for respective markets and funding suppliers. Would there be any implications of the tentative required degree of coverage for various asset categories for respective bank clients?

Please refer to FBF response to BCBS CP.

Question 7: Do you agree that all parameters should be transparently set at European level, possibly in the form of Technical Standards by the EBA where parameters need to reflect specific sub-categories of retail deposits?

The BCBS CP is based on a one-size-fits-all approach that denies market-specificities (client behaviour, legal environment, insurance mechanism, history…) that are actually different.

Within the Seventeen BCBS Principles, FBF suggests a comprehensive liquidity supervisory framework with a liquidity risk *measurement* framework that would allow different approaches, in a way similar to the Basel II solvency requirements for market and operational risks.
Such approaches would be LCR- and NSFR-based with assumption sets on runoff/rollover factors that would be either:

A. standardized (cf Appendix E for suggested changes to BCBS proposals), or
B. bank-specific subject to review and validation by supervisor.

Within the standardized approach, it would make sense that standardized assumptions are jurisdiction-specific and transparently disclosed to all participants. Those assumptions should be derived from evidence-based analyses in each jurisdiction. They do *not* need to be more severe than the hard-wired assumption in the proposed BCBS paper, if evidence leads to less severe assumptions.

One of the issues to address will be how to accommodate each market's specificity without ending up creating a huge number of rules within the standardized approach. In that context, the advanced measurement framework that FBF recommends would help avoiding this. In the review process of advanced measurement framework, part of which consists in reviewing bank-specific assumptions, the College of Supervisors will be review jurisdiction-specific assumptions.

Question 8: In your view, what are the categories of deposits that require a different treatment from that in Annexes I and II and why? Please provide evidence relating to the behaviour of such deposits under stress.

Please refer to the suggestions for changes in LCR and NSFR assumption sets in the FBF response to BCBS CP (Appendix E): they are based on additional breakdown; notably for deposits.

In a nutshell, it consists in:

- breaking down of the too broad "financial institution" category into smaller pieces: custodian, insurance companies, asset manager, broker/dealer, money market funds, central bank, fiduciaries
- taking into account relationship for all types of depositors.

Question 9: Comments are sought on the scope of application as set out above and in particular on the criteria referred to in point 17 for both domestic entities and entities located in another Member State.

As mentioned in FBF response to BCBS CP, FBF considers that the scope of application for LCR and NSFR should be consistent with:

- actual liquidity risk management organization (which is bank-specific)
- capacity to transfer liquidity in LCR-scenario and in NSFR-scenario
- legally binding commitments between the entities that are liquidity risk management-pooled

Subject to the above mentioned criteria, FBF recommends that LCR and NSFR apply to *no smaller break down* than groups of entities that meet the above described criteria. Home vs. host supervision should be articulated accordingly: host supervision should not be applied to any sub-group of entities within than the groups fulfilling the above mentioned criteria.

This is consistent with CRD IV PC (§17). The asset transferability should not be considered a "must have" criterion since other mechanisms are available. As an example, overnight lending between two internal counterparts could be stopped being rolled over: no asset transfer would be required.

Question 10: Should entities other than credit institutions and 730K investment firms be subject to stand-alone liquidity standards? Should other entities be included in the scope of consolidated liquidity requirements of a banking group even if not subject to stand-alone liquidity standards (i.e. financial institutions or 50K or 125K investment firms)?

Question 11: Should the standard apply in a modified form to investment firms? Should all 730K investment firms be included in the scope, or are there some that should be exempted?

Applying the CP at sub-consolidated levels would magnify the disruptive effects of the CP on the banking industry, and consequently for the whole economy: **FBF recommends limiting the scope of application to the consolidated level.** Should LCR and NSFR be required to some sub-consolidation levels, it should *not* be applied to smaller scopes that the ones satisfying the criteria listed in our response to *Question 9*.

The treatment of intra-group transactions, be they within between entities in the same group of pooled entities, or between entities that are in different groups of pooled entities (some of

which may be constituted of a single entity) would need to be clearly articulated as described in our response to *Question 12*.

So as not to create comparative disadvantages and uneven playing field between banks subject to LCR and NSFR requirements and other banks, **the liquidity regulation should apply to *all* banks** (be they internationally active or not)**, in *all* jurisdictions** (US, Asia, Europe…)**, with the *same* transition process, notably in terms of timing.**

The funding requirements should apply to *all* financial intermediaries, not only banks. Otherwise, not only the playing field would be uneven, but a portion of the funding risk in the economy would be transferred from banks to non bank institutions. Actually, this is one of the (most probably unintended) consequences of the BCBS CP: the overly conservative assumptions[2] in the BCBS would push a portion of the funding risk back to non financial institutions which are not subject to funding liquidity requirements and which do not have the counter-balancing strategies to mitigate a stress test (liquid assets to generate cash inflows, liquidity buffer, access to central banks...).

Question 12: Comments are sought on the different options and in particular for how they would operate for the treatment of intra-group loans and deposits and for intragroup commitments, respectively. Comments are also sought as to whether there should be a difference made between the liquidity coverage and the net stable funding ratio.

FBF disagrees that the liquidity regulation could deny legally binding commitments, such as asymmetrically dealing with liquidity lines, as suggested in the BCBS CP.

Subject to our response to *Question 9,* FBF considers that the guiding principles for dealing with intra –group transactions should be that those assumptions:

- should be consistent with legally binding commitments;
- should be symmetric from both sides of the internal deal;
- should be consistent with the rollover assumptions of the transactions that are ultimately funded / invested. If an activity is scaled down in the stress scenario, the scale down assumption should be applied to the same extent to intra-group with this subsidiary.
- may be differ within the same Group (ie: not necessarily a single method in a specific Group)

Question 13: Do stakeholders agree with the conclusion that for credit institutions with significant branches or cross-border services in another Member State, liquidity supervision should be the responsibility of the home Member State, in close collaboration with the host member States? Do you agree that separate liquidity standards at the level of branches could be lifted based on a harmonised standard and uniform reorganisation and winding-up procedures?

FBF concurs with the statement: that "*for credit institutions with significant branches or cross-border services in another Member State, liquidity supervision should be the responsibility of the home Member State".*

The governance for the "*close collaboration with the host member States*" will need to be articulated more clearly so that, subject to satisfying pre-defined criteria, such as the ones elaborated in our response to *Question 12*, the host supervisor can *not* require regulation to be applied to sub-entities in the Group.

[2] Example : 100% drawdown assumption for liquidity line to corporate.

Actually, this should apply to non Member State as well.

As detailed in response to *Question 7*, FBF suggests creating a two regimes funding risk measurement framework: one standardized, one advanced. Within the standardized regime, the statement should be that "*separate liquidity standards at the level of branches should be lifted based on a harmonised standard*". In other words, the waiver should be automatic subject to criteria detailed in our response to *Question 9*.

Since the advanced regime is subject to College of Supervisor's review and validation, with host supervisor from significant branches or cross-border services in any jurisdiction (not only a Member State). The statement "*separate liquidity standards at the level of branches could be lifted based on a harmonised standard or advanced measurement regime*", should apply.

Question 14: Comments are sought on the merit of using harmonised Monitoring Tools, either in the context of Supervisory Review or as mandatory elements of a supervisory reporting framework for liquidity risk. Comments are also sought on the individual tools listed in Annex III, their quality and possible alternatives or complements.

The contractual maturity mismatch that BCBS CP suggests is basically useless for actual funding risk management and is misleading. This should not be a monitoring tool, and should even less be disclosed.

For funding concentration suggested metrics, the total balance sheet is not a relevant balance to consider in a funding risk metric since the accounting entries are not driven by funding / liquidity. As an example, as IFRS requires derivatives to be accounted for their fair value, a perfectly matched position with two offsetting swaps would increase both sides of the balance sheet (one of the swap would be accounted for an asset for its fair value, while the other swap would be accounted for a liability for the opposite fair value).

Rather than widening the list of standardized monitoring tools, FBF suggests that banks are incentived to develop their own monitoring tools that would be adapted to their specificities.

Question 15: What could be considered a meaningful approach for monitoring intraday liquidity risk?

For this highly technical issue, we suggest organizing working group with banks, payment system providers and supervisors to elaborate a framework for intraday liquidity risk management. Note that intraday liquidity risk is mentioned (§4) but not elaborated in BCBS CP.

Section II – Definition of capital

General Comments:

We see significant issues as BCBS is currently working on the same issues. We therefore ask the European Commission to ensure appropriate coordination and alignment with BCBS on the definition of capital and of eligibility criteria. Further amendments could be done when Basel requirements are finalised.

We would also like to comment on assumptions made in articles 33, 73 and 74 that are copied below. Although it is true that significant government intervention was required to prevent the failure of certain major institutions, which substantially affected the financial stability, most banks – especially in Europe – suffered from this financial instability rather than from a lack of going concern regulatory capital. On that basis, we dispute the anticipative assumption that the outcome of the calibration to be made by the BCBS and by the CEBS would result in higher minimum requirements, as capital requirements will already be meaningfully increased given the regulatory deductions to be imposed on Common Equity and as the quality of the eligible instruments will already be significantly improved and harmonised.

Article 33: "During the financial crisis, institutions made significant unexpected losses. In many cases, the amount of going concern regulatory capital held was insufficient to absorb losses on a going concern basis, and created broader concerns about financial stability."
Articles 73: "In revising the definition of capital, the Commission services intend to introduce explicit, **higher** minimum requirements for the minimum levels of the ratios of Core Tier 1, Tier 1 and total capital (net of deductions) to risk weighted assets. This approach is required in order to align minimum capital requirements more closely with an institution's ability to absorb losses. It also reflects the focus of the market on going concern capital in assessing an institution's financial and solvency position. The Commission services will reflect on whether the proportion of Tier 1 capital that must comprise Core Tier 1 capital – i.e. the required level of predominance of Core Tier 1 - should be raised above the current level of 50%. The Commission services will also consider the potential for the minimum ratios for Core Tier 1 and Tier 1 to be used to deliver the requisite level of predominance."
Articles 74: "CEBS' quantitative impact assessment will be used to determine the appropriate calibration of these regulatory minima, and the nature and extent of any changes required to the level of predominance."

Question 16: What are your views on the prudential appropriateness of eliminating the distinction between upper and lower Tier 2, and of eliminating Tier 3 capital?

We support the approach of CRD IV to align with the BCBS consultation 164, in terms of a simplified capital structure and harmonised eligibility criteria.

Question 17: Are the criteria proposed for Core Tier 1, non-Core Tier 1 and Tier 2 sufficiently robust and how might they be improved?

French cooperative banks specify they have sent a full answer about the application of the criteria on cooperative banks through "Groupement National de la Coopération" (GNC). Comments are to be made on at least two criteria:

Criterion 2: in the case of liquidation, securities representing the capital must have a right to the net assets in proportion with the capital that they represent (= right to the liquidation surplus).

In the view of the stated objectives in response to the financial crisis, it should be noted that the system used by cooperative companies is more satisfactory from a prudential standpoint than the one envisaged by joint stock companies. Indeed, cooperative shareholders can not lay claim to the company's net assets, which strengthens the financial solidity of cooperative banks (notably in view of the permanency criterion).

Criterion 5: it seems to be a great paradox if the Basel Committee were to impose the disappearance of remuneration cap, thereby favouring the dispersal of profits to the detriment of the establishment of reserves, while nonetheless defending the establishment of buffers within the same document.

Criteria proposed for Core Tier-1, non Core Tier-1 and Tier-2 are, subject to comments made below, sufficiently robust and aligned on Basle consultation CP 164, which is important for obvious and critical harmonisation.

