Subject: Comments on proposed changes to the Capital Requirements Directive

Dear Madam or Sir,

National Bank of Slovakia welcomes the opportunity to comment on the European Commission´s proposal for an amendment to the Capital Requirements Directive.

The proposed changes, in particular to large exposure rules and supervisory arrangements, could have a signifacant impact on financial stability and the quality of supervision in countries where there is a large subsidiaries foreign banking presence.

With regard to the ongoing discussion, we would like to explain our position in enclosed comments.

Should you need any further information, please do not hesitate to contact me.

Yours faithfully,

Martin Barto
Deputy-Governor
National Bank of Slovakia

NATIONAL BANK OF SLOVAKIA

Martin Barto
Deputy - Governor

Bratislava, June 12, 2008

Current position of National Bank of Slovakia regarding public consultation on possible changes to the Capital Requirements Directive (CRD, consisting of Directives 2006/48/EC and 2006/49/EC)

Implementation of CRD in Member States indicated a need for changes in the Directive and certain clarification of technical details. We support majority of proposed changes. However we would like to describe our concerns regarding to intra-group exposures and supervisory arrangements and propose changes of text in the final proposal of the CRD.

Large exposures

Article 113 (f) - intra-group exposures

Although the **elimination of intra-group large exposure limits** (however contingent upon fulfilment of conditions stated in Art 80.7, except for point (d), or in Art. 80.8 of CRD) could increase the efficiency of the allocation of fund surpluses throughout the group, we are deeply concerned about **the increase in potential for brand contagion throughout the group and consequently across all national (interbank) markets where the related group is present**.

Wholesale counterparties – being aware of **no** or (potentially) **high** intra-group limits – **would** in our opinion **react more sensitively to any "bad news"** or even **rumours concerning none but one entity belonging to the same group as a borrowing bank** (regardless of the national market on which a hit entity operates or is incorporated). In this connection there is a major threat that **lenders outside the group would automatically increase the borrowing costs** (or even cut credit lines) for a bank inside a group as a consequence of a failure of any entity belonging to the given group. The reason for such behaviour is given by the fact that **the lenders would run the risk that just its borrower is excessively exposed (directly/indirectly) to the distressed entity**.

In this way, we suppose, **the contagion would spread more easily throughout the group** and concurrently **throughout the individual (national) interbank markets** across EU **than** it is the case of the current regime (provided that ND is not applied) under which **the intra-group exposure to another (potentially stricken) entity is transparent and reasonably limited.** It means that the intra-group large exposure limit has now **the function of firewall** which protects each group member from any (potential) risk related to the rest of the group.

In addition to this, we fear that the **regime without strictly defined backstop limits** on intra-group (large) exposures **would allow subsidiary bank to become excessively exposed to its parent bank**. If this were the case, **the insolvency of parent bank** (e.g. due to suddenly uncovered fraud) **would almost automatically lead to the insolvency of its otherwise sound subsidiary bank**.

Taking into account the above-mentioned facts, you may easily come to the conclusion that the efficiency of a group could only be increased (through elimination of intra-group large exposure limit) **at the expense of vulnerability** of individual group members (vulnerability to malaises occurred on whatever market where the given group is present). This could eventually facilitate **the spill over of crisis** from one Member State's market into another one. **The mitigation of the mentioned implications could present – under stressed conditions – the significant costs** (e.g. provision of Emergency liquidity Assistance or funds from deposit-guarantee scheme, etc.) **to Member States´ taxpayers.** As the cost/benefit ratio varies across the EU (e.g. in countries where there is a large subsidiaries foreign banking presence **the given costs would only be in very small part offset by the related benefits**), we strongly believe that each of the Member States should have the right to decide whether or not to eliminate the intra-group large exposure limit.

We are strongly in favour of National Discretion in this regard and so we propose retaining Art. 113 (2) in its original form (i.e. "Member States may fully or partially exempt…").

<u>Supervisory arrangements</u>

A. Systematically relevant branches

We support proposed changes of Article 42, where the more detailed provisions are proposed regarding the systematically relevant branches. We suggest including 2 % as the percentage in the Article 42 Para 2 sub-paragraphs 2.

B. Process of permission granting (Article 129 Para 2)

Article 129 Para 2 sub-paragraphs 5 include a new requirement that <u>"the consolidating supervisor shall, at the request of the applicant, consult the Committee of European Banking Supervisors."</u> We consider this provision as not systematic and consistent with the process of reaching the joint decision on model approval application. **We propose deleting words "at the request of the applicant" from the sub-paragraphs 5.**

C. Colleges of supervisors

Cooperation and information exchange between banking supervisors are very important issues for an effective supervision on cross-border banking groups in EU. NBS welcomes the Commission's intention to clarify issues regarding the cooperation between banking supervisors in more details as the explicit introduction of colleges of supervisors and the role of CEBS as a mediator.

