

ON THE LEAD SUPERVISOR MODEL AND THE FUTURE OF FINANCIAL SUPERVISION IN THE EU

FOLLOW-UP RECOMMENDATIONS OF THE EFR - JUNE 2005



European Financial Services
Round Table



ON THE LEAD SUPERVISOR MODEL AND THE FUTURE OF FINANCIAL SUPERVISION IN THE EU

FOLLOW-UP RECOMMENDATIONS OF THE EFR

JUNE 2005

Foreword

For some time now, the EFR has argued that a more efficient and effective supervision of financial institutions is a key element to improve growth and integration of European financial markets. As we explained in two previous papers (issued in October 2003 and June 2004 respectively) the appointment of a fully empowered lead supervisor for each financial institution is considered to be a realistic way to achieve this goal.

Since then, this concept has been debated intensively and elements of the lead supervisor concept have found their way into forthcoming EU financial regulation. But a lot remains to be done to allow the lead supervisor concept to deliver its full potential in terms of consistency, cost and quality of supervision.

This third report builds on the reactions the EFR received on its previous proposals and broadens the debate, taking into account other aspects of the supervisory framework, like the function of the lender of last resort and deposit guarantee schemes. This report also provides considerations on alternative structures for financial supervision in the EU, in order to provide a broader frame of reference for discussion.

With this paper, the EFR aims at further contributing to the much-needed debate about the future architecture of the European financial system, which in turn is key for confidence, stability and economic growth.



Jean-Paul Votron

Sponsor of the EFR Steering Group
on Regulation and Supervision



Pehr G. Gyllenhammar

Chairman of the
European Financial Services Round Table



Content

Key messages	6
Introduction	11
Interplay in a crisis situation	15
Status Quo : Inefficient and ineffective	19
The lead supervisor concept.....	23
The lead supervisor concept and the Lamfalussy process	28
Responding to comments on the lead supervisor concept	30
Some general considerations on crisis management	33
Suggestions concerning the organisation of the lender	34
of last resort and guarantee schemes	
Emergency Liquidity Assistance within the Eurosystem.....	36
Longer-term options	39
Mission	44
Members of EFR	45

Key messages

- Reassured by the discussions it had with various officials on the June 2004 paper, the EFR reiterates its conviction that the lead supervisor concept would be a positive step towards a more efficient and effective prudential supervisory structure in the EU. By providing incentives for more integrated risk management and more efficient supervision it would contribute to reducing the risk of crisis. With a more transparent set-up for the respective institutions involved, it should also make crisis management more effective.
- It is encouraging that the debate on prudential supervisory structures within the EU (and elsewhere) is increasingly influenced by the concept of a “lead supervisor”. However, it should be clear that
 - what is discussed in the CRD is at best only a first step towards a lead supervisor regime and leaves open the risk of inconsistencies in implementation;
 - Solvency II for the insurance sector should be able to build on the CRD framework and go further towards a lead supervisor;
 - the revision of the Conglomerates Directive is an opportunity to transform the co-ordinating supervisor into a fully empowered lead supervisor for EU-wide operations;
 - generally, the framework for financial supervision in the EU remains highly fragmented and overregulated, and therefore inefficient and ineffective.

- In clarification of the concept developed in the June 2004 paper, the EFR proposes that the lead supervisor should be responsible for the prudential supervision not only of branches in other EU member states, but also of fully owned (fully controlled) subsidiaries in other EU member states. It is stressed that the interests of supervisors in member states, where systemically important branches and subsidiaries are located, should be taken adequately into account by their being represented in the “college of supervisors”. Thus, the lead supervisor concept explicitly recognises the value of intensive dialogue between supervisors and of the input host authorities provide.
- As regards the representation of authorities in the “college of supervisors”, in normal circumstances this would comprise at a minimum representatives of the supervisory authorities of those countries where the institution has sizeable operations. In a crisis situation, the college would give way to a core group of supervisors, comprised of representatives of those locations where the market impact of difficulties of the group in question is significant. Together with central banks, deposit insurance / insurance guarantee schemes and treasuries (and other parties which may be involved) in the countries concerned by the difficulties, this core group would manage the crisis. The lead supervisor would have a special role, particularly as regards the coordination of crisis management efforts.
- To the extent that there are no provisions in EU laws for resolving conflicts between supervisors, disagreements should be resolved by means of a mediation mechanism. This mechanism must be effective as well as efficient, whilst paying due attention to accountability of national supervisors. If a mediation (which is likely to be on a firm-specific issue) results in an outcome that has general applicability, supervisors should ensure that a level playing field is maintained.

- As regards the structure of lender-of-last-resort operations under a lead supervisor regime, the EFR recommends an arrangement that mirrors that of the lead supervisor concept, i.e the national central bank corresponding to the nationality of the lead supervisor would be the responsible lender of last resort and would ultimately take the decision on whether to activate the function or not. In doing so, it would consult all the other national central banks within the EU (and elsewhere) where the institution in question has operations. In order to avoid different policies being followed across the EU and, hence, to prevent competitive distortions, this arrangement would have to be complemented with the development of a general framework for lender-of-last-resort operations, which all EU central banks subscribe to.
- Organising deposit insurance / insurance guarantee under a lead supervisor regime is a difficult task, which defies simple solutions. At the same time, the more harmonised deposit insurance / insurance guarantee schemes are across member states, the less of a problem these schemes will be in the case of changes to the design of the supervisory structure and the easier it will be to assess the role of these schemes in a crisis situation. Against this background, the EFR would strongly recommend that the Commission presents a model to which the existing system should gradually converge over a specified time period, with such model aimed at levelling the playing field without imposing additional burdens on the financial industry.

- In order to avoid competitive distortions, the lead supervisor concept must be applied by all member states. To ensure this, a legislative basis – most probably an EU regulation (directly applicable in all member states) – will have to be created. This should not prevent supervisors, in the interim, from continuing current efforts to build “supervisory colleges” on a bilateral and multilateral basis by means of traditional MoUs provided that the period until a union-wide legal framework is enacted is brief and known. Likewise, it should not prevent member states to make extensive use of existing legal provisions that allow for a delegation of supervisory powers (as allowed for, e.g., in the Second Banking Directive).
- The Lamfalussy Level 3 committees have already contributed towards the aim of implementing EU financial legislation in a more consistent way across the EU. However, it should be clear that a number of items should be high on their agenda: full convergence, making choices about best practices; and removing hurdles for market integration to the extent that this is within their mandate. The more successful the Level 3 committees are in doing this, the better a lead supervisor regime would work.

- In order to be considered optimal and conducive towards reaching its goals, any supervisory structure must meet – and must be assessed against – objective criteria. In our view, these would be the following:
 - It must create financial stability, while at the same time set a framework for a dynamic and competitive financial sector;
 - The supervisory structure must be cost efficient;
 - It must be competitively neutral, i.e. ensure a level-playing field;
 - It must be transparent, thereby increasing the general public's and industry's confidence in the stability of the financial system;
 - It must provide for an effective and transparent framework for crisis management;
 - It must foster market integration and efficiency and be responsive to the evolution of market structures;
 - It must provide for clear structures of political accountability.