For non Core Tier-1 (Annex VI of CRD IV):

With respect to instruments to be included in Tier-1 Additional Going Concern Capital, we draw attention that these instruments can not be redeemed on short notice and that grandfathering arrangements should not result in issuers systematically calling their instruments. We promote the grandfathering rule included in the CRD:

- *Instruments that by 31 December 2010, according to national law were deemed equivalent to the items referred to in points (a), (b) and (c) of Article 57 but do not fall within point (a) of Article 57 or do not comply with the criteria set out in Article 63a, shall be deemed to fall within point (ca) of Article 57 until 31 December 2040, subject to the following limitations:*
  - *up to 20 % of the sum of points (a) to (ca) of Article 57, less the sum of points (i), (j) and (k) of Article 57 between 10 and 20 years after 31 December 2010;*
  - *up to 10 % of the sum of points (a) to (ca) of Article 57, less the sum of points (i), (j) and (k) of Article 57 between 20 and 30 years after 31 December 2010.*

With respect to eligibility criteria, we strongly fear that a limited number of eligibility criteria are too strict and will deprive banks of a large and flexible source of diversified capital. We would like to draw the attention of the Committee on the fact that new regulatory deduction rules will put more pressure on banks required Common Equity and Tier-1 Additional Going Concern Capital, banks will need to attract new investors and all investors will have to adapt to the new designed of eligible instruments. Consequently, we propose and strongly support adjustments to criteria 7a, 11 and 12.

Tier-1 Additional Going Concern Capital is recognised as a valuable source of diversified capital, similar to Common Equity but with distinctive characteristics such as the embedded seniority above Common Equity instruments. This seniority is not detrimental to more senior creditors and does not affect the capital quality of Tier-1 Additional Going Concern Capital framed by the eligibility criteria. Abolishing this seniority by either refusing dividend pusher mechanism or by imposing a write down that is permanent would have for only purpose to protect ordinary shareholders. It is therefore critical to maintain a hierarchy between the different types of investors in order to have an efficient and diversified capital investor base.

The requested amendments to Criteria 7a and 11 have for only purpose to maintain this objective.

Criterion 7a: It must be clarified those dividend pushers are allowed, because it is critical to maintain a hierarchy between the different types of investors in order to have an efficient and diversified capital investor base. The seniority of holders of instruments included in Tier-1 Additional Going Concern above the holders of most subordinated instruments included in Common Equity must be respected. In this respect, we strongly support the allowance of dividend pusher, in the form and with the restrictions promoted by CEBS, which are critical to the Additional Going Concern Capital investor base. Dividend pusher mechanism is a fundamental feature to draw the relationship between Common Equity holders and Additional Going Concern Capital holders. Fixed income investors, who represent the main available investor base for hybrid capital, relies on this fundamental feature to accept, or to simply be allowed, to invest in Tier-1 Additional Going Concern Capital instruments. We strongly support the approach of CEBS' guidelines (published on December 10th, 2009) in its article 83, which provides:

- *Dividend pushers are acceptable in order to preserve the rank of subordination between shareholders and hybrid investors and between hybrid investors themselves. Nevertheless, they must be waived at least when one of the following events occurs between the date the coupon is pushed and the date it is to be paid:*
    - *the credit institution no longer complies with the capital requirements set according to Article 75 (Article 63a (3), subparagraph (2)); or*
    - *the competent authorities require the cancellation of such payments based on the financial and solvency situation of the credit institution (Article 63a (3), subparagraph (3) first sentence); or*
    - *the dividend to shareholders is paid in shares.*
- *Under those circumstances, payment of the coupons/dividends will be forfeited and no longer be due and payable by the issuer.*

Criterion 8:

We are of the opinion that this criterion is unclear given the ranking issues mentioned before for hybrids structured as deeply subordinated debts. Therefore we would recommend the following wording: "*Dividend/Coupons are paid only if there are distributable items (retained earnings included)*".

Criterion 11:

First, we do not see why this criterion is only applicable to instruments classified as liabilities and not all Non Predominant instruments. Such distinction, if maintained would not be rationale from a capital benefit perspective and would create a competitive distortion with US and UK markets practice as preference shares, which have a legal nature of equity, would not be subject to such conversion or write down.

Moreover we are of the opinion that the requirements (a) and (b) should be deleted. A permanent write down is not acceptable for investors but also conceptually not acceptable as it effectively subordinates Tier-1 Additional Going Concern Capital to Common Equity, while Common Equity must be the most subordinated form of capital according to CRD IV' eligibility criteria. Indeed it must be clarified that a write up is possible to preserve the ranking if the situation of the bank improves; otherwise investors would be worse off than ordinary shareholders as these participate in the recovery of the bank when retained earnings are built up again. The same applies in case of liquidation, once all other creditors have all been repaid.

Criterion 12:
We strongly support to include an exemption, in the form promoted by CEBS, for market making purpose. CEBS'guidelines article 73 provides :

- *It is proposed that repurchased instruments held by the institution for market making purposes shall not at any time account for more than either 10% of the relevant issue or 3% of the total amount of all outstanding hybrid instruments issued by the institution, whichever of the two limits is the lowest. Supervisors may nevertheless apply stricter limits.*

For Tier-2 (Annex VII of CRD IV):

With respect to grandfathering, we support appropriate arrangements in line with the CEBS rules for Tier-1 Additional Going Concern Capital. Although the time horizon might be shorter, we favour the digressive approach developed by the CEBS.

With respect to Criterion 4.c, we believe that moderate incentive to redeem should be accepted in Tier-2 instruments. Contrary to Tier-1 Additional Going Concern Capital instruments, Tier-2 instruments, which is in the Gone Concern Capital category, are not perpetual and are expected to be repaid at maturity. The existence of moderate incentive to redeem, in particular such as step up, is an important term for the Tier-2 investor base. Refusing moderate incentive to redeem will certainly affect the available investor base for the category of capital, especially for institutional transactions. Restricting all form of incentives to call will significantly impact Tier 2 raising prospects of European banks and much lesser so their US counterparts which benefit from the deep retail market.

With respect to Criterion 8, we strongly support to include an exemption for market making purpose, in the form promoted by CEBS for Tier-1 Additional Going Concern Capital.

- *It is proposed that repurchased instruments held by the institution for market making purposes shall not at any time account for more than either 10% of the relevant issue or 3% of the total amount of all outstanding hybrid instruments issued by the institution, whichever of the two limits is the lowest. Supervisors may nevertheless apply stricter limits.*

With respect to Criterion 8, we also support the temporary deletion of part of the criteria 8 as follows "The issuing institution shall not knowingly purchase, or directly fund the purchase of the instrument". The deleted part of the criterion should be examined and drafted in more details to ensure that the requirement does not prohibit sound market practices Alternatively, it should be clarified that this criterion aims at discarding financial engineering turning intentionally funding into Tier-2, as opposed to sound banking relationship including funding that could be partially used by the client (i.e. corporate, institutional investors, employees, …) for investment in shares of Banks

Additional comments on articles of CRD IV:

Besides the critical comments made above on the eligibility criteria, we would like to reflect on the CEBS pending questions which are embedded in article 52, 53, 77 and 78.

Article 53: "In relation to the nature of the trigger required for conversion of a hybrid instrument to a Core Tier 1 instrument, the focus of the proposed requirements is upon an objective trigger for conversion, e.g. a fall in a capital ratio to a particular level. In Article 66 of CRD II, additional regulatory recognition is afforded through a limit of 50% of Tier 1 to convertible instruments that must be converted into Core Tier 1 instruments during

emergency situations and may be converted at any time by the competent authority based on the solvency situation of the issuer. A number of different types of situation could precipitate a need to convert hybrid instruments. Such situations could, for example, include a fall in capital requirements to a pre-determined level, or possibly a projected shortfall in capital requirements in the near future. In light of the potential for different drivers of the need for conversion, the Commission services continue to believe that an element of discretion has a potentially useful role to play in triggering conversion. The Commission services will reflect further on the potential triggers for conversion in the context of a review of the role and potential nature of contingent capital."
Basle CP 164 only refers to a specific trigger point to trigger the write down or conversion (see article 89 criterion 11 in Basle CP 164 and annex VI criterion 11 in CP CRD IV), and does not refer to a required discretion of the issuer. We suggest to align on the Basel CP 164 approach for obvious and critical harmonisation reasons.

Article 57 and 58 are related to tax treatment of instruments. We note that the Commission services have been reflecting on the tax treatment of instruments to be included in non-Core Tier 1. We also note that the Commission services do not consider additional eligibility requirements in relation to the tax treatment of hybrid instruments to be required. We fully support this conclusion of the Commission.

Question 18 : In order to ensure the effective loss absorbency of non-Core Tier 1 capital, would it be appropriate under certain circumstances to require the write down of the principal amount of an instrument or its conversion to a Core Tier 1 instrument? To what extent should the trigger for write-down / conversion be determined objectively or at the discretion of an institution or its supervisor?

This question relates to Criterion 11 of the eligible criteria for inclusion in Tier-1 Additional Going Concern Capital (annex VI criterion 11 in CP CRD IV and article 89 criterion 11 in Basel CP 164).

We agree that the importance of going concern loss absorbency is paramount. The CEBS' Guidelines on hybrid capital instruments (CRD II implementation guidelines) have already listed the various loss absorbency features, which are in our view sufficient to perfectly ensure a loss absorption mechanism on going concern:

98 Various characteristics have evolved to provide loss absorbency of the principal amount of a hybrid instrument. These include subordination, flexibility to cancel coupon/dividend payments with full access to waived payments, principal write-down features, convertibility into higher forms of capital and the fact that the instruments must not be taken into account for the purposes of determining whether the institution is insolvent.

99 The relevance of these loss absorbency mechanisms varies depending on the actual situation of an institution. Subordination, for example, is most important in a liquidation to ensure that hybrid holders' claims are not met before all more senior claims are satisfied. The write-down of the principal or the conversion of hybrids into instruments referred to in Article 57(a) at an appropriate trigger point, on the other hand, enables loss absorbency on a going-concern basis and may help the institution to recover.

Therefore in the case where the bank's situation deteriorates, a write down or a conversion into ordinary shares enables the bank to postpone liquidation (and can be activated in conjunction with other recapitalisation mechanisms such as a capital increase). Regarding write down, as said before, we advocate that this mechanism remains temporary and not permanent.

We are of the opinion that triggers must remain objective (such as a breach of minimum solvency ratio) and be referenced on regulatory ratios that may be verified by investors at any time. In addition, the CEBS' Guidelines on hybrid capital instruments prescribes that the bank and the supervising authority may have the possibility to activate a loss absorption mechanism on a discretionary basis in case ratios come under pressure.

Nevertheless we are of the opinion that criteria 11 may rather be removed given the issues it may create (see above). Then the requirement for loss absorbency mechanism could apply to the definition of contingent capital instruments.

Question 19: Which of the prudential adjustments proposed have the greatest impact? What alternative, robust treatments might be considered and what is their prudential rationale?

1. **Minority Interest deduction:**

   The Commission's proposal is to deduct minority interests from the common equity component of Tier one. Although it is not explicit, we assume that minority interests will continue to be fully included in Tier one.

   Since a core tier one ratio will become a regulatory ratio, this proposal leads to a situation where a group core tier one ratio integrates 100% RWA of consolidated subsidiaries (denominator) but cannot take into account 100% of consolidated subsidiaries' capital (numerator).

   There appears to be no good reason for this imbalance in the prudential treatment of the denominator (RWAs) and the numerator (Minority interests) as minority investors do effectively absorb part of the risks of the subsidiary.