NBS is actively involved in the work of CEBS regarding the colleges of supervisors, especially the work done by the CEBS pilot project of supervisory operational networking (SON). Good functioning of colleges is the way for effective supervision for cross-border banking groups by cooperation, exchange of information and coordination among the authorities.

Consolidating supervisor defined in the Article 4 Para 49 needs to get appropriate information about all relevant details regarding activities of subsidiaries and branches to get a whole picture about the risk profile of a cross-border group. Supervisor of subsidiary and supervisor of branch also have information need regarding the parent credit institution and general picture of group's activities. Multilateral cooperation in college is important for an effective supervision, but it is important to state that bilateral exchange of information between supervisors will still remain necessary tool for supervisory cooperation especially in large cross-border groups.

Planning and coordination of supervisory activities in going concern and also in crisis situation done by consolidating supervisor is a responsible way of executing supervision which does not impose supervisory burden on cross-border banking groups. However, requirements and expectations from colleges of supervisors should balance with responsibilities of each supervisor (parent company, subsidiary, branch) stipulated in the CDR.

We propose to include following basic principles of the functioning of the colleges in the directive:

- There should be one college of supervisors per group at the consolidated level in EU
- Membership of the college should be defined in the directive as containing:
    - consolidating supervisor
    - competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company
    - competent authorities of a host country where systemically relevant branches are established

- Effectiveness and efficiency of the colleges' operation should be ensured through:
    - the possibility of the consolidating supervisor to set up ad-hoc or standing groups depending on the activities and allocation of tasks
    - the possibility of supervisors to agree on two levels structure for colleges (general college and restricted college)
    - information to members of the college on the purpose and mandate of such ad-hoc and standing groups
    - reporting of ad-hoc and standing groups to the college
    - bilateral cooperation between supervisors in group

We consider the proposed changes of Article 129 Para 3 sub-paragraphs 3 and 4 to be not in line with the responsibilities of supervisors stipulated in the CDR, especially:

1. Article 129 Para 3 sub-paragraph 3 includes „The competent authorities participating in the colleges **shall agree on the entrustment of tasks and delegation of responsibilities** and cooperate closely, having regard to the obligations in Articles 40(3), 42 and 132."

Delegation of responsibilities is in our view not in line with the legal responsibility of each Member State and supervisory body in a member state. **We propose deleting words "delegation of responsibilities"** from the text of sub-paragraph 3.

Delegation of task should be on voluntary basis taking into account differences between different groups and supervisors. We propose replacing words **"shall agree" in the sub-paragraph 3 to "may agree."**

2. Article 129 Para 3 sub-paragraph 4 includes a list of issues a consolidating supervisor and the competent authority responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company in a certain Member State, shall reach an agreement on. The list includes Article 72(2), Article 74(2), Article 113(1) (f) and Article 136(2).

We consider colleges as a structure for cooperation and information exchange. Proposed list of articles exceeds this concept and reaches responsibilities of individual supervisors and we do not consider colleges as the appropriate forum for agreement on these issues.

- Articles 72(2) (Disclosure requirements for 'significant' subsidiaries),

  Disclosure requirements are stipulated in regulation of each Member State and there is limited room for reaching an agreement between supervisors.

- Article 74(2) (reporting for the calculation of minimum capital requirements),

  Reporting requirements are closely connected to national reporting regulation and information systems used by supervisors to monitor banks. Accepting several different formats and frequency of reporting would make monitoring of national banking sector in country impossible for supervisor and could lead to the declined ability of supervisor to react to systemic problems in that country.

- Article 113(1)(f) (treatment of intra-group exposures for large exposures purposes)

Treatment of intra-group exposures for large exposures purposes should result from certain conditions for assets transferability in each Member State and thus it is not an issue to be agreed within a college.

- Article 136(2) (own funds requirements in excess of the minimum level) to these subsidiaries.

Under the current status of responsibilities of supervisors, Pillar 2 is responsibility of each individual credit institution and supervisor in each Member State. Treatment of own funds requirements in excess of the minimum level should than remain on the basis of discussion and information exchange, but not as an issue for agreement within a college.

We propose deleting the sub-paragraph 4 of Article 129 Para 3 from the text.