- As stated at the outset, the EFR is convinced that the lead supervisor concept would be a positive step towards a more effective and efficient structure for financial supervision in the EU, which would be conducive to fostering cross-border integration of EU financial markets. However, financial markets and the structure of financial institutions will continue to evolve. Consequently, a continuous monitoring must be established to ascertain whether the structure of financial supervision meets the above-mentioned criteria or whether other, more pan-European concepts will ultimately be warranted. A report on this should be published annually by an expert group based on consultations with all stakeholders.

Introduction

1. Optimising the environment for financial services providers in Europe is not only in the interest of the financial industry, but is of benefit to the EU's economy as a whole. Stable and efficient financial systems are a pre-condition for underpinning investment, for channelling funds into the most productive uses and, thus, for a smooth growth path. Empirical studies confirm that there is a positive correlation between the level of financial market development and economic growth. In fact, a study commissioned by the EU Commission estimated that the effect of completing financial market integration in the EU could be as high as 1.1% of GDP¹.
2. Financial market integration has a beneficial effect through various channels: First, deeper and more liquid financial markets reduce financing costs; second, broader financial markets allow for greater product choice; third, in integrated financial markets, financial institutions can exploit economies of scale. The latter is important as fixed costs seem to be rising in the financial industry: According to a joint study by Morgan Stanley and Mercer Oliver Wyman, the share of fixed costs in total costs rose from 10-15% in the early 1990s to around 25-30% today². Those costs are partly due to the fragmented and overregulated legal and supervisory framework in the EU.
3. Finally, the system of financial supervision itself has an important impact on the competitive position of financial institutions. As competition in the financial industry is also becoming increasingly globalised, lawmakers and regulators must ensure that the supervisory regime does not put Europe's financial services providers at a competitive disadvantage vis-à-vis their peers elsewhere.

¹ London Economics (in association with PwC and Oxford Economic Forecasting, 2002): Quantification of the Macro-Economic Impact of Integration of EU Financial Markets.

² Morgan Stanley / Mercer Oliver Wyman (2005): European Banking Consolidation: IT Synergies and Basel II Will Drive Cross-Border Restructuring, p.2.

4. Multi-jurisdiction firms (also referred to as cross-border institutions or pan-European institutions) play a particularly important part in integrating Europe's financial markets. Notwithstanding technological change in recent years, the provision of financial services, in all market segments, still predominantly requires personal contact between customers and services providers. Hence, integration is advanced particularly by those firms that have distribution points – in whichever form – in more than one member-state.
5. When talking about multi-jurisdictional firms one needs to realise that this encompasses a (given the total number of more than 8,800 credit institutions in the EU) comparatively small number of institutions, but that these institutions account for a disproportionate share of total assets³. In addition, these institutions almost exclusively account for cross-border business and are therefore prime channels for the distribution of capital and associated financial risk across borders in the EU. Furthermore, it needs to be realised that the companies that provide the infrastructure (broadly defined) to Europe's financial markets are primarily multi-jurisdictional in character and are therefore, again, of particular importance for the stability of financial markets in the EU (e.g. C&S providers such as Clearstream and Euroclear, exchanges such as Deutsche Börse and Euronext).
6. Against this background there can be no question that the supervisory regime in the EU must evolve with the evolution of financial markets. Only then can the benefits of an integrated financial industry be realised and the various financial risks contained, which represent the rationale for supervising financial institutions, viz.
 - Recognising the nature of the financial system as a key sector of the economy with strong interlinkages to all other segments of the economy,

³ For instance, in 2003 the top-50 EU banks accounted for more than 60% of total assets of all EU banks.

- Recognising the need to maintain depositors' confidence, so as to forestall banking runs which could destabilise the entire economy,
 - Recognising the crucial role of the financial system in channelling savings into the most productive use / investments,
 - Recognising the need for a stable and efficient payments system to foster economic exchange,
 - Recognising the role of the financial system as a transmission mechanism for monetary policy
 - Recognising the desirability of encouraging the improvement of risk management and diversification as key factors for financial stability.
7. In other words, it is in the common interest of the public sector, all private economic actors and financial institutions that financial supervision be structured in a way that guarantees systemic stability and market integrity at all times. Governments, in particular, must take a strong interest in maintaining the stability of, and public's confidence in, the financial system, as the economic, social and fiscal costs of a crisis are high.
8. In order to be considered optimal and conducive towards reaching its goals, any supervisory structure must meet – and must be assessed against – objective criteria. In our view, these would be the following:
- It must create financial stability, while at the same time setting a framework for a dynamic and competitive financial sector;
 - The supervisory structure must be cost efficient;
 - It must be competitively neutral, i.e. ensure a level-playing field;

- It must be transparent, thereby increasing the general public's and industry's confidence in the stability of the financial system;
- It must provide for an effective and transparent framework for crisis management;
- It must foster market integration and efficiency and be responsive to the evolution of market structures;
- It must provide for clear structures of political accountability.

Interplay in a crisis situation

9. Historically, systems of financial supervision, like financial markets, evolved in a national context. In all member states they included the same elements⁴, though the specific shape of institutions as well as their interplay varied. These elements include

- macro- and microprudential supervision of financial institutions,
- a lender-of-last-resort regime (whose working procedures are usually kept vague in the name of “constructive ambiguity”),
- a deposit insurance scheme / insurance guarantee scheme,
- an implicit or explicit understanding that, in the case of a major financial crises, fiscal resources will be made available to limit the damage to the overall economy.

Apart from prudential supervision, regimes are in place for conduct of business supervision⁵.

10. The above-mentioned elements work together in an intricate interplay. Microprudential supervision acts as an instrument of crisis prevention aiming at ensuring adequate risk management as well as a sufficient level of liquidity and solvency for all financial institutions. The functions of banking supervision, lender of last resort and deposit insurance / insurance guarantee are interrelated⁶. They are all part of a system that aims at maintaining the systemic stability

⁴ Some member states created deposit insurance system only after the Deposit Insurance Directive was passed on the European level in 1994, which required all member states to have these kinds of systems.

⁵ In this paper, as in previous papers, the EFR will limit itself to discussing issues of prudential supervision only.

⁶ For instance: The classic lender-of-last-resort principle refers to the provision of liquid funds to a solvent, but illiquid bank, which has good collateral. In principle, such a bank should be able to borrow from the market. If it cannot, then this is due to a breakdown of the market mechanism, e.g. because of a lack of transparency. If a public authority such as a central bank is to lend in such a situation nonetheless, it must have access to private information not available or conveyable to the market. Hence a close cooperation or identity of the lender of last resort and banking supervisor is sensible.

of the banking sector and at reducing the impact of any instability – should it occur nonetheless – to a minimum. Any change to the structure of financial supervision must therefore have consequences for the institutional set-up of both deposit insurance / insurance guarantee schemes and the lender-of-last-resort function. The lender-of-last-resort function focuses on liquidity, providing solvent, but illiquid institutions with funds. Given its nature, this function usually resides with central banks. In contrast, deposit insurance and insurance guarantees target solvency issues and are either self-regulatory regimes or publicly-funded / publicly-backed institutions.