   This would have a very large impact on the European market:

- it would penalize the business model of cross-border groups, especially in the context of the EU single market : local authorities sometimes impose for a group not to take control of 100% of a bank in order to have part of the capital owned by local investors or to maintain a meaningful listing on the national stock exchange. In some instances, historically banks were simply not able to acquire 100% of the capital of local banks as only a controlling stake was offered for sale in the privatisation process. Independently of such constraints, it can also be a well devised strategy for banks to share the risks associated with investments in foreign markets by bringing along local investors. Similarly, the terms of successful collaborations between banks and industrial partners often relies on shared ownership of dedicated in order to ensure an alignment of interests. Finally, there are instances where banks may need to incentivise the founders and Management by allowing them to retain minority interest in the capital of a newly acquired company. The proposed deduction will penalize banks in their external growth strategy and/or will change their behaviour in relation to the capitalisation of their subsidiaries. In particular, it may reduce banks' appetite when it comes to contributing direct investments to the modernisation of the banking industry in certain emerging countries including in Europe.

Selected examples of presence of minority interests in certain subsidiaries

Poland

Historically, the Polish FSA (or its predecessor - KNB) required the foreign purchaser of a controlling stake in the capital of a Polish bank to assume certain obligations such as:

1. keeping the bank listed on the Polish Stock Exchange;
2. capping the controlling stake to 75%..

As a result of that constraint, Foreign banks were compelled to maintain significant minority interests in their local Polish subsidiaries, as can be illustrated by the examples of ING and Citibank/

ING / Bank Slaski:

In March 2001, ING was allowed by the FSA to cross the 75% threshold in the capital of Bank Slaski but on the condition that subsequently the stake held by Citibank would be reduced to 75% ; This was achieved in 2005 when ING sold a 12.77% stake in Bank Slaski and thus reduced its holdings to 75%.

Citibank / Bank Handlowy:

In 2000, CItigroup was allowed by the FSA to cross the 75% stake in Bank Handlowy and to merge Bank Handlowy with Citibank Poland, on condition, that within two years from the acquisition, Citigroup would reduce its shareholding to 75%. In December 2004, Citigroup sold an 18.2% stake in Bank Handlowy and thus reduced its stake to 75%

Romania

Société Générale / BRD:

There are significant minority interests alongside Société Générale in the capital of BRD (ca 40%) This results from the fact that when BRD was privatised in 2002 only 47% of the capital was put for sale. Société Générale was thereafter able to increase it stake above 50% thanks to a capital increase but the rest of the capital remains held by a few local institutional investors who do not intent to sale their stake.

Czech Republic

Société Générale / KB:

Although there was no explicit regulatory constraint in respect of the level of foreign ownership in KB, only a controlling block was put for sale and the Government was keen to maintain KB listed on the Czech Stock Exhange given its weigh in terms of market capitalisation.

Nederland

BNP Paribas / Insinger de Beaufort:

BNP Paribas acquired ca 63% of the capital while the remaining 37% remained the ownership of the historical founders and management of the acquired company in order to align the interests of the historical management with those of BNP Paribas and to maintain its entrepreneurship component.

- it would limit private sector solutions for rescuing ailing banks: if minority interests had not been considered by regulators as part of core tier one, some operations would have probably never happened. This is contradictory with the Commission's objective to build a stronger framework of crisis management in Europe with a more balanced burden-sharing between private and public sectors.

The BNPP/FORTIS case

During the financial crisis, BNP Paribas has negotiated with the Belgian and Luxembourg governments for the acquisition of Fortis Bank and BGL. The complex acquisition would have been more difficult under the newly proposed regime.

Indeed the fact that the shareholders' equity held by the Belgian and Luxembourg States was taken into account as minority interests in Tier-1 while 100% of the RWA were also taken into account in BNP Paribas's ratio was a key ingredient to this complex transaction and a major lever to reach an agreement with the Belgian and Luxembourg States that wanted to remain reference stakeholders.

In order to **achieve a more balanced treatment**, we should **exclude RWA supported by minority interests** from the denominator of the group Core Tier One ratio. For each subsidiary with minority interests, the consolidated RWA of the subsidiary would contribute to the total group's RWA only up to the percentage held by the parent company when calculating the Core Tier One ratio of the Group. The Group core tier one ratio would then reflect in a symmetrical way both the capital held by the Group (ie excluding minority interests) and the risks associated with the subsidiary (ie excluding the portion of RWA assumed by minority shareholders) – see numerical example below (case 2).

An other approach could also consist in the **inclusion of Minority Interest up to a limit in the numerator of group core tier one ratio**. There can be instances where the local subsidiary is capitalised well in excess of the Core Tier One ratio of the group measured on a consolidated basis. In this case, one could argue that the Group unduly benefits from this overcapitalisation through the inclusion of minority interests in the Group's regulatory capital.

To prevent this situation, minority interests in subsidiaries could be included only up to the level corresponding to the Core Tier One ratio of the group. The portion exceeding this threshold would cease to be recognised in Core Tier One capital of the group - see numerical example below (case 3)

Numerical examples for a more balance treatment of minority interests

Assume one Group with only 3 subsidiaries with minority interests (other subsidiaries held 100%[3]). The group Tier One capital is 3 000 M, including 240 M Minority Interests (MI), 500 M regulatory adjustments and 900 M Non Predominant instruments. The total group's RWAs are 30 000 M, of which 7100 M represents the contribution of the 3 subsidiaries to the consolidated RWAs.

[3] for the purpose of the calculation, "mother" will thereafter refer to the parent company consolidated with its 100% subsidiaries.

	%ownership MI	cap+ res+ MI	deductions	hybrids	Total T1	RWA
Mother		2 360	-500	900		22 900
Sub1	30%	50				1 000
Sub2	45%	150				1 100
Sub3	10%	40				5 000
Total subsidiaries		240				7 100
Total Group		2 600	-500	900	3 000	30 000

Group Tier One ratio is 10%. If minority interests were fully recognised in the Core Tier One for the purpose of the calculation of the ratio, the Core Tier One ratio would be 7%.

Case 1 / Basel proposal

Minority interests are excluded from predominant capital AND Core Tier One ratio continues to be caculated based on the Consolidated Group's RWAs. Core Tier One capital is therefore 2600-240-500 ie 1860 while the RWA to be taken account in the calculation of the ratio remain unchanged at 30 000.

	Core T1	RWA	Core T1 ratio
Basel Ratio (MI excuded from Core)	1 860	30 000	6,20%

Case 2: Symmetrical deduction of RWA and Minority Interests

Minority interests are deducted from Core Tier One capital but for symmetry purposes, only the portion of the subsidiaries' RWAs corresponding to the ownership percentage of the group is taken into account in the denominator of the Core Tier One ratio.
Σ %ownership $_i$ * RWA $_i$ = 1 295 M = RWA to be excluded from denominator.

	%ownership MI	RWA belonging to MI
Sub1	30%	300
Sub2	45%	495
Sub3	10%	500
Total subsidiaries		1295

	Core T1	RWA	Core T1 ratio
subsidiary's RWA are reduced to the group's percentage	1 860	28 705	6,48%

NB1: data collected in table 2 of QIS could allow to compute this case.

It is to be noted that Banks could continue as today to report consolidated RWAs (ie including the portion attributable to minority shareholders), in particular for the purpose of the Tier One ratio calculation.

Case 3: Group Core Tier One ratio adjusted for the "overcapitalisation" of subsidiaries

Minority interests are included in the Group Core Tier One capital but only up to a cap defined by reference to the Mother's Common equity Ratio (such ratio

being defined as per the QIS as (Mother's capital+ reserves)/ Mother's RWA = 10,3%).

The "overcapitalisation" of the subsidiary which should be excluded from the calculation of the Core Tier One capital can then be defined as:

Overcapitalization $Sub_i = MI_i - 10.3\% * RWA_i * \%$ ownership $MI_{i.}$

For instance, in sub 2, the Portion of RWA attributable to minority shareholders is 495 and if the reference Mother's common equity ratio was applied, the minority interests should be equivalent to 51, hence a 99 "overcapitalisation" compared to the actual amount of minority interest (150). Based on this calculation, the amount of relative "overcapitalization" attributed to MI can be excluded from Core Tier One capital:

	overcap vs Common cap
Sub1	- 19
Sub2	- 99
Sub3	-
Total sub	- 118

	Core T1	RWA	Core T1 ratio
overcap MI based on mother's common equity	1 982	30 000	6,61%

	Tier one	RWA	T1 ratio
overcap MI based on mother's common equity	2 882	30 000	9,61%

NB 2: data collected in table 5 of QIS could allow to compute this case.

NB 3: One can notice that the exclusion of this overcapitalization could also apply for Tier One capital

2. Deduction of DTAs:

The Commission consultative states that deferred tax assets ("DTAs") that rely on future profitability to be realised should be deducted from the common equity component of Tier 1 capital. We recognise that a degree of prudence may be required when allowing DTAs in regulatory capital as their value can be affected in periods of economic stress. However, we see little justification for such a draconian deduction, which in our view fails to take into proper consideration the various categories of DTAs as well as the value they retain on a going concern basis.

a. *The Commission must appreciate that DTAs result to a large extent from the discrepancies in national tax rules and that in any case the accounting standards make the recognition of all DTAs subject to confirmation by the external auditors.*

DTAs dependent upon future profitability to be realised arise both from tax loss carried forward and timing differences between the recognition of gains and losses in financial statement and their recognition for tax computation. Such timing differences commonly derive from the numerous discrepancies between tax and accounting rules, which vary greatly depending on tax laws and jurisdictions. For instance, discretionary or no-name-specific provisions may not be tax deductible in some jurisdictions, thereby creating DTAs that will only reverse when the actual loss is incurred. Inevitably, banks do record significant

amounts of DTAs associated with "temporary differences" in their normal course of operations.
In reporting net DTAs companies are required by accounting standards to make an assessment of recoverability based on estimates of future taxable profits. Importantly, this assessment is subject to scrutiny from external auditors in the context of their periodical accounting review, particularly in periods of economic stress: DTAs will not to be recognised (or will be written off in whole or in part if they have been previously recognised) in case there is not enough certainty that taxable profits will be available to support the utilisation of DTAs in future years.

b. *We can accept that harmonised rules be defined in order to avoid undue reliance on DTAs in regulatory capital but consider that the proposed blanket rule deduction is unwarranted and will entail undesired effects.*

We do understand the concern about the undue reliance on DTAs that can be derived from lessons learnt during the Japanese banking crisis of the 1990s. The introduction of an internationally accepted rule for DTAs allowance in regulatory capital could therefore be useful to avoid this type of situation. We are also cognisant of the fact that DTAs are commonly recorded based on their nominal and not time-discounted value. However, we strongly urge the Commission to revisit the blanket rule deduction envisaged which is not only unwarranted but could also have undesirable effects:

- **The logic underlying the proposed deduction, i.e. that DTAs dependent on future profitability should hold no value at all whatever the circumstances, does not appear coherent with the "going concern" approach adopted by the Basel Commission for Tier 1 capital.** As explained earlier, DTAs are already subject to an economic value test conducted by external auditors to confirm their recoverability. Actually, DTAs, do retain value over the long term as long as the bank is in operation. This is even true for the part that has not been recognised since the time limit set by tax authorities to utilise DTAs is usually very long or unlimited. It is only in a liquidation scenario that DTAs will loose entirely their value, at least in most tax jurisdictions and from that perspective a deduction from Tier 2 rather than Tier 1 capital could even appear defendable. Evidence that DTAs, whether that be on tax losses carried forward or timing differences, do retain value in periods of stress is supported by the fact that DTAs will be fully factored in when conducting a valuation of the business in case the bank or one of its subsidiaries is acquired or transferred.

- **Clearly, the proposed deduction increases the pro-cyclicality of the capital regime**. DTAs resulting from tax losses, loan loss reserves (not always tax deductible) and unrealised investment losses will increase during downturns and be reversed when results improve. As a consequence, the proposed deduction will further deplete capital in periods of economic stress.
- **The forward-looking provisioning scheme advocated by the Commission will translate into non tax-deductible provisions thereby increasing substantially the amount of DTAs**. Deducting such DTAs from Tier One Capital would annihilate in part the benefit of this countercyclical measure and may even disincentivise conservative provisioning policy.
- **The proposed deduction is in part contradictory with the stated objective to maintain a level playing field.** The proportion of DTAs resulting from temporary differences varies widely between countries depending upon local tax laws. Deducting such DTAs penalise banks operating in tax jurisdiction where certain asset value adjustments (e.g. loan loss reserves, impairment, write down) are not tax deductible and this will translate into undesirable distortions based on the localisation of a bank's activities.

c. *We recommend that the Commission devise a more balanced partial deduction rule, taking into proper consideration the different categories of DTAs.*

We ask the Commission to give consideration to a more balanced approach for DTAs:

- Based on the partial deduction rule principle already accepted by some bank supervisors: capping the amount of DTAs that can be recognised for prudential purposes would address the concern about excessive reliance on DTAs while recognising that DTAs do retain value on a going concern in most circumstances. It would also alleviate the procyclical effect of the measure. We think that in the context of prudential supervision, a cap expressed as a percentage of capital would be more straightforward and effective than a limit based on a set time horizon[4].

- Based on an important distinction to be made between tax loss carried forwards and timing differences. The Commission must take into account that the level of timing differences, contrary to tax loss carried forwards, can be heavily influenced by the tax regimes in the jurisdiction where the banks operate. Furthermore, banks record a permanent cushion of timing differences which are very likely to reverse normally in most circumstances. Applying a permanent deduction for such DTAs would be unduly penalising. Admittedly, where a bank starts making a loss and record a Tax Loss Carried Forward, more convincing evidence will be required that sufficient future taxable profit will be available for such tax losses to be utilised. For those reasons, no deduction should be apply for DTAs on timing differences while a cap may be required for DTAs on tax loss carried forward.

Following that logic, we recommend that:

- **no deduction should apply to DTAs on timing differences;**
- **DTAs on tax loss carried forward should only be deducted from the Common equity component of Tier 1 capital in all or in part where the total amount of DTAs exceeds a certain threshold of Tier 1 capital (for instance 10%[5]) as illustrated by the example below:**

	Net DTAs arising from Timing differences In % of Tier One Capital	DTAs arising from Tax loss carried forward In % of Tier One Capital	Total Net DTAs In % of Tier One Capital	Portion to be deducted from Predominant Tier One
Case N°1	9%	9%	18%	8%
Case N°2	12%	5%	17%	5%
Case N°3	4%	6%	10%	0%

Finally DTAs generated on elements that are not included in Predominant Tier One capital in the first place cannot be subject to the deduction either. If minority interests are deducted from Predominant Core Tier One capital, DTA deductions on the entities concerned should

[4] *A maximum time horizon for DTAs recognition in regulatory capital could involve the presentation of tax business plans on a regular basis and for several entities within the Group (i.e for each domestic and foreign tax entity within the Group as assessing recoverability of DTAs based consolidated financial information is irrelevant). The suitable time horizon can also vary depending upon the business mix of the entity and the reliability of forward looking estimates.*

[5] Such % being set – potentially at a higher level- when all consequences of the proposed BCBS measures can be evaluated.

therefore also be adjusted to the pro-rata of the holding. Besides, DTAs on OCIs (Cash flow hedges) and therefore no contribution to Predominant Tier One capital should not be subject to the deduction.

3. Deduction of participation in insurance companies:

With respect to the deduction of the participations in financial institutions, we urge to restrict the scope of this deduction to discard insurance companies. The full deduction is not the right answer to participations in insurance companies.

Banking and insurance groups: an integrated successful business model but with different risk types and horizons

First of all, it should be mentioned that substantial holdings in insurance companies allow banking groups to significantly enlarge the range of products they are offering to their customers, at a competitive price, through a common distribution channel. Thanks to the durable partnership that exists between banking and insurance activities, the "bancassurance model is a very strong one.

However, risks borne by insurance companies are of different nature compared to the banking risks. In the insurance sector, the main risks are composed of (i) underwriting risks (insurers predict the likelihood that a claim will be made against their policies and they price their products accordingly) and (ii) asset management risks (companies have to ensure that the premiums and life insurance deposits they receive are invested in an appropriate way). The requirements on investments are also different, in particular since the insurance investment period is typically very long-term. Banks and insurance companies are therefore regulated by specific regulatory requirements: in Europe, banks must comply with the Basel 2 prudential requirements, known as the Capital Requirements Directive (CRD) in the EU, while insurance companies are subject to the Solvency 1 and tomorrow the Solvency 2 directives.

Avoiding Double counting: the conglomerate approach

The issue of potential double counting effects of own funds between banks and insurance companies has been identified in the late '90s by the Joint Forum (a working group of the BSBC, IOSCO and the IAIS) which has established the roots for the consolidated supervision of mixed financial companies and has proposed *"measurement techniques and principles to facilitate the assessment of capital adequacy on a group-wide basis".*

In the EU, these recommendations were translated into the Financial Conglomerate Directive (EC 2002/87) in 2002. This global framework has now been operational for several years in all EU countries and has strongly proved its efficiency during the recent crisis.

The absence of double counting is analysed on the one hand at a global level (conglomerate ratio) and on the other hand at the banking and insurance level respectively.

Indeed, the way the conglomerate directive may be applied following the methods proposed by the Joint Forum, as it is the case in France, correctly takes into consideration this consolidated approach as follows:

- a global control of the solvency of the conglomerate through the calculation of an "observation ratio". The latter is produced by adding up the requirements of the banking activities and those of the insurance group and by comparing this amount to the consolidated total capital of the group (intra-group transactions being eliminated) to ensure that the requirements are fully covered ;

- for the bank solvency calculation, including :
* deductions from the core tier one for the goodwill relating to insurance purchases ;
* deductions from tier one for the part which relates to the double counting in the tier one (i.e. neutralisation of the insurance reserves and elimination of the potential capital gains and losses booked in the insurance companies as they would otherwise also appear as banking capital due to the prudential consolidation methodology which is used) and equity participation risk weighting for any remaining holdings.

It should also be mentioned that this prudential assessment is integrated in an additional stringent European EC framework for all financial groups which have been designated as conglomerates, with more constraints than Basel 2 and CRD framework on larges exposures, sectorial analyses (equity investments, real estate), internal control issues and a review and elimination of the reciprocal transactions between the banking entity and the insurance one.

This double geared system includes therefore a full monitoring of all the risks taken by financial conglomerates and the careful control of their capital coverage.

In this context :

- We are convinced that the current EC regime of the conglomerates Directive is the appropriate answer to the BCBS concerns and urge the Authority to avoid inserting redundant or interfering rules to the current treatment.

- We also call on regulators to focus first on the implementation of Solvency 2 (and its equivalents outside of the EU) and then on the forthcoming Basel 3 and CRD4 framework before undertaking any review of the regulation in the conglomerate field.

Question 20: Are the proposed requirements in respect of calls for non-Core Tier 1 and Tier 2 sufficiently robust? Would it appropriate to apply in the CRD the same requirements to buy-backs as would apply to the call of such instruments? What restrictions on buy-backs should apply in respect of Core Tier 1 instruments?

Proposed requirements for calls of non Core Tier-1 and Tier-2 are, except for comments made below on articles 49 and 63, sufficiently robust and aligned on Basle CP 164, which is important for obvious and critical harmonisation.

We are very concerned by Article 49 that is copied below. The use of call options is a critical feature of Tier-1 Additional Going Concern Capital for the banks to manage their capital base. The use of call options should not be jeopardised.
"There are two aspects of our proposals that the Commission services will continue to review: (a) the requirement for principal loss absorbency; and (b) the use of call options."

With respect to article 63, we consider that a lock-in provision for supervisor to stop the redemption at maturity of Tier-2 capital is neither necessary nor appropriate because Tier-2 capital falls in the gone concern capital category and because its capital contribution is amortised during the 5 years preceding the maturity date, hence the instrument does not provide any capital credit at time of maturity.
Article 63: "A lock-in clause could be argued to be an additional measure that could enhance further the permanence of Tier 2 capital. Such a clause could afford the institution or competent authorities the ability to prevent Tier 2 instruments from being redeemed in times of stress. A similar clause is currently required of Tier 3 capital - Article 13(3) of 2006/49/EC

refers. However, a lock-in clause could equally be argued not to be necessary in respect of a Tier 2 instrument, as the purpose of Tier 2 is to absorb losses on a gone concern basis. The Commission services would welcome comments on the appropriateness of a lock-in clause in respect of Tier 2 capital."

With respect to buy-back of non Core Tier-1 instruments, we strongly dispute assertion that buybacks are analogous to the exercise of call options at par, hence should be treated in the same way with a prohibition to carry on such transaction in the first five years unless previously replaced by an instrument of at least the same or better quality.
The mechanisms for a call occur contractually and are explained in the documentation. There can be an incentive for the institution to exercise such call. On the contrary, a buyback opportunity is completely at the discretion of the institution's management and the only incentive of a justified buyback is to add economic value to the institution by actively managing its capital structure for reasons that differ from a pure market obligation to call or redeem a hybrid capital instrument at a certain point in time.
This being said, we understand the importance of the prudential requirements for a buyback to be at the full discretion of the institution and subject to a prior regulatory approval. However, as we consider that buybacks are of a materially different nature than calls or redemptions, we strongly recommend avoiding any reference to a five-year restriction and to a mandatory replacement. Appropriateness of timing and replacement should be left at the discretion of the institution and of its supervisor, depending on the specific situation justifying the economic and prudential rationale of a buyback.

With respect to buy-back of Core Tier-1 instruments, and in line with BCBS consultation CP 164, we have no objection to a requirement for regulatory approval in all circumstances subject to the following request. We strongly support the inclusion of either exemptions for market-making / liquidity contracts, hedges, and employees' remuneration plans, or a defined yearly allowance covering all these practical constraints / daily management of the Core Tier-1 capital.

Question 21: What are your views on the need for further review of the treatment of unrealised gains? What would be the most appropriate treatment of such gains?

We believe it should be made clear that the proposed rule only applies to gains and losses recognized in equity and not to unrealised gains and losses accounted in net income.

For unrealised losses recognised in equity, we agree no filter should be used in the future to reinforce the quality of the capital base.

For unrealised gains on equity instruments, equity investments that will continue to be accounted with unrealised gains in equity under IFRS 9 will be long term investments. There will indeed be no rational for developping short term or medium term activities with unrealised gains recognised in equity under the new standard as banks *"will have to make an irrevocable election to present in other comprehensive income subsequent changes in the fair value of an investment in an equity instrument"* meaning that, if the investment is sold, the profit would no longer be recognised in net income.
As unrealised gains generally apply to strategic equity investments and as this will be strongly reinforced by the new accounting standard, it would really be appropriate to take part of the growth of the value of the investments for the calculation of the own funds of the bank: for example, if a bank buying a stock of 100 and this investment has after 20 years of holdings a value of 300, it does not seem realistic to base the value of the investment on the original value of the investment for its capital base (numerator). It may be advisable to apply a haircut to the value of the investment (in Belgium 20 % and in France even 55 % currently applies) and to consider the unrealised gains in the Tier two, but to fully filter unrealised

gains whereas on the other side capital losses are deducted at 100 % from tier one clearly does not make sense.
The unrealised gains on debt instruments are for their part not accounted in equity under IFRS 9.

We would however recommend that the Basel Committee wait for US GAAP and IFRS amendments and transition provisions on financial instruments to be fully finalised before implementing the new rules on unrealised gains and losses. This would prevent unwanted swings in the capital base triggered by changes in accounting standards. On this matter we would also like to stress that in order to reduce the need for prudential filters, it is crucial that accounting standards allow for a proper consideration of the actual business model of financial institutions and do not introduce artificial volatility in equity.

Question 22: We would welcome comments on the appropriateness of reviewing the use of going concern Tier-1 capital for large exposures purposes. In this context, would it be necessary to review the basis of identification of large exposures (10% own funds) and the large exposures limit (25% own funds)?