11. In a crisis situation, the interlinkages of the pieces become evident: Lender of last resort and deposit insurance / insurance guarantee are inextricably linked with the issues of recapitalisation or winding-down of institutions that are insolvent or, at least, fail to meet minimum capital requirements. The lender of last resort almost never operates in textbook fashion – not the least because in an actual crisis situation (as opposed to textbooks) it is almost impossible to assess with any precision whether an institution is merely illiquid or is insolvent. It is also a matter of a case-by-case assessment as to how large the danger of contagion and systemic risk is, as repercussion obviously depend on the overall level of macroeconomic and financial market stability. Instead, a more or less formalised framework of crisis management has developed in most countries. Depending on national institutional arrangements and depending on the severity of the crisis, crisis management will involve the prudential supervisor, deposit insurance / insurance guarantee schemes, more or less voluntary collective action by solvent banks, central bank liquidity and ministries of finance. Within such a framework, central banks provide reassurance to markets by indicating that liquidity would be available (to the healthy bit of the banking sector) as an accompanying / flanking measure, i.e. in an effort to calm markets whilst a solution is found for the institution in trouble. In other words, the lender of last

resort, in reality, does not work (only) to the benefit of the individual institution that faces problems, but rather and more importantly to the benefit of other institutions and the financial system as a whole, which are thus shielded from the potential fall-out of the individual failure.

12. As their effectiveness depends on their smooth and effective interplay, these elements must interlink within a system that clearly defines the respective roles of the elements, defines their interplay and ensures their working together smoothly. The latter is all the more important in times of crisis, when time comes at a premium and must not be lost in unnecessary delays.
13. Historically, the elements have indeed interlinked within such a system, viz. the various member states. However, in the EU financial market, the elements have become delinked from the object they are designed to work on – i.e. financial markets: There is, increasingly, an integrated financial market, but there is no established framework in which the elements that safeguard the stability of that market could interlink smoothly.
14. This historically grown institutional set-up and the inconsistencies that it causes are structurally embedded in the system. However, they were tolerable in the past as the structure and business models of banks were different. Financial firms had a parent company with a clearly defined nationality, and foreign operations – whether in the form of subsidiaries or branches – were small both in relation to the business of the parent firm and overall banking volume in host countries. In addition, the internal structure of banks was organised in such a way that there were full banking operations – including all corporate centre functions – in all countries.

15. All of these characteristics have changed substantially over the past years, which is why the existing inconsistencies have created additional challenges and require a re-thinking of the supervisory structures. There are a growing number of truly multi-country organisations that operate as integrated cross-border institutions with single product and function platforms. Notably, the centralisation of corporate functions, such as risk and capital management does not necessarily entail a uniform legal form. Nor does centralisation of corporate and back-office functions necessarily require all of these to be performed at the same location. Depending on the locally available expertise and specialisation, back offices – such as post-trade securities handling, payments platforms – that provide services for the entire group may be located in different locations. Moreover, some of the centralisation of functions was actually triggered by regulatory developments: The centralisation of risk management functions, for instance, certainly was triggered by the preparation for Basel II.

In many cases, institutions' foreign operations are systemically important in other countries. This is causing particular concern with host supervisors if these operations are conducted in the legal form of branches, over which host supervisors have only a limited scope of influence. Finally, the option of converting companies into the legal form of a *Societas Europaea* (SE) will, over time, imply that the definition of a company's home country will be more diffuse; indeed, with the SE the legal seat of a company can be transferred.

Status Quo : Inefficient and ineffective

16. Admittedly, the institutional structure of banking supervision has evolved, too, but has done so largely irrespective of deliberations concerning prudential supervision with regard to crisis management and without aiming at aligning it with financial institutions' organisational structure. Rather, changes have been triggered by the establishment of the so-called Lamfalussy process for EU financial market regulation. Yet, it must be emphasised that effective cross-border prudential supervision is neither an explicit aim of the Lamfalussy process and the level 3 committees, nor do the Level 3 committees have any mandate or means to perform this task⁷. They are strictly intergovernmental in nature and thus have no supervisory powers of their own whatsoever. In other words, other than the beneficial side effect of more frequent contacts between supervisors, the Lamfalussy process did not change the structure of financial supervision in the EU.

17. The current institutional set-up is not only inefficient (causing unnecessary cost burdens to financial institutions), but has resulted in largely ineffective supervisory structures. It is doubtful whether there are sufficient incentives to pass on information and whether cooperation is actively sought. Given the absence of a supranational structure for prudential supervision, there is, unsurprisingly, also no supranational structure for crisis management.

18. For internationally active groups, supervisory responsibilities no longer coincide with, nor are they suited to the reality of those groups. The institutional set-up of financial supervision in Europe currently is a patchwork of different and largely incompatible regimes, where responsibilities, procedures and incentive structures are unclear. For instance, for the purpose of prudential supervision, there

⁷ Another downside of the current level 3 structure is its sectoral nature. While there are regular meetings of the chairmen of the three level 3 committees, these are mere information exchanges which do not do justice to the convergence of capital market segments which led to the emergence of integrated financial supervisors, such as Germany's BaFin and the UK's FSA.

is a split regime depending on whether operations outside of the home country are run as branches or subsidiaries: In the former case, the home supervisor (i.e. the one where the legal seat of the group's HQ is located) is responsible; in the latter case the responsible supervisor for the host location is in charge. For the purpose of lender-of-last-resort operations, the arrangement in place in the "domicile" of the entity that experiences a liquidity shortage is implemented, irrespective of whether the entity is a bank's HQ, a branch or a subsidiary.

19. Specifically, the status quo of lender of last resort is specified as follows:

This function has been established in different ways in EU member states ranging from very explicit to very general rules. Mostly, authorities have preferred to maintain considerable ambiguity as regards the lender-of-last-resort function lest moral hazard be caused. As regards the rules applicable for internationally active institutions in a European context, the following general principles seem to have been set: For both branches and subsidiaries, the host central bank is the lender of last resort. This, of course, was (and for member states not participating in EMU still is) a logical corollary of the existence of different national currencies. For the concept of lender of last resort to be credible, the respective central bank must be able to provide the currency that the illiquid bank is using, without any restriction – which is only the case if it can print the currency itself. This is, by the way, the reason why host regulators, to this day, have retained the right of liquidity control for bank branches in other member states despite the existence of the single passport. Hence, the present day arrangement – host country supervision of subsidiaries and host country liquidity control for branches and subsidiaries – is (if nothing else) at least logical as regards the lender-of-last-resort issue in those cases where a bank's head office on the one hand and the branch / subsidiary on the other hand reside in different currency areas.