The large exposures framework is a back-stop regime which seeks to protect regulated institutions against large losses that could threaten their solvency. In this context, the use of the Tier one as a basis for measuring large exposures purposes could be considered given that Tier one aims at absorbing losses on a going concern basis.
However, as specified in the consultative paper, CRD II provisions have already significantly strengthened the large exposure regime by a multiplying factor of 5, especially in relation to inter-bank exposures. Further tightening would severely penalise the inter-bank market and could lead to undesired effects as banks may then seek to « diversify » their portfolio by lending to riskier counterparties. As a consequence the thresholds, should be increased substantially and in proportion to the change in basis used for identifying large exposure (as the response to the QIS will illustrate). The rationale is to enable insitutions to keep a lending capacity identical to the current CRD 2 level.

Question 23: What is your view of the purpose of contingent capital? What forms and triggers would be most appropriate?

Because the proposals on contingent capital are yet to be released for consultation, we would like to emphasize the following points, on a principal basis:

- To appeal to investors, especially traditionally debt-focused investors, triggers must be simple and completely transparent and predictable.

- The triggers that result in conversion or write-down must not be discretionary to avoid any market expectation that they might not be activated despite breach of conditions and that they will not be activated abusively. Requirements should not preclude for issuers in beach of the defined triggers some flexibility to implement alternative recovery plans before effective conversion or write down is activated.

- Discussions with investors and market participants make clear that triggers that depend on regulatory decisions will not be acceptable, because of the loss of transparency and predictability that leaving the decision to regulators, as much as to management, would imply.

- To be appeal to the deep market of debt investors, triggers will need to be set low enough that breach should only occur at a level that appears remote upon issuance: normally this would be when the issuer is in a state where recovery plans might need to be activated without the capital infusion offered by the conversion or write-down of the security.

- Only triggers related to the idiosyncratic conditions of a particular institution are likely to be attractive to the market.

- The contingency could be provided by conversion or by write-down; however, it should be made clear that, where write-down is the means of improving the firm's capital situation, write-up should not be precluded a priori. With supervisory approval of the form of instrument, there is no reason why write-up as the firm returns to health should be precluded.

Question 24: How should the grandfathering requirements under CRD II interact with those for the new requirements? To what extent should the grandfathering provisions of CRD II be amended to bring them into line with those of the new capital requirements under CRD IV?

1) We are puzzled by the question of how CRD II well defined grandfathering rules should interact with undefined and unknown grandfathering rules of CRD IV. The CRD II has introduced new eligibility criteria and grandfathering rules that have been built after wide industry consultations and quantitative analysis.

2) With respect to CRD IV grandfathering arrangements for non Core Tier-1 Capital and Tier-2 Capital, we strongly advocate to maintain the rules of CRDII and to align grandfathering rules of CRD IV, which are yet to be published.

3) The Basel CP 164 mentions 17 December 2009 as the starting date for possible grandfathering rules. It is worth to note that this has created much confusion in the market. Indeed, the new instruments features will be determined in the final Basel text to be published end 2010 or early 2011, and phased in as of end 2012 while, in the meantime, institutions need to continue issuing new instruments to comply with their Pillar 2 requirements, according to the usual RWA increase. It is also worth to note that from a legal point of view, CRD 2 is now becoming applicable in Europe and provides a grandfathering period starting December 31st 2010. For all these reasons, we urge both CEBS and BCBS to clarify urgently the intended grandfathering arrangements. We strongly advise that they should start when the rules will be applicable, while CRD II grandfathering rules should apply until then.

SECTION III: Leverage ratio

Question 25: What should be the objective of a leverage ratio?

We strongly put the leverage ratio concept into question as an effective way to control risks or improve the resilience of the banking sector:

The leverage ratio may have had its rationale in the "old good days" but is nowadays totally powerless to assess the leverage level of the economy. Except for its apparent simplicity, the Leverage Ratio has no objective and clear justification. No demonstration has been convincingly made of its ability to keep the leverage of the economy within a reasonable range compatible with the financial stability, in particular in the jurisdictions where it was in force such as the USA.

Taming excessive leverage may be legitimate in certain circumstances but cannot be only achieved through a single banking ratio. Such leverage ratio is harmful to the exit strategies of central banks as, commingled with the hardened solvency and liquidity ratios it will create conflicting pressures to reduce balance sheets, especially inter-bank money markets and repos which combine high volumes and low risks. It will also create a pressure to reduce lending and may thus be harmful to the economy.

Given the conceptual flaws of the leverage ratio, we are strongly opposed to a migration to Pillar 1. If a leverage ratio were to be imposed despite the lack of evidence as regards its efficiency, it should be maintained in Pillar 2.

The proposed leverage ratio has unclear objectives. Conceiving it as a possible Pillar 1 hard rule is an historic error and is totally at odds with the successive risk sensitive BCBS solvency reforms. It must solely remain a Pillar 2 indicator. The level of banks' leverage ratio is impacted by many external factors like the accounting and consolidation standards –for instance the accounting of repos- and the prudential rules for the valuation of assets, derivatives and other off balance sheet commitments.

The leverage ratio cannot be read, as well, without considering the banking business mix, the structure of the financial markets concerned, the level of intermediation, and the existence of actors absorbing part of banks' off-balance sheets. This analysis is all the more justified as the proposed crude approach inflates significantly the level of apparent leverage.

The ratio or rather its evolution needs therefore to be carefully interpreted by the supervisor in conjunction with other indicators before any conclusion can be drawn.

In any case the "crude and neutral" proposed definition of the leverage ratio is only conceivable as an undisclosed Pillar 2 indicator, as unless it is read in conjunction with other key risk indicators, it can be misinterpreted and in the end be completely misleading for the market.

Because of its complex interpretation, the concerns expressed above and its classification as a Pillar 2 component, we are strongly opposed to its disclosure as recommended by the CP and trust it should remain information only disclosed in the course of the dialogue with the supervisor.

Question 26: Which element of going concern capital do you consider would be a more appropriate basis for the leverage ratio? What is you rationale for this view?

Please refer to our comments on question 25

Question 27: What is your view on the proposed options for capturing the overall extent of an institution's derivatives business in the denominator of the leverage ratio?

Please refer to our comments on question 25

Question 28: What is your view of the proposed approach to capturing leverage arising from credit derivatives?

Please refer to our comments on question 25

Question 29: How could the design of the leverage ratio ensure that it would act as an effective constraint only in benign economic conditions?

Please refer to our comments on question 25

Question 30: What would be the appropriate calibration of a leverage ratio?

Please refer to our comments on question 25

SECTION IV Counterparty Credit Risk

Question 31: Views are sought on the suggested approach regarding the improved measurement or revised metric to better address counterparty credit risk. With respect to suggestion to incorporate - as an interim measure - a simple capital add-on by means of calculating the loan-equivalent CVA charge, views are sought on the implications of using VaR models for these purposes instead.

- On the Bond-Equivalent approach

- First of all, we want to stress that the proposed one year bond equivalent approach presents serious deficiencies. The associated methodology is totally inadequate as it is based on a wrong representation of the CVA risk, which does not reflect the real CVA sensitivities and precludes hedge recognition and impact. As a result, the required capital resulting from this approach amounts over tens of billions of Euros per significant bank and is clearly outrageous. A mere re-calibration would not address the wrong representation of the risk.
- More over, it leads to a full double counting of the risks which add-up to the double-counting already existing in the current framework. Indeed, if on top of the CVA, we put aside a capital charge to protect the bank against the potential increase of these CVAs during the coming year, it means that we put aside today not only the CVA, but this new capital charge as well. This means that we increase the double-counting which already exists since the CVA are not used to mitigate the counterparty risk capital charge. The more CVAs we have the less a loss due to default will affect the bank. The CVA plus this new capital charge are in total double counting with the current capital charge for counterparty risk (Expected Loss + Unexpected Loss).

- On the alternative approaches

- Industry practices are still very heterogeneous both in the way bank compute their CVAs and in their managing intent around CVAs. Therefore, if regulators want to capitalize CVAs as these can affect the bank's results, we strongly believe that this new capital charge should take into account the CVA framework in place so that the capital charge corresponds as much as possible to the real risk incurred by the bank.

- We also believe that the capital charge should take into account the managing intent of the CVA position. The same way a bond, dynamically hedged in the trading book, would be marked to market and would attract a market risk charge (now VaR, Stressed VaR and IRC), whilst a bond in the banking book could be valued in accrued and would attract a credit risk charge, the same way CVAs could be valued differently depending on their managing intent and would represent a very different risk for the bank. As a consequence, we believe that the managing intent should be taken into account to decide how to capitalize CVAs.

- If a bank decides to mark part of their CVAs to market and hedge them dynamically, these should be considered as a trading book position and their capital charge should address their potential spread risks in the same way than for any other trading book position. More specifically, we recommend that the regulatory capital on counterparty risks should be assessed by including the CVA (and all its single-name, credit index and other hedges) in the trading VaR, stressed VaR, and IRC frameworks. In this way, the CVA risks and hedges would be treated as integral parts of the full trading book and would be measured within the full trading book context. The banking book EPE-based charge should be eliminated for those banks. It is inconsistent with the way that the CVA

of those marked-to-market portfolios is managed and redundant with the IRC charge that already capitalizes the impact of default at a one year horizon. Moving to an integrated approach under the market risk framework would also allow mitigating the double counting issues highlighted in the first section.

- If a bank decides to carry part of their CVAs as a pure credit position which depends on historical probabilities, these should be considered as a banking book position which calculations are mainly driven by counterpart credit quality assessed through ratings. This impact can be broken down into two components:

  * The default risk which already adequately capitalised through the current counterparty capital charge,
  * The rating migration risk which will impact the CVA variability. This latest risk could be addressed using a separate charge similar (in terms of concept and method) to the IRC charge, but excluding the impact of defaults in the loss calculation (since it is already taken into account in the counterparty charge).

  In the same way the recognition of all hedges in the trading book proposed approach provides incentives to monitor and risk manage dynamically the counterparty risk and the CVA volatility, the use of CDS should also be recognised in the banking book approach as a strong mitigant to the counterparty risk. Such recognition could be achieved using either the double default framework or the substitution approach.

- Whenever the full trading book approach (VaR + sVaR + IRC) does not apply, the double counting issues raised in the bond-equivalent related paragraph must be addressed as in no real scenario, would a bank make a loss due to the CVA PLUS a loss at the time of default. Hence, and except in the full trading book approach, the new capital charge for the increase of CVA should be compared to the full capital charge for counterparty risk (EL+UL-CVA), and the maximum should be retained.

Question 32: Stakeholders are invited to express views on whether the use of own estimates of Alpha should continue to be permitted subject to supervisory approval and indicate any evidence in support of those views.

As a general principle, we think it is important to maintain incentives to adopt the more advanced approaches and risk management tools with the highest standards. In that respect, the use of own estimates of Alpha under tight control of Supervisors to demonstrate the robustness of the internal calibrations should continue to be permitted.

Question 33: Views are sought on the suggested approach regarding the multiplier for the asset value correlation for large financial institutions, and in particular on the appropriate level of the proposed multiplier and the respective asset size threshold. In addition, comments are sought on the appropriate definitions for regulated and unregulated financial intermediaries.

We recognise that there is some rationale, on past data and experience, to review the calibration of asset correlations for financial institutions. We regret the Committee has not further detailed the empirical evidence supporting the proposed figure of an increase of 25%, which would have allowed us to provide additional comments.

We point to the fact that this measure will penalise the inter-bank money market, which has already been hit by the strengthening of the large exposure regime under CRD II. Accordingly, we suggest careful consideration in the calibration of the measure that will be

detrimental to the implementation of central banks' exit strategies, as well as to the international trade and export financing.

Further, we note that the proposed measure has the following weaknesses:

- it is backward-looking: considering the numerous changes being implemented and/or considered in the banking sector structure and regulation, there is no reason to believe that past correlations are any guide to future correlations,

- it is very blunt as it does not differentiate between various business models across financial institutions (e.g. universal/retail banks vs brokers/dealers), and
- it provides perverse incentives as it penalises more significantly highly rated counterparties.

More generally we consider that additional work would be required to review the calibration of these asset correlations and we would strongly support that bank be allowed to model correlations internally as part of the IRBA approach.

From a more technical perspective, we suggest the following amendments to the Committee's proposal:

- Apply the size threshold to all counterparties, irrespective of whether they are regulated or not. In our view, the fact that a firm is regulated is not a significant driver of its systemic correlation and there is no convincing evidence in the recent crisis that small hedge funds are more correlated than small banks. Further this would avoid level-playing field issues as the definition of a 'regulated' institution may vary across jurisdictions.

- Use 'net asset value' as the relevant size metric rather than total assets. Indeed, 'total assets' is not a comparable metric across industry sub-segments (eg banks vs insurance) and may be largely distorted by differing accounting standards (eg IFRS vs US Gaap). We suggest using NAV (or total equity) as a better metric, using an adjusted threshold (eg $3b).

- Exclude mutual funds from the scope of the measure. Indeed, the recent crisis has not evidenced any specific risk issue with mutual funds, as they are remotely, if not at all, levered (most regulations such as UCIT will limit borrowing to 10% of total assets).

Question 34: Views are sought on the suggested approach regarding collateralized counterparties and margin period of risk. Views are particularly sought on the appropriate level of the new haircuts to be applied to repo-style transactions of (eligible) securitisations. In this context, what types of securitisation positions can, in your view, be treated as eligible collateral for purposes of the calculation of the regulatory requirements? Any qualitative and/or quantitative evidence supporting your arguments would be greatly appreciated.

While we welcome the principle of rules designed to strengthen collateral management units, processes and systems as this is a goal the industry has been consistently seeking during the last years, we think some of the proposed measures might lead to unintended and in fact, undesirable consequences.

This is particularly the case for the increase in margin period of risk when there are more than 5000 trades in a netting set. Experience during the Lehman bankruptcy does not show that the number of trades within a netting set increased the actual period of risk. We

furthermore believe this arbitrary threshold will only lead to firms splitting these netting sets into smaller ones, actually reducing the netting effect and increasing risk. We therefore strongly oppose the introduction of increased margin periods of risk for large netting sets.

With regard to the other circumstances leading to increased margin period of risks, we first want to highlight that the Industry – led by ISDA - has been very active in improving the time for resolution of a dispute through the implementation of the Dispute Resolution Protocol.

We would also suggest introducing a materiality threshold to avoid spill-over or cliff-effects because of a few minor disputes that happened in the past. Such thresholds will be included in the Dispute reporting framework the ISDA Steering Committee will be proposing to Regulators by May 31st and we suggest using these thresholds when determining whether the margin period of risk should be doubled or not.

On the illiquid OTC derivatives or collateral, we support the proposal of doubling their margin period of risk, but we would recommend using a more widely accepted definition of illiquidity (such as level 3 assets) and introducing materiality thresholds in a similar way than for disputes.

Question 35: Views are sought on the suggested approach regarding central counterparties and on the appropriate level of the risk weights to be applied to collateral and mark to market exposures to CCPs (on the assumptions that the CCP is run to defined strict standards) and to exposures arising from guarantee fund contributions.

We believe it is important that a clear and robust regulatory framework applies to CCPs. In that respect, we welcome the set of international recommendations that the Committee on Payment and Settlement Systems (CPSS) and the International Organization of Securities Commissions (IOSCO) that are being up-dated and enhanced, along with the risk management elements that are described in paragraph 120.

We also think it is important to create strong incentives for CCPs to comply with those strict standards and for market participants (and by extent, their clients) to privilege facing those CCPs. In that respect, it is definitely appropriate that banks counterparty credit exposures to CCPs exhibiting strict standards attract a 0% risk weight.

We think that regulatory incentives should indeed push towards central clearing on the following basis:

- no regulatory charges for cleared trades,
- risk weight for bilateral trades are already higher than for CCP cleared trades and they will probably increase due to the counterparty risk adaptations proposed in CRD 4 (higher capital requirements for exposures between financial institutions).

We support the view that:

- there should be a link between capital requirements and risk; i.e. future capital requirements for OTC derivative contracts non-cleared through CCPs should reflect the actual level of risk and not be artificially higher;
- capital requirements for non-CCP cleared contracts should not be punitive as it would artificially raise the cost of the products that may not be eligible to CCP, or cannot be cleared on CCP for risk management reasons.

We strongly suggest the European Commission to examine the CRD4 consequences on capital requirements for central counterparties together with the future European Market

Infrastructures Legislation and conduct a comprehensive impact study taking into account both texts.

Question 36: Views are sought on the risk management elements that should be addressed in the strong standards for CCPs to be used for regulatory capital purposes discussed above. Furthermore, stakeholders are invited to express their views whether the respective strong standards for CCPs to be used for regulatory capital purposes should be the same as the enhanced CPSS-IOSCO standards.

We think CCP primary objectives should be the following:
- CCP must be safe, efficient and reliable,
- CCP must contribute to trade processing rationalisation for OTC transactions,
- CCP must mitigate systemic risks, in particular in a crisis situation.

To reach these objectives, a CCP must be based on the following criteria:
- They must accept "quality" clearing members only, i.e. have high-standard and clear admission criteria tailored by asset classes and based upon factors such as capitalisation, rating and technical competencies.
- The risk management of the CCP should be robust, i.e. sufficient margining to absorb multiple simultaneous defaults; transparent margining methodology; strong risk infrastructure systems, daily and intraday margin call and collateral management; effective, transparent, documented and tested default management process; separate default fund per asset class to avoid "spill over" effect.
- CCP must retain a clear account segregation between its clearing members, including segregated buy-side accounts to ensure portability;
- CCP should have access to central bank liquidity provision in order to ensure its stability in case of liquidity squeeze

In order to ensure a level playing field and a coherent application of strong risk management principles for CCPs, the standards for CCPs to be used for regulatory capital purposes should be the same as the enhanced CPSS-IOSCO standards.

Question 37: Views are sought on the suggested approach regarding enhanced counterparty credit risk management requirements.
Do the above proposed changes to the counterparty credit risk framework (in general, i.e. not only related to stress testing and backtesting) address fully the observed weaknesses in the area of risk measurement and management of the counterparty credit risk exposures (both bilateral and exposures to CCPs)?

We fully support the goal of enhancing counterparty credit risk management requirements, in particular in terms of set-up and organisation. Most, if not all, of the proposed standards are consistent with our own set-up and we believe it is important for the stability of the whole system that such standards and best practices are widely shared and implemented.

With regard to the quantitative requirements and namely the new rules on VaR on CVA and increased margin period of risks, we tried to highlight in the previous answers the various flaws and unintended consequences they might trigger.

- The VaR on CVA capital charge, on top of leading to outrageous capital requirements, is simply disconnected from the risks it seeks to capture and gives no incentive for proper risk management.

- The triggers for increased margin period of risks, in particular the number of trades per netting set, are likely to lead to undesirable avoidance tactics, which will reduce the netting effect and increase the risk.

- We also note that the introduction of a stressed EPE concept will raise a number of operational issues such as use-test difficulties and negative impact on filters at origination set-up. We therefore oppose the principle of two calculations (stressed and current) and recommend instead one single calibration on a period covering a full economic cycle <u>and</u> the stressed period used for the stressed var. This would allow achieving the objective of stressing the EEPE without the negative operational consequences linked to a dual computation.

- Finally, we support the measures related to the general and specific wrong way risk on the principle as they are widely consistent with sound risk management practices. As far as specific wrong way risk is concerned, we recommend however the use of an "own risk based assessment" for correlation between the underlying and the counterparty as we think the "legal connection" criterion is too vague and sometimes mis-represents the correlation risk. In addition, we think the exposure should be commensurate with the risks and not necessarily set at 100% of the notional, hence:
  - whenever there is a degree of decorrelation between the underlying and the counterparty, this should be reflected in the exposure,
  - we oppose the use of notional for CDS presenting wrong way risk and propose to use the jump-to-default measure instead. Indeed, CDS are more and more traded on an up-front basis implying that the maximum loss is much lower than notional.

Beyond these technical issues, we are worried to observe that the proposed measures are mostly impacting banks under the most advanced approach, with no visibility on how and when a recalibration of the standardised approach would be envisaged.
This fails to create the right incentives to move to more risk sensitive approaches and hence improved risk management standard.

As a conclusion, we still believe that the overall counterparty risk capital framework is far from being consistent with the way Banks manage their counterparty risk, especially for those who had massively invested in risk management set-ups and systems to properly monitor and mitigate their counterparty risk. We therefore urge Regulators to engage in a global revision of this framework (similarly to what is being undertaken for market risk), with a view of migrating counterparty risk into a more integrated market risk approach for banks which dynamically manage their CVAs.

SECTION V: Countercyclical measures

Question 38: The Commission services invite stakeholders to perform a comparative assessment of the three different methods (ie ECF, incurred loss and IRB expected loss if it could be used for financial reporting) for credit loss provisioning from 2002 onwards based on their own data.

We have no mean to move down to 2002 and to estimate what scenarios would have been retained in order to evaluate expected losses under the different methods to be assessed. Furthermore, the proposals in the IASB ED raise practical issues making these proposals complex and difficult to be implemented due to the need to completely revise the methodology for effective interest rates and the need to define expected cash flows by time period whereas entities manage expected losses and due to insufficient modelling capabilities.

Question 39: Views are sought on the suggested IRB based approach with respect to the through-the-cycle provisioning for expected losses as outlined above.

General comments on forward looking provisioning

The French Banking Federation has pinpointed, since 2002, the weaknesses of the IASB'incurred losses model for provisioning credit risk. The crisis confirmed our analysis: during the period 2005-2006, banks have to release previously built provisions due to the benign economic conditions, when in same timeframe, their loans portfolios were growing significantly. Therefore, we are in favour of a more forward looking approach that suppresses the overstatement of interest revenues in the periods before a loss event occurs.

The IASB provide with a proposal based on an expected loss approach, but, in our views, the exposure draft 2009/12 presents three fatal flaws:

- The use of TTC parameters is prohibited, though nobody is able to predict the behaviour of the economic cycle through the whole life of most loans portfolios. PIT data will lead to a sharp increase in procyclicality of banks'provisionning
- Changes in expectations for losses are recorded immediately always in P& L, despite the fact that risk premiums included in interest revenues are collected over the loans maturities.
- Credit losses are incorporated in EIR calculations, even it is impossible to predict accurately when the expected losses will occur. Furthermore, this methodology raises huge operational challenges.

European Banking Federation is currently developing an alternative to this model, aimed at achieving the same objective, without these drawbacks.

The main features of this project, sponsorized by all Europeans Banking Federations, are:

- Historical losses experience provides the basis for estimating expected losses. French Banking federation is of view that, in most circumstances, TTC Basel 2 parameters, are the best proxy for historical losses experience
- Parameters are adjusted to reflect changes in credit policies distribution
- The corresponding provision is built over the average life of the portfolios
- Portfolios are defined according to the Basle segmentation standard approach

- Adjustments to expectation are spread over the remaining life of the portfolio until a threshold to be defined. Significant adjustments may have to be taken in full in P&L as they occur
- Incurred losses (defined as now in IAS 39, excluding IBNR losses) are booked against the corresponding expected loss allowance.

We think that this model has to be developed to achieve sound expected loss provisioning approach. We notice that it is fully compliant with the six principles adopted by BCBS in this matter.