It is equally obvious, however, that the logic no longer applies to banks and their subsidiaries / branches located in the Eurozone. In fact, Eurozone banks with branches and subsidiaries in other Eurozone member states have generally centralised their liquidity management in headquarters. Thus, the notion that such a bank has a liquidity problem in one of its subsidiaries, but not in its home market (or vice versa) is no longer tenable.

Within the Eurosystem, all participating national central banks decide, in principle, autonomously on whether or not to provide emergency liquidity assistance to an institution operating in its jurisdiction. However, given that the repercussions of providing liquidity in any one EMU member state extend beyond this member state, the Eurosystem has to be informed. In practice, it can probably be assumed that no national central bank that is a member of the Eurosystem would act in isolation.

20. For deposit insurance, the current set-up is as follows:

- In the EU, the home country principle applies for deposit insurance. Therefore, deposit insurance covers deposits held in the country of incorporation as well as deposits held in foreign branches. Subsidiaries of foreign banks must join the host nation's scheme, provided there is one (which is the case in all EU member states due to the EU Directive on Deposit Insurance)
- To provide for a level-playing field, foreign branches are allowed to join the host scheme, if the latter provides more favourable conditions than the home scheme ("topping up")⁸. The "topping up" rule extends only to deposit insurance as covered by the EU directive – it is therefore only of relevance in those countries, where coverage exceeds the minimum prescribed in the

⁸ Note, that the "topping up" rule extends only to deposit insurance as covered by the EU directive. As the schemes in most EU countries do not exceed the EU minimum, topping up is of limited practical relevance.

Directive (EUR 20.000) or where the scope of coverage differs⁹. In other words, even under the present regime, a foreign branch can, in principle, obtain insurance coverage in another country even though the entity running the scheme has no **ultimate** authority¹⁰ to regulate the risk-taking behaviour of the foreign branches.

21. Supervisory authorities often argue that there is a simple way for firms to solve the problem of inconsistencies: To convert all foreign operations in the EU into branches. By doing so, all of these would come under the jurisdiction of the home country supervisor, obliterating all duplications. However, the solution is not at all as optimal as it appears to be. First, some inconsistencies would remain: Lender-of-last-resort operations would still reside with the respective host authorities and the inconsistencies in the deposit insurance set up would likewise remain. Second, supervisory arrangements should not dictate the organisational set-up of a firm, which should be the prerogative of a bank's management. There are good commercial reasons for not converting subsidiaries into branches (minority shareholders, brand value, the need to placate local politicians, management and customers, tax issues, etc.). Third, experience shows that host supervisors will take a keen interest in a foreign bank's branch, even if it has little actual legal right to do so. This is particularly so, when the branch is systemically important.

⁹ Branches of foreign banks may join voluntary schemes that offer higher coverage, such as the one in Germany, provided that they meet the requirements for these schemes.

¹⁰It should be noted, though, that the deposit insurance / insurance guarantee schemes may (and do) have their own supervisory arrangements, which work independently of official supervision.

The lead supervisor concept

22. In June 2004, the EFR presented a proposal for addressing these problems: The “lead supervisor” concept. The lead supervisor, which is the supervisor of the parent company, would be fully empowered to conduct the entire prudential supervision over all operations of a financial institution within the EU. The lead supervisor would have the following rights and obligations with respect to a financial institution’s EU operations :
- It would be the single point of contact for all issues of prudential supervision;
 - The lead supervisor would coordinate all reporting duties and, to the extent that there still are national discretions, decide on the reporting format;
 - The lead supervisor would be responsible for model validation and authorisation to the extent that these models are used group-wide;
 - The lead supervisor would decide about pillar II issues at group level;
 - It would approve capital allocation at group level and liquidity rules at group and branch level;
 - It would decide upon and coordinates all on-site inspections;
 - It would approve the cross-border set-up of central functions;
 - It would coordinate licensing procedures.
23. In the broader context, the EU lead supervisor would also act as the EU coordinator vis-à-vis the non-EU home country supervisor. The EU lead supervisor would cooperate closely with the financial institution’s global lead supervisor, respectively its home supervisor, to support a consistent approach to prudential supervision at the EU and global levels.

24. It is encouraging that the debate on supervisory structures within the EU (and elsewhere) is increasingly influenced by the concept of a lead supervisor. Thus, the current draft of the Capital Requirements Directive (CRD) includes a provision on establishing a consolidated supervisor (art. 129) which will have a leading, potentially decisive role for model authorisation at group level. However, it should be clear that what is discussed in the CRD is at best only a half way solution which can lead to inconsistencies in implementation. Similarly, in the discussion on the Solvency II Directive for the insurance industry, there is a broad recognition of the necessity of consolidated supervision for cross-border operations, but, in the EFR's view this should build on the CRD framework and go further towards a lead supervisor model¹¹.

25. Importantly, as the EFR pointed out in its earlier paper, the lead supervisor would not only have rights, but would have obligations, as well. In particular, the establishment of the lead supervisor would be complemented by the setting-up of a so-called "college of supervisors", which, in normal circumstances, would include at a minimum representatives of the supervisory authorities of those countries where the institution has substantial operations; however, to the extent an EU supervisor does not want to participate in the college of supervisors, such supervisor would not be exonerated from implementing the decisions of the EU lead supervisor. The college of supervisors will serve as a conduit for close information-sharing and interaction amongst supervisors. It is absolutely clear that the lead supervisor concept cannot operate without this interaction; hence, this should be considered an essential part of the concept.

¹¹CEIOPS uses the term „lead supervisor“, too. However, unlike in the EFR's concept this institution would have hardly any powers.

26. The authorities represented in the college would assist – in a spirit of mutual trust – the lead supervisor by giving input on local market conditions and by executing inspections in local operations. Via the college, local supervisors would get all relevant information from the lead supervisor.

27. In the first paper we proposed that the authority of the lead supervisor in prudential supervision would extend not only to branches in other EU member states, but also to fully owned (fully controlled) subsidiaries in other EU member states. Correspondingly, the college would include representatives from countries that host subsidiaries as well as those that host branches – thus taking into account concerns on systemically important branches and subsidiaries in other member states. While there are arguments against including authorities from countries, where a financial group only has branches, on balance the EFR feels that it is more useful, if these authorities are represented, too. The lead supervisor concept explicitly recognises the value of intensive dialogue between supervisors and of the input host authorities provide.

28. To the extent that there are no provisions in EU laws for resolving conflicts between supervisors, disagreements should be resolved by means of a mediation mechanism. This mechanism must be effective as well as efficient. If a mediation (which is likely to be on a firm-specific issue) results in an outcome that has general applicability, supervisors should ensure that a level playing field is maintained. Such a mediation mechanism would only be available under normal market circumstances, though.

29. In a crisis situation, the college of supervisor would need to change in character. Whatever structure is chosen for the college in times of crisis, three elements seem evident: First, the lead supervisor would continue to have a special role amongst supervisors, in particular as regards the coordination of the crisis

management efforts. Second, a core of the college would become a management team for the group of supervisory authorities; this core would presumably comprise (a) those locations that would have the largest impact on the group's solvency and liquidity situation and (b) those locations where the market impact of difficulties of the group in question would be greatest. Third, this core group would, of course, have to liaise closely with central banks, deposit insurance / insurance guarantee schemes and treasuries (and other parties which might be involved) in the countries concerned.