As the accounting calculation of expected loss will be built over *at termination*, we expect the prospective provisioning framework to produce an excess of provision over the Basel 2 one year Expected Loss benchmark.
Under the current Basel 2 rules, this excess will only be recognized as Tier Two capital and capped.
We therefore ask, if the new accounting rules once stabilised confirm the contemplated orientation :
1) for a revised prudential mechanism which will allow, through a filter, to include this excess of provisions in the Core Tier One (as these amounts would have impacted the earnings and therefore depleted directly the Core Tier One), at least during down turn periods when the prospective provision is inflated by the high incurred specific provisions;
2) and, in addition, the suppression of the 0.6 % cap based on risk weighted assets.

Regarding the CRD proposal, we believe that the system would need a ceiling in order to avoid the building of an excessive provision compared to the actual risk of the portfolio. Indeed, it is likely that the implicit conservative bias that exists in most Basel II parameters will result in a higher provision than what would be necessary to cover a crisis. Given that the CRD approach only deals with flows and not with the total amount of the provision, there is no mechanism that would correct this drift other than imposing a ceiling on the total amount of the provision.

Question 40: Do you agree with the proposed dual structure of the capital buffers? In particular, we would welcome your views on the effectiveness of the conservation buffer and the counter-cyclical buffer, separately and taken together, in terms of enhancing the resilience of banking sector going into economic downturn and ensuring the flow of bank credit to the "real economy" throughout economic cycle.

Question 41: Which elements should be subject to distribution restrictions for both elements of the proposed capital buffers and why?

Question 42: What is the appropriate timing – following the breach of capital buffer targets – for the restriction to capital distributions to start? Should the time limits for reaching capital buffer targets be determined by supervisors on a case-by-case basis or harmonized across EU?

Question 43: What is the most suitable macro variable (or group of variables) that may be used in the counter-cyclical buffer to measure the dynamics of macro-level risks pertinent to the banking sector activities?

Question 44: What are the relative merits and drawbacks of capital buffers versus through-the-cycle provisioning for expected losses with respect to minimizing procyclical effects of current EU banking regulation?

Global answer to question 40 to 44:

Capital buffers through capital conservation

The French banking Federation welcomes the explicit recognition that as a general matter buffers should be designed to be drawn down during bad periods.

However, we do not understand how the objective of this measure will really be achieved and are highly skeptical as to the potential effectiveness of this approach: banks will be allowed, neither by their supervisor nor by the market, to use their buffer when the economic situation gets worse. As experimented during the crisis, market participants, investors and rating agencies expect banks to hold *additional* capital and not less capital during times of economic stress conditions. Thus, buffers being in effect unable to be used would inevitably become another layer of capital requirement, above the minimum capital requirement set by the regulators. Combined with the other measures regarding liquidity, leverage ratio and new capital requirements, it will force banks to reduce tremendously new lending to the economy.

Furthermore, we can argue that this measure is contrary to our legal framework where distributions of earnings are determined by the shareholder's representatives. The intrusion of the supervisory bodies in the banks' management seems to us excessive and fundamentally not consistent with the independence principle between the supervisors and the entities they control.

Besides, we consider that the application of any potential measure developed in this area is meaningless at a solo level.

To summarize our views :
- we consider that such a provision should not be anything else than a Pillar 2 requirement.
-we observe that a number of the banks which weathered the financial crisis well had discretionary buffer in place over the minimum capital requirements, grounded in effective utilization of the Pillar 2 process.
- our feeling is that the best way to tackle this issue is to improve the proposed accounting standards on forward looking provisioning so that they become in line with the prudential point of view. There will then be no need for additional prudential rules (see above).

Question 45: Do you consider that it would be too early to fully assess the cyclicality of the minimum capital requirement?

Cyclicality of the minimum requirement

The French banking Federation believes that the Basel 2 framework, if correctly implemented, has not demonstrated nor shown in actual data any material pro-cyclical effect.

The Basel 2 framework has introduced a great number of safeguards against excess cyclicality (long term data horizons to estimate PD, downturn LGD, stress tests considering downturn migration, etc…).

Moreover, the use of the highest average PD estimate or the average of historic PD estimate to each of the bank's exposure classes would be a strong disincentive to review obligor's ratings and would not meet the 'use test' requirement.

We believe that the whole concept that aims to correct the assumed pro-cyclicality of the Basel 2 framework is not well-founded. We reject it as such but would favor measures allowing banks to build up reserves in good times for the bad times (see above).

We urge the Basel Committee to require all countries to be compliant with the Basel 2 requirements, in particular as far as the “through the cycle” concept for Basle 2 parameters and the Pillar 2 requirements.

Addendum on Excessive credit growth

We agree that one of the lessons of the financial crisis is the need for macro-prudential regulation with a view to control the supply of credit to the economy.

This being said, the proposal to limit the excessive credit growth is very imprecise both in its content and its scope. Neither the definition of any potential use of buffers for macroeconomic purposes, nor the macro variables to be considered are sufficiently clear to enable us to support this approach. We think that further consideration is needed in order to determine the right approach to the macroeconomic use of additional capital buffers. We advocate not proceeding at this stage with concrete proposals and spending enough time to address this issue.

Once more, our feeling is that the best way to tackle cyclicality issues is to improve the proposed accounting standards on forward looking provisioning so that they become in line with the prudential point of view. There will then be no need for additional prudential rules (see above).

SECTION VI: Systemically important financial institutions

Question 46: What is your view of the most appropriate means of measuring and addressing systemic importance?

The 2007-2008 financial crisis highlighted the importance of systemic risk and the need to make plans to deal with it as best as possible. However, the term covers two somewhat different, albeit connected, real risks. The first is **market risk**, which was clearly at the heart of the crisis. The second is **institution risk**, related primarily to their size (concept of institutions "*too big to fail*"). This is the risk most frequently evoked, but all too often it is questionable.

In fact, an examination of the crisis reveals that while the public authorities had to intervene to rescue several institutions given the potential impact of their collapse, the cause of the systemic risk was first and foremost the functioning of the markets in which they operated with their interconnection and lack of transparency. The prime market concerned was the structured products market (CDOs, CMOs etc.), the direct cause of the crisis: these markets which were subject to no form of supervision almost totally disappeared in the space of a few weeks, whereas the products in question were placed in trading portfolios and were supposed to be booked at their market value. Moreover, these products were often held in entities (SIVs etc.) that had been withdrawn from bank balance sheets, and not factored into ratio calculations. The next market concerned was the CDS market, which remained active but because of a lack of registration was subject to no supervision by the authorities. This enabled some institutions such as AIG to play a disproportionate role and, more importantly, meant that these products were not cleared, creating, between all the institutions, an accumulation of reciprocal counterparty risks without any economic usefulness.

In this context, the systemic importance of some institutions resulted primarily from the malfunctioning of these huge, unregulated markets, as well as the incorrect strategic decisions made by their management, reinforced or at least tolerated by a weak supervision system. All of which effectively placed the governments of these institutions' host countries in the unacceptable position either of not intervening at the risk of triggering an uncontrollable financial panic, or of committing public resources to ensure the proper unwinding of these unjustifiable positions.
Getting out of this dilemma is a question that does not even arise. However, this will not be achieved by increasing minimum solvency ratios by a few points, nor by recommending the specialisation of institutions, nor by reducing the size of the largest of them. The institutions that were at the origin of the various stages in the worsening of the crisis, were nearly all relatively small, specialised, and well capitalised (*Northern Rock, Bear Stearns, Lehman Brothers*). The same can be said of the monolines. Only AIG was large-scale but its bankruptcy was due mainly to aberrant, unmeasured diversification, which indicates both an error by the management and a failure by the regulators.

Question 47: How could the Commission services ensure a consistent prudential treatment of systemic importance across financial sectors and markets?

A three-pronged approach is advisable:

- *reforming the operating method of significant markets* that are currently unregulated, since this was the prime cause of the crisis;

- *implementing effective supervision, on a consolidated basis, of all players* involved in a banking or market activity, whatever their legal status, without confining oneself to one individual category of institution defined by size, status or any other factor;

- *organising the orderly liquidation of insolvent financial institutions*, in an identical manner whatever their size, so as to be able to intervene rapidly while at the same time eliminating the moral hazard risk. It is only at this price that the measures to enhance capital requirements, which moreover have already been decided in order to remedy obvious inadequacies in such or such activity (such as the underweighting of market activities), will be effective in preventing the next financial shock, even limited, from being transformed, as in 2008, into a general banking crisis. However, the creation of a specific category of so-called "systemic institutions" is unlikely to provide a convincing solution, and could even be counter-productive.

SECTION VII: Single rulebook and other issues

Question 48: In which areas are more stringent general requirements needed given national or other circumstances? Is Pillar 2 a sufficient tool to address specific negative circumstances at credit institutions and if not, how could it be strengthened?

First we welcome the initiative of the Commission to remove options and national discretions. We agree that a single rule book does not mean uniform rules and that in some fields national regulators could implement stricter rules if they consider it to be necessary to maintain financial stability. The recognition of the diversity of legislation in place should also be taken into consideration within the harmonized framework since they can lead to very different nature of risk assessment.

We believe that Pillar 2 seems to be an efficient and sufficient tool to anticipate particular risks.

Question 49: What is your view of the suggested prudential treatment for exposures secured by mortgages on residential property outlined above? What indicators and their respective values do you consider appropriate as possible preconditions for the application of the preferential treatment of exposures secured by mortgages on residential property?

For residential real estate, instead of « *exposures secured by mortgages* », it would be more appropriate to add « *or similar sureties*» because this text does not take into account national schemes, which were very efficient during the crisis and led to a level of risks equivalent to ordinary mortgage portfolios.

<u>LTI and LTV ratios</u>

The French banks are not favourable to an alignment of LTV nor LTI. LTI would be more in line with the origination practise in France but would be very difficult to follow during the life of the loans.

With regard to qualifying lending criteria, it is important to note that French banks have developed a lending approach based on the client's ability to repay its loan rather than on the property's value and its evolution.

It is therefore not unusual that the Loan To Value exceed 80%, at least at origination. Also, because of specific tax incentives on rented property, investments in rental property may be eligible to a LTV in excess of 100%.Consequently, introducing normalised or maximum LTV ratios could be highly detrimental to housing policies geared at promoting home-ownership and home-building. It could prompt banks to restrict this type of lending or lead them to increase the interest rate margin on certain type of loans.

Besides, there are specific legal specificities in France that make LTV ratios less relevant: in case of a default, lenders have by law recourse on other assets of the borrower (ie beyond the property financed) even though those assets were not originally pledged. As a result, , the concept of LTV appears from a prudential perspective basis less relevant in France than in other jurisdictions. This point should be confirmed by the answer to QIS.

Imposing a minimum LTV could actually be counterproductive as it may result in reducing lending to customers which represent a sound risk profile based on their income or other assets. Again, reasoning on the basis of the LTV appears unjustified in France in so far as banks take lending decision based on the borrower's ability to repay.

We also dispute the proposal to set an harmonised debt limit. Not only will it very difficult to agree on an harmonised definition of LTI across Europe (due to different methods for calculating debt to income ratio, large variations in the level of gross income, taxes, average household debt ratio…), but the risk will remain that such a measure exclude categories of clients representing a sound risk, in spite of a relatively high debt to income ratio. This may be the case of young borrowers with high potential for income increase in future years or borrowers with large estate capable of sustaining a high debt to income ratio.

In some countries (such as France since 1989), banks are already under an obligation to monitor excessive indebtedness and can be held responsible if they fail to perform this role (as evidenced by the case law concept of "duty to alert").

Finally evidence suggests that excessive indebtedness among French individual borrowers is not due to a drop in real estate value or excessive LTVs: in more than two out of three cases, illness, unemployment, divorce, are the main causes for unsustainable indebtedness.