30. It needs to be emphasized that in a crisis situation the college of supervisors would only be one element of the institutional structure for crisis management. Clearly, institutions like finance ministries, deposit insurance / insurance guarantee funds and central banks will also have a crucial role. As described above, the role of the lead supervisor in this set up and situation would essentially consist of organising the "supervisory element" (i.e. the role of financial supervisors) in the overall structure for crisis management. It is difficult to define the structure of this "supervisory element" more concretely at this stage, as its design will depend on the overall arrangement for crisis management and the relative role of financial supervisors therein.
31. In order to avoid competitive distortions, the lead supervisor concept must be applied by all member states. To ensure this, a legislative basis – most probably an EU regulation (directly applicable in all member states) – will have to be created on the basis of a consultation process. This should not prevent supervisors, in the interim, from continuing current efforts to build "supervisory colleges" on a bilateral and multilateral basis by means of traditional MoUs provided that the period until an EU-wide legal framework is enacted is brief and



known. Likewise, it should not prevent member states from making extensive use of existing legal provisions for delegation of supervisory powers (as allowed for, e.g., in the Second Banking Directive)¹².

¹²In fact, the opportunity to delegate supervisory powers provided in the Second Banking Directive has not been used by member States, so far. The EFR encourages them to do so.

The lead supervisor concept and the Lamfalussy process

32. The EFR fully supported the establishment of the Lamfalussy process and its extension to banking and insurance regulation. Overall, the process is working well and has already brought tangible benefits in terms of faster and more flexible legislation, more intensive consultation processes, and better coordination of supervisory action. Nonetheless, it is certainly too early to pass definitive judgement on the process, not the least because the possibility of amending existing legislation by level 2 measures has, for obvious reasons, not yet been used and because level 4 is largely untested. For equally obvious reasons, little experience has been gained with the Lamfalussy process in the areas of banking and insurance.
33. The four-level Lamfalussy process, of course, encompasses more than financial supervision. Indeed, it is primarily concerned with financial rule-making, rather than with supervision *strictu sensu*. Against this background, it is important to point out that the EFR proposal for a lead supervisor regime would not have a direct impact on the process of financial lawmaking in the EU. In other words, levels 1 and 2 of the Lamfalussy process would not be affected and would remain as they are.
34. The EFR wishes to point out that the actual working and the set up of the institutional structure of prudential supervision in the EU can already be improved substantially by means of exploiting the potential that the Level 3 committees offer. We recall the mandate of the Level 3 committees which, *inter alia*, is to foster a consistent and coherent implementation and application of EU financial regulation in all member states. Some of the practical benefits, which would result from the introduction of a lead supervisor regime could already be realised if the Level 3 committees made full and extensive use of their mandate. This would, *inter alia*, include:

- initiatives to harmonise reporting requirements by defining a common, streamlined reporting format;
- initiatives to cut the number of national discretions as exercised by, or available to, member states (the work of CEBS on reducing the number of national discretions in the CRD is a case in point);
- enhancing and standardising the use of MoUs;
- encouraging the delegation of supervisory powers, possibly developing best practices for this.

Responding to comments on the lead supervisor concept

35. The EFR's June 2004 paper met with great interest in both the public and the private sector. The EFR received a great number of constructive comments on its proposal from public-sector representatives. These comments covered a number of different issues, which, by and large, fall into the following broad categories:

- The need to ensure that knowledge on local market conditions is not lost.
- The need to take the global dimension into account.
- The need to differentiate between institutions that are locally active only and multi-jurisdiction institutions.
- The limits to delegating supervisory authority amongst EU financial supervisors.

In the eyes of the EFR, none of these pose insurmountable problems.

36. As regards the need for ensuring that local conditions are taken sufficiently into account, the following needs to be kept in mind:

- The establishment of a college of supervisors would ensure a constant and extensive flow of information between all supervisors involved.
- In addition, the lead supervisor obviously would have a strong incentive to take into account information that might flow from the host authorities.
- The extent of national discretions is being reduced gradually in any case. For instance, there is a strong effort in place to reduce the number of national discretions in the CRD.
- On-sight inspections can and probably would be executed by local supervisors who know the local situation and bring information and vision to the college. Actually, we would anticipate the college developing into an important instrument for exchange of practices and information beyond the Level 3

committees.

- Finally, the possibility of an appeal / mediation mechanism will reduce the likelihood that lead regulators will exercise their power without due regard for the interests of the other authorities represented in the college.

37. Some commentators have argued that a lead supervisor system will be insufficient for large, internationally active financial groups as they operate on a global level, implying that the added value of having a more streamlined system in Europe alone is low. However, recognising that the lead supervisor regime might not solve all problems for globally active EU financial institutions, is not to say that it would not constitute a great step forward in making at least the supervisory environment with the EU more efficient. In addition, the EFR feels strongly that the intensity and political will for integration in Europe is and should be a strong argument that justifies such an approach within the EU. Furthermore, clear, workable, innovative, and forward-looking structures in the EU will strengthen Europe's position in international negotiations – not only in the ongoing negotiations in the international arena, but also in the discussions that will inevitably arise in the future on the evolution of the global system of financial supervision. To some extent, the negotiations underway in the Basel Committee's AIG might be regarded as a precursor to this.

38. Responding to the argument that the lead supervisor system is unsuited for small institutions that are active only on the local level, the EFR wishes to note that the lead supervisor concept does not affect these institutions in any case. At the same time, however, cross-border players, as noted above, are important catalysts for financial market integration and should not be hindered in their operations by an inefficient supervisory regime.

39. As regards the need for taking due notice of the accountability of national authorities, which might limit or even prevent the use of delegation, the EFR is of course keenly aware of this issue – and, indeed, already highlighted this concern in its earlier paper. We fully recognise the political sensitivity of these issues and the prerogative of national parliaments to decide on the responsibilities of national authorities. Yet, we would note a couple of issues that authorities should keep in mind, when deliberating on this issue:

- Current institutional arrangements neither serve the interest of the wider public nor that of the industry. The status quo is not an option. It will lead to difficulties and irresolvable disputes in case of a crisis, which will increase the costs of dealing with a crisis situation for society.
- When financial groups are integrated on a European, if not on a global level, insisting on supervising subsidiaries on a stand-alone basis appears to be an unsuitable concept even from the point of view of the responsible authority in the country where the subsidiary is located.
- Current EU laws already provide the option of delegating responsibilities to other regulators; and even though this option is not used, the lead supervisor would thus only be different in degree, not in principle.

40. Whilst solutions to a crisis situation are inherently difficult, the EFR believes that the lead supervisor concept would contribute to reducing the risk of crisis by providing incentives for a more integrated risk management and more efficient supervision. In addition, with a more transparent set up for the respective institutions involved, it should also make crisis management more effective.

Some general considerations on crisis management

It is well understood that the resolution of financial crises is more of an art than a mechanistic application of pre-determined rules. This holds true both in case of difficulties of an individual institution and, a fortiori, in case of a system-wide crisis. In addition, it should be noted that crisis resolution does not only rest on (semi-)official institutional frameworks, such as deposit insurance / insurance guarantee and lender of last resort. Private sector involvement has always been another important element for three reasons. First, it enlarges the pool of available resources. Second, it is often indispensable for the orderly wind-down of a failed institution in order to provide for the continuity of outstanding contracts in financial markets, so that chaos is prevented (LTCM is a case in hand). Third, it is assumed that private sector involvement has a positive impact in terms of market discipline and limits the costs of crisis resolution to the general taxpayer. While, therefore, a good case can be made for private sector involvement, its limits must also be acknowledged. For instance, private sector engagement can never fully substitute for the lender-of-last-resort function as private actors cannot create ultimate liquidity on their own. Also, there are obvious and well-acknowledged limits to private sector involvement, viz when doing so threatens to endanger the viability of the hitherto healthy part of a financial system.

Distinction must also be made between financial crises concerning only a small or a few smaller institutions and those of systemic dimensions affecting either one systemically important institution or entire financial systems. In the former, the orchestration of a private sector solution is usually sufficient and, hence, the instrument of choice. The take-over of an insolvent institution by one or several healthy ones is often complemented with the financial involvement of deposit insurance / insurance guarantee funds in order to shield the acquirer(s) from assuming undue amounts of risk and losses. It must be noted though that these kinds of private sector solutions are possible only under restrictive conditions: First, the acquiring institution(s) must be sufficiently financially stable, so that the burden can be absorbed. Second, the acquiring institution(s) must feel a sufficient degree of self-interest in maintaining the stability of the market in question. As a consequence of the latter, private sector solutions are, at present, only realistic in a national context or in markets marked by a high degree of concentration (as was the case with LTCM). Whether EU banking markets are already interlinked to a degree that would provide sufficient incentive for a private sector solution in the case of the crisis of a systemically relevant institution is an open question.

It is an equally open question whether an exclusively private sector solution would in fact provide a sufficient amount of funds for the rescue or at least the orderly winding down of a systemically relevant institution, let alone in case of a large-scale banking crisis. Experience with banking crises in industrial countries over the last two decades suggest that the answer to this question is "no". Consequently, in these cases some combination of official money (fiscal funds and central bank money), private funds and deposit insurance / insurance guarantee funds will be necessary.

Suggestions concerning the organisation of the lender of last resort and guarantee schemes

41. In an environment of a lead supervisor, with respect to the issue of lender of last resort and deposit insurance / insurance guarantee, the key issue is the incongruence of those taking a decision on the liquidity and / or solvency of a financial institution on the one hand and those responsible for the funds on the other hand. The action of the lead supervisor, in other words, causes an externality for those institutions that run deposit insurance / insurance guarantee or lender-of-last-resort facilities in another country where subsidiaries are located. In case of a crisis situation, these externalities would, at a minimum, cause delays due to the necessity of co-ordination or, of more concern, may even cause inaction by the authorities due to disagreement over the course of action – which would only serve to intensify the crisis.
42. As to lender-of-last-resort operations, within a lead supervisor framework, assuming the continuation of the status quo arrangement, the host central bank would continue to have the lender-of-last-resort function for foreign branches and subsidiaries – but host supervisors would no longer have first-hand insight into the financial situation of the institution, or at least not on a continuous basis¹³. Instead, the host central bank would, in extremis, have to base its decision on whether to advance funds or not on the information provided by the lead supervisor. (Alternatively, one might conjecture that the host supervisor is given special supervision powers to assess the financial status of the institution, if and when the activation of the lender-of-last-resort function is deemed necessary. However, this would obviously cause a delay in decision-making, in a situation when time is short in any case.)

¹³This problem might actually appear greater in theory than, at least currently, it is in practice: Local (host) supervisors do collect information on the institutions operating within their jurisdiction, even if they have no legal basis for doing so. In particular, conduct of business supervision is often (mis)used as an entry gate for checks on matters of prudential supervision.

43. Within current institutional arrangements, it would seem that an arrangement that mirrors that of the lead supervisor concept, would be a sensible institutional response: The national central bank corresponding to the nationality of the lead supervisor would, thus, be the responsible lender of last resort and would ultimately take the decision on whether to activate the function or not. In doing so, it would consult a forum of, at a minimum, all the other national central banks within the EU where the institution in question has significant operations.
44. This institutional set up would also seem sensible given the centralisation of liquidity management in financial groups. Due to this centralisation, liquidity shortage will always be a group-wide phenomenon.
45. In order to avoid different policies being followed across the EU and, hence, to prevent competitive distortions, this arrangement would have to be complemented with the development of a general framework and an adherence to common principles for lender-of-last-resort operations, which all EU central banks subscribe to. The unpublished “memorandum of understanding on crisis management” signed by banking supervisory authorities and central banks of the EU in March 2003¹⁴, which, as we understand it, is merely geared towards practical issues at the moment, could be a basis to build upon. In addition, we note in this context that Eurosystem members are already obliged to coordinate lender-of-last-resort operations as these would have an impact on the money supply in the Eurozone.

¹⁴Memorandum of Understanding on high-level principles of co-operation between the banking supervisors and central banks of the European Union in crisis management situations.

Emergency Liquidity Assistance within the Eurosystem

“Co-ordination mechanisms are primarily called for within the Eurosystem. This is the case for emergency liquidity assistance (ELA), which embraces the support given by central banks in exceptional circumstances and on a case-by-case basis to temporarily illiquid institutions and markets. At the outset, it is necessary to stress that the importance of ELA should not be overemphasised. Central bank support should not be seen as a primary means for ensuring financial stability, since it bears the risk of moral hazard. Preventive measures aimed at fostering the adoption of sound risk management practices on the part of financial institutions, and the effectiveness of prudential regulation and supervision in achieving this goal, are the first line of defence against excessive risk-taking behaviour and financial distress. Furthermore, the provision of ELA has been a very rare event in industrial countries over the past few decades, while other elements of the safety net have gained importance in the management of crises. However, if and when appropriate, the necessary mechanisms to tackle a financial crisis are in place. The main guiding principle is that the competent NCB takes the decision concerning the provision of ELA to an institution operating in its jurisdiction. This would take place under the responsibility and at the cost of the NCB in question. Mechanisms ensuring an adequate flow of information are in place in order that any potential liquidity impact can be managed in a manner consistent with the maintenance of the appropriate single monetary policy stance. The agreement on ELA is internal to the Eurosystem and therefore does not affect the existing arrangements between central banks and supervisors at the national level or bilateral and multilateral co-operation among supervisors and between the latter and the Eurosystem. However, their smooth functioning assumes an ability to implement, swiftly and efficiently, co-ordination mechanisms aimed at dealing with the cross-border implications of financial crises and at preventing contagion.”