Question 50: What is your view of the suggested prudential treatment for exposures secured by mortgages on commercial real estate outlined above? What indicators and their respective values do you consider appropriate as possible preconditions for the application of the preferential treatment of exposures secured by mortgages on commercial real estate? In particular, are additional preconditions needed to ensure the soundness of this treatment? Do you believe that the existing preferential risk weight applied to exposures secured by mortgages on commercial real estate should be increased?
For both questions, any qualitative and/or quantitative evidence supporting your arguments would be greatly appreciated.

Similarly to residential mortgages, we consider that real estate markets are very much country-specific and that there is no economic rationale to use a unique LTV threshold across member states.

We also stress that financing is more frequently secured by the revenues generated by the borrower's commercial business rather than the value of the property. Accordingly, LTV ratios are not necessarily the most relevant metrics to assess the risk profile.

We do not see any rationale for modifying the existing preferential risk weight applied to exposures secured by commercial mortgages.

Question 51: Should the prudential treatment for exposures secured by mortgages on residential property be different from the prudential treatment for exposures secured by mortgages on commercial real estate? If so, in which areas and why?

The prudential treatment for exposures secured by mortgages on residential property and mortgages on commercial real estate is already different.

We consider that residential mortgages, when meeting the current qualitative requirements of the CRD, exhibit lower risk level than commercial mortgages and should accordingly receive a lower risk weight.

In most of the member states markets, sociological studies demonstrated that the attachment of the borrowers to the residential property is such that it explains the particularly low level of risk generally observed. This feature also motivates a distinction in the prudential treatments of these two lending activities.

Question 52: What is your view of the merits of introducing measures that would help to address real lending throughout the economic cycle? Which measures could be used for such purposes? What is your view about the effectiveness of the possible measures outlined above?

Concerning economic cycle, the option of LTV does not seem to be a relevant idea.
The French banks have proved their resilience during the worst period of the cycle without this type of measure.
We suggest promoting or reinforcing death, invalidity, sickness or unemployment insurances in order to secure income. Moreover, we stress that a guarantee fund such as Crédit Logement or other players (like insurance guarantees) is a powerful damper.

We do not think that a contra-cyclical feature should be included at the level of RWA (Risk weighted Assets) calculation. We favour a contra cyclical feature within a dynamic provisioning approach.

Appendix: Detailed Comments on the CRD IV Public Consultation (PC)

LIQUIDITY RATIOS

The table below details FBF comments on each PC paragraph

Topic	§ #	Comment
General	2	A harmonized regulatory treatment would certainly help increasing banking industry resiliency to a systemic crisis. However, harmonized regulatory treatment is different from one-size-fits-all standardized risk metrics.
General	3	LCR and NSFR should be seen in combination: NSFR should ensure that the liquidity risk is soundly and sustainably managed over a one year horizon; LCR is an additional test to ensure that the bank is resilient enough to a one month acute stress test scenario.
General	3	If one of the two requirements is not met, the bank should be responsible for setting up a restoration plan that *it* would have to present to competent authorities. The wording "competent authorities would be required to define a restoration plan and to follow its implementation up" is misleading and could be interpreted as a take-over by the "competent authority".
LCR	4	The one-size-fits all assumption set that would define the LCR cannot represent the specificities of all banks whose businesses, management, organizations are different in many ways.
LCR	5	Experience derived from that crisis that began mid-2007 should be used as much as possible. However, this calls for two remarks. The first remark is that this crisis has been the most acute for nearly one century. Fixing the risk aversion at this severity level will have consequences on banks' funding capacities that have to be well understood and chosen by stakeholders well beyond the banking industry. The second remark is that combining each of the most severe assumption, even though actually observed individually for specific banks, compounds the severity level to a level that is not consistent with the actual experience.
LCR	5	Liquidity risk regulation has to be consistent with legally binding commitments: the "non contractual obligations" should be part of the risk appetite that each bank is willing to determine. Note that, should there be a regulation for "non legally binding commitments", they would become "legally binding", which is inconsistent.
LCR	6	For sure, liquidity risk has to consider currency break down, and buffers have to be usable in a stress test scenario. The "supervisory review" needs to be elaborated further, notably to make sure that trapped pools of liquidity are not required when the liquidity can be drained to where it is needed in a crisis.
LCR	7	In a market-wide liquidity stress test scenario, central banks should be part of the crisis managing stakeholders: central bank eligible assets should be part of the LCR-liquidity buffer. Counting on market liquidity to mitigate a market liquidity crisis is simply inconsistent. Excluding central bank from crisis managing stakeholders would actually increase systemic risk. In a market wide crisis, all banks would be led to sell the very same assets, which would have vicious circle effects: sales => lower prices => lower liquidity => decrease in liquidity buffer => need for

		more sales. Moreover, a large sale of LCR-liquidity buffer assets could be misinterpreted as signalling a liquidity crisis, and ignites an actual liquidity crisis: this is all the more possible as the LCR-liquidity buffer is narrowly defined and as market mechanism to mitigate a liquidity crisis is assumed.
LCR	7	Widening the far too narrow defined BCBS High Quality Liquid Assets that qualify for liquidity buffer is necessary and welcome. Conversely, if assets are excluded from the liquidity buffer, notably due to "an additional characteristic to be eligible as collateral for central bank credit operations", they should be fairly recognized their market liquidity in the cash inflow factors in the denominator of the LCR. We recommend that central bank eligibility is not an additional criterion but constitutes a *sufficient* criterion to qualify as a LCR-liquidity buffer asset. Within these central bank eligible assets, EBA could restrict the assets that could qualify as LCR-liquidity buffer assets. This would give EBA a very monetary policy like tool to lean on liquidity risk management.
LCR	7	To the extent that there is no restriction to the flow of liquidity, EU subsidiaries' excesses of their liquidity buffers over their liquidity needs (their net cash outflows) should benefit the other Group entities the excess can be passed to (no cap should apply)
LCR	8	cf our comment on paragraph 7: 1. Central bank eligibility should be a sufficient criterion to qualify for LCR-liquidity buffer 2. Within the central bank eligible assets, EBA could restrict the list of assets qualifying for LCR-liquidity buffer 3. The assets that are not qualifying for LCR-liquidity buffer should be recognized their market liquidity in the LCR-cash inflow factors. 4. To the extent that there is no restriction of flow of liquidity, local excesses of local liquidity buffer over local cash outflows should benefit the other Group entities the excess can be passed to.
LCR	9	We fully concur with the objective of striking the right balances between: severity of stress test scenarios bank are required to resist to, the definition of LCR-liquidity buffer assets, incentives for bank for prudent funding liquidity profiles.
LCR	10	For references to BCBS assumption sets, please refer to our response to BCBS Consultative Paper that is attached to this response.
NSFR	12	Liquidity risk regulation has to be consistent with legally binding commitments: the "non contractual obligations" should be part of the risk appetite that each bank is willing to determine. Note that, should there be a regulation for "non legally binding commitments", they would become "legally binding", which is inconsistent.
NSFR	12	For references to BCBS assumption sets, please refer to our response to BCBS Consultative Paper that is attached to this response.
Completeness of Legislative Approach	13	Even though BCBS assumption sets are tentative so far, there's no reason to commit to consider them as floor/cap EU assumption sets, provided that a strong enough rationale for departing from BCBS suggested assumptions sets.
Completeness of Legislative Approach	13	For references to BCBS assumption sets, please refer to our response to BCBS Consultative Paper that is attached to this response.
Completeness of Legislative Approach	14	We support the EU Council's desire for a Single Rule Book, without proliferation of new national options and discretions, and to elaborate a supervisory framework that could be timely adapted down the road.
Completeness	14	Attention will need to be paid to ensure level playing field: in EU with non

of Legislative Approach		EU credit institutions, and outside EU where EU-banks are active in.
Scope of Application	15	Should they apply to each individual entity in a Group, NSF and LC requirements would be highly disruptive when denying actual liquidity risk management. Within a harmonized regulatory zone, regulation should not be required at sub level.
Scope of Application	15	We suggest that requirements apply to combinations of group entities provided that: 1. there is no restriction of flow between the different entities (asset transferability is not a requirement if it can be substituted with cash transferability) 2. there are legally binding commitments between entities that make sure that they can be seen in combination from both a business as usual and stress test scenario perspectives,
Scope of Application	17	We fully support the application of requirements at combinations of entities, rather than at each entity level.
Scope of Application	17	We suggest that requirements apply to combinations of group entities provided that: 1. there is no restriction of flow between the different entities (asset transferability is not a requirement if it can be substituted with cash transferability) 2. there are legally binding commitments between entities that make sure that they can be seen in combination from both a business as usual and stress test scenario perspectives,
Scope of Application	17	The waiver mechanism has to be elaborated further.
Scope of Application	18	The waiver mechanism has to be elaborated further.
Scope of Application	19	The transferability of assets is not the exclusive criterion to consider. The LCR-liquidity buffer comprises not only assets but short term lending that do not need to be "transferred" to mitigate a liquidity crisis.
Intragroup	21	The asymmetries that apply to intra-group transactions are inconsistent and deny legally binding commitments, both of which we disagree with.
Intragroup	21	Liquidity risk regulation has to be consistent with legally binding commitments: the "non contractual obligations" should be part of the risk appetite that each bank is willing to determine. Note that, should there be a regulation for "non legally binding commitments", they would become "legally binding", which is inconsistent.
Intragroup	22	We support that intra-group transactions should be dealt with symmetrically.
Intragroup	22	Liquidity risk regulation has to be consistent with legally binding commitments: the "non contractual obligations" should be part of the risk appetite that each bank is willing to determine. Note that, should there be a regulation for "non legally binding commitments", they would become "legally binding", which is inconsistent.
Intragroup	22	LCR and NSFR assumption sets should be consistent with legally binding commitments, and should not be denied. Subject to being consistent with legally binding commitments, symmetric assumptions on intra-group transactions need not be predetermined in the regulation.
Intragroup	22	There is no reason to impose that "*It would however not give any credit for a central pool of liquid assets as the entities would be assumed not to be able to draw on that central pool*". When operational set up have been developed to mitigate a liquidity crisis by transferring assets from one entity to another, it should be recognized by regulation. Diversification in mitigation strategies among different banks is part of

		mitigating systemic risk.
Intragroup	23	LCR and NSFR assumption sets should be consistent with legally binding commitments, and should not be denied. Subject to being consistent with legally binding commitments, symmetric assumptions on intra-group transactions need not be predetermined in the regulation.
Intragroup	24	LCR and NSFR assumption sets should be consistent with legally binding commitments, and should not be denied. Subject to being consistent with legally binding commitments, symmetric assumptions on intra-group transactions need not be predetermined in the regulation.
Branch Liquidity Supervision	25	We support a regulatory framework that would be consistent with actual liquidity risk management.
Branch Liquidity Supervision	25	De facto, EU regulation that will apply to branches will set precedent for non EU branches. The branches' supervisors will call for the exactly the same rights. That's why the suggestion that is elaborated at the end of the paragraph is not satisfactory ("They could for example entail - for significant branches - full ongoing access by the host supervisor to the home country supervisory reporting and the monitoring tools discussed in points 28 and 29."). We suggest that the College of Supervisors is used.
Branch Liquidity Supervision	26	The legal framework that is described in this paragraph (§26) should apply now.
Branch Liquidity Supervision	27	We support a regulatory framework that would be consistent with actual liquidity risk management.
Branch Liquidity Supervision	28	We support a regulatory framework that would be consistent with actual liquidity risk management.
Monitoring Tools	29	We support a regulatory framework that would be consistent with actual liquidity risk management.
Monitoring Tools	30	The contractual mismatch does not bear relevant information, neither for actual liquidity risk management, nor for regulation, and is misleading if it was required to disclose. We suggest suppressing this tool as a relevant monitoring tool.
Annex - Additional monitoring tools	I-II III	Please refer to our response to the BCBS CP