Source: ECB (2000). Annual Report 1999, p.98.

46. Generally and irrespective of the discussion of the lead supervisor concept, we see a need for EU central banks to state publicly that a workable agreement on liquidity provision in (individual and systemic) crisis situations exists between Eurozone members as well as with non-EMU members. While we accept the virtues of constructive ambiguity, there must be certainty and confidence about the existence of a workable framework for multi-jurisdictional crisis management – which are currently absent or, at least, far from transparent.

47. Organising deposit insurance / insurance guarantee under a lead supervision regime obviously is a difficult task, which defies simple solutions. All of the possible options bring up serious structural or political problems, the root cause of which is the immense heterogeneity of existing schemes in the EU. However, it is important to realise that already the current institutional set up is not without difficulties. Therefore, this cannot be an argument against moving towards a lead supervisor regime.
48. It should be obvious that the more harmonised deposit insurance / insurance guarantee schemes are across member states, the less of a problem these schemes will be in the case of changes to the design of the supervisory structure and the easier it will be to assess the role of these schemes in a crisis situation. Against this background, the EFR would strongly recommend that the Commission presents a model to which the existing system should gradually converge over a specified time period, with such model aimed at levelling the playing field without imposing additional burdens on the financial industry. In addition, it needs to be recognized that convergence of deposit insurance / insurance guarantee schemes will probably trigger a need to work on issues that are linked to them, such as national bankruptcy and company laws.
49. Again, it needs pointing out that the current set up of deposit insurance in Europe entails problems already, irrespective of the lead supervisor concept. In particular, if a bank decided to change the legal status of its operations from the form of subsidiaries into that of branches, the potential burden of deposit protection would be shifted from the host country to the home country. In other words, a mere change in the organisational set up of a company which, *ceteris paribus*, does not change the risk inherent in a bank's operations in economic terms, has consequence for the inter-national distribution of risk to third parties, viz. those funding deposit insurance schemes. Thus, a need for revising the existing framework seems in order in any case.

50. The fiscal dimension: As mentioned above, it should be clear that in case of systemic problems, there are limits to the capacities of the private sector and deposit insurance / insurance guarantee schemes to restore stability to the financial system. Consequently, as past experience (e.g. in Sweden, France, Italy, Spain, the US) shows the use of fiscal resources will have to be considered by governments in these cases. It should be equally clear that in an integrated European financial market, close coordination of governments' actions is warranted – either to control the side-effects of action by individual governments or, as will be the case should a pan-European institution get into solvency problems, because the problem has a transnational dimension anyway.

Longer-term options

51. As stated at the outset, the EFR is convinced that the lead supervisor concept would be a positive step towards a more effective and efficient structure for financial supervision in the EU, which would be conducive to fostering cross-border integration of EU financial markets. In suggesting the lead supervisor regime, the EFR was motivated by the need to find a near-term arrangement for financial supervision in Europe, which simultaneously (a) would bring about a substantial improvement for the effectiveness and efficiency of financial supervision in the EU, (b) seemed politically acceptable and (c) could be realised with comparatively little change in the legislative framework.
52. However, financial markets and the structure of financial institutions will continue to evolve. Hence, the lead supervisor concept may not necessarily be the optimal structure for financial supervision in the EU in the medium-term to long-term given the continuing evolvement of financial markets, the internal structure of financial institutions and the political environment in the EU. The EFR feels that an open discussion on the relative merits of alternative concepts is warranted. Consequently, a continuous monitoring must be established to ascertain whether the structure of financial supervision continues to meet the above-mentioned objective criteria (cf. para 8) and – if satisfactory improvements cannot be achieved within existing structures - whether other, more pan-European concepts (some of which are discussed below) will ultimately be warranted. A report on this should be published annually by an expert group based on consultations with all stakeholders.
53. Besides the lead supervisor concept, a number of alternative concepts are being discussed at present. These include proposals, such as,
- essentially conserving the status quo;
 - giving greater powers to the Level 3 committees, e.g. by giving them power to mediate disputes between Level 3-committee members (as was suggested,

e.g. in CESR's Himalaya report);

- establishing a separate, mandatory regime for multi-jurisdictional institutions only;
- establishing a European System of Financial Supervision (ESFS) with an ESCB-type structure, with a new EU-level institution (a European FSA, or EFSA) which would supervise the systemically relevant financial institutions that operate on a pan-European basis and would be the final authority on interpretation and implementation of EU financial market rules in cases of conflicts between national regulators. Small and domestically-oriented institutions would continue to be supervised by national authorities, acting on the basis of common rules and subject to the final say of EFSA.

54. Conserving the status quo and complementing it with mechanisms for improved cooperation and coordination would appear to have an advantage in that it is politically feasible and can be implemented without major (legal and operational) pre-requisites. Nonetheless, it is the EFR's firm conviction that conserving the status quo is a practical stop-gap measure, but not a long-term option. As shown above, the present arrangements create a supervisory structure that is neither efficient nor effective in terms of ongoing supervision and crisis management. Likewise, as has frequently been evidenced, present supervisory arrangements are a severe obstacle to further market integration. The present arrangements also endanger the principle of competitive neutrality of supervision – and stand in the way of a more effective EU voice in international financial diplomacy.

55. Giving greater powers to the level 3 committees could, in principle, increase the effectiveness of supervision and lead to a more consistent and hence competitively neutral supervision in the EU. They could also be empowered to appoint a

lead supervisor for cross-border groups in the EU, by means of which the lead supervisor would be based on a European mandate¹⁵. However, increasing the powers of the Level 3 committees will inevitably lead to conflicts with their legal status¹⁶ : presently, the Level 3 committees are purely intergovernmental and have no legal personality. They are therefore legally not allowed to take binding decisions which have legal power in and vis-à-vis member states. Put differently: expanding the use of “soft law” techniques at level 3 risks a situation in which political accountability is unclear and market participants are faced with legal uncertainty.

56. Establishing a separate, mandatory regime for multi-jurisdictional institutions only would offer the opportunity to establish an efficient and effective regime for these institutions, while keeping existing structures for the vast majority of EU financial institutions (i.e. those that are only active in one member state) as they are. Erecting such a regime would require EU-level legislation (possibly a Treaty change) and willingness of member states to cede sovereign rights to an EU-level institution. As is the case in the lead supervisor concept, the repercussions for crisis management would have to be clarified.

One obvious disadvantage of this kind of bifurcated-regime model would be the danger that it might violate the principle of competitive neutrality by introducing different supervisory regimes for multi-jurisdictional and single-jurisdictional financial institutions – which, after all, compete directly with each other in local markets. It may also lead to disputes about competences between the national supervisory authorities and the EU-level one, which might be par-

¹⁵Cf. Sander Oosterloo and Dirk Schoemaker (2004): A lead supervisor model for Europe; in: *The Financial Regulator*, Vol.9, No. 3, December.

¹⁶This was also noted by the IIMG in their latest report, cf. IIMG (2004): Third report monitoring the Lamfalussy Process; p.29.

ticularly damaging in a crisis situation, where smooth cooperation would be needed, because problems at a large EU financial institution would inevitably have repercussions on smaller players.

57. An ESCB-type European System of Financial Supervision (ESFS) would overcome this disadvantage by giving, in cases of conflicts between regulators, the final authority on interpretation and implementation of EU financial market rules to the central institution, EFSA. Unlike in other concepts, it would be legally impossible for national authorities to impose additional requests / burden on banks. This is key: Current experience shows that local authorities use any possibility to retain influence even in those cases where EU laws already enshrine the principle of home supervision. The model would also offer the advantage of being organisationally efficient, by leaving national supervisory structures as they are and limiting the direct influence of EFSA to multi-jurisdictional firms¹⁷.

In a crisis situation, there would be no uncertainty in both official and private sector on which authority takes the lead; there would also be no danger that information on financial health of banks is withheld by national supervisors. The problem of how to deal satisfactorily with “systemically important branches” would be resolved, as host countries would have share responsibility via the EFSA.

Building an ESFS-type model, too, would require EU-level legislation, possibly a Treaty change – making it a medium-term option only. In addition, satisfying arrangements for the political accountability of an EFSA would need to be found. A possible downside of the ESFS-model would be that it would reduce the scope for regulatory competition – though it could be argued that an

¹⁷Note that EFSA is **not** a „single“ or „centralised“ EU supervisor that would oversee all EU financial institutions directly.

ESFS would, of course, find itself in regulatory competition with other regulators around the globe. Such a concept also implies a greater degree of harmonised law in areas relating to enforcement. Additional specific issues also arise in non-prudential areas of regulation such as conduct of business and market supervision. A further risk is that the ESFS model could lead to overregulation if it merely added all existing national practices instead of establishing a new, streamlined and efficient system. Difficulties with aligning it to the lender of last resort and deposit protection / insurance guarantee schemes would also remain, if these were kept in their current form.

58. Looking at the various options, there obviously is a general trade-off: Essentially, while the more supranational alternatives would be more difficult to realise given the political and legal prerequisites, they would have the advantage of providing a clear-cut, consistent framework, where accountability and responsibilities were clear and where costs would be lowest for all parties concerned. The lead supervisor regime would be easier to realise, but may, in the end, only provide an interim solution for a rapidly evolving financial services industry.

Mission

The Members of the **European Financial Services Round Table (EFR)** strongly support the completion of the Single Market in the area of financial services. Creating true competition on a level playing field - with more harmonised regulations and a single capital market - will bring substantial benefits to consumers across the 25 Member States of the European Union. These benefits will help to drive down prices and deliver a wider and better choice of financial products to consumers. The EFR provides a strong industry voice and participates actively in the debate aiming at a further integration of the financial services markets.

The EFR welcomes the effort undertaken both at the European and national level to accomplish the goals set by the Lisbon Agenda, including the Financial Services Action Plan.

The **policy priorities** of the EFR are:

- to promote effective and efficient financial **regulation** and **supervision**
- to encourage harmonisation of **consumer protection** rules in the area of financial services at European level
- to promote a single market for **pensions**
- to support a single **capital market**

The EFR has **published**, inter alia, a report on the major obstacles to a fully integrated financial market *The Benefits of a Working European Retail Market*, 2002; a report on the integration of pensions in Europe *One Europe, One Pension – Affording the Future*, 2002; recommendations on the *Harmonisation of Regulation and Supervision of the European Financial Sector*, October 2003; a statement on the European securities market infrastructure *Securities clearing and settlement in Europe*, 2003; in March 2004 a report on consumer protection *Consumer Protection and Consumer Choice*; recommendations on regulation and supervision *Towards a lead supervisor for cross border financial institutions in the European Union*, June 2004; recommendations on pensions *Creating a Common Structure for Pan-European Pensions*, September 2004.



MEMBERS of EFR

Pehr G Gyllenhammar

Chairman, EFR and Chairman,
Aviva

Sergio Balbinot

Co-Chief Executive Officer,
Generali

Matt Barrett

Chairman,
Barclays

Dr. Nikolaus von Bomhard

Chairman of the Board of Management,
Munich Re

Dr. Rolf-E. Breuer

Chairman of the Supervisory Board,
Deutsche Bank AG

Henri de Castries

Président du Directoire,
AXA

Dr. Hans Dalborg

Chairman of the Board,
Nordea AB

Michael Diekmann

Chairman of the Board of Management,
Allianz AG

Francisco González Rodríguez

President,
BBVA

Rijkman Groenink

Chairman of the Managing Board,
ABN-AMRO Bank

Walter B. Kielholz

Chairman,
Crédit Suisse Group

Jean Laurent

Directeur Général,
Crédit Agricole

Sir George Mathewson

Chairman,
Royal Bank of Scotland

Marcel Ospel

Chairman,
UBS AG

Michel Pébereau

Président du Conseil d'Administration,
BNP Paribas

Alessandro Profumo

Chief Executive,
UniCredito Italiano SpA

James J. Schiro

Chief Executive Officer,
Zurich Financial Services

Don Shepard

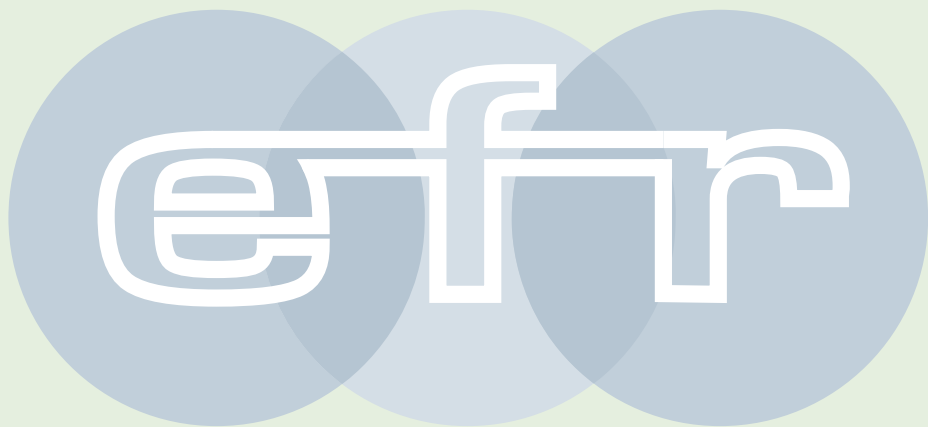
Chairman of the Executive Board,
AEGON NV

Michel Tilmant

Chairman of the Executive Board,
ING Group

Jean-Paul Votron

Chief Executive Officer,
Fortis



European Financial Services Round Table

**EFR - European Financial Services Round Table
5th Floor
Rond Point Schuman 6, Box 5
B-1040 Brussels
Belgium**

**Tel: +32-2-234.78.06 - Fax: +32-2-234.79.11
secretariat@efr.be
www.efr.be**