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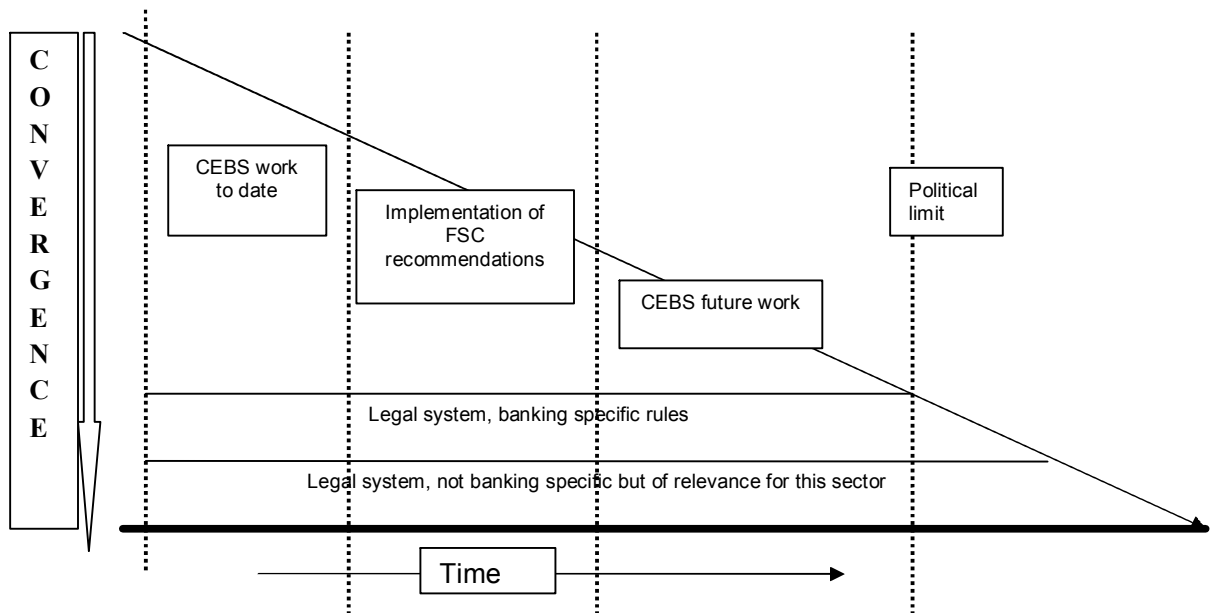
## **Progress report to the Financial Services Committee**

### **Background**

1. The Report on Financial Supervision (the 'Francq Report'), issued by the Financial Services Committee (FSC) on 17 February 2006, discussed the challenges facing financial regulation and the concrete steps that could be taken to improve supervisory arrangements in the European Union.
2. In the report, the FSC identified three major challenges for coming years:
  - (i) fostering supervisory co-operation and convergence,
  - (ii) enhancing the cost-efficiency of the EU system, and
  - (iii) improving cross-border supervision.
3. The FSC laid out a set of recommendations for meeting these challenges, some of which were addressed specifically to CEBS and its sister Level-3 Committees.
4. In particular, the FSC directed CEBS to provide an assessment of existing tools for fostering a common European supervisory culture; to explore non-binding mechanisms, such as mediation, for resolving supervisory disputes; to explore the preconditions for the delegation of tasks and responsibilities between supervisors, and to develop common supervisory reporting formats and data-sharing arrangements.
5. In this Report to the FSC, CEBS reports on the outcome of its work in these areas and on the progress made in promoting supervisory convergence. The timeline in the Annex provides an overview of the progress made and the expected deliverables.
6. For further detail on CEBS' recent activities, FSC members are invited to consult CEBS' 2006 Annual Report.
7. The three Level-3 Committees will report jointly on the cross sectoral mid-term agenda as part of their final report to the FSC.

## Executive summary

8. CEBS is responsible for promoting a consistent approach to EU banking supervision as well as for enhancing cooperation among supervisors. CEBS exercises these responsibilities within the overall framework of EU and national legislation concerning in particular banking and in general the status of supervisory authorities, companies law, tax systems and so forth.
9. CEBS is of the view that convergence is both a process and a "destination": an area or zone to which supervisory practices may ultimately converge. The process must be viewed over time, as current and past work beds down and future work takes shape. The destination or end point is harder to identify as the underlying legal constraints, both financial and general, constitute a political limit to the degree of convergence which can be achieved by supervisory authorities. A clear political commitment will thus be necessary in order to meet the target of significantly increased convergence.



10. Against these constraints and within the scope of activity open to CEBS to undertake, CEBS has made significant progress during its relatively short history in effecting convergence. This is particularly true in light of the fact that key Directives, such as the Capital Requirements Directive ('CRD'), have only recently come into effect.
11. CEBS has developed a wide range of tools for facilitating convergence. These include a comprehensive set of Level-3

guidelines to guide the implementation of the CRD at national level, as well as a number of tools recommended by the FSC in the Francq Report.

12. From a very early stage in the development of those tools, CEBS has encouraged dialogue with market participants through a variety of mechanisms, including meetings with expert groups, public consultations and hearings, technical workshops, panel discussions, questionnaires, and informal contacts. As CEBS enters the critical phase of practical implementation of the CRD, this dialogue is being intensified.
13. The close co-operation established with the other Level-3 Committees in November 2005 (the Joint Protocol) has been put into practice in 2006 and 2007 in the form of 3L3 work programmes and ever closer liaison.
14. Throughout 2005 and into 2006, CEBS developed guidelines focused on the implementation of Basel II in the EU. They cover on the supervisory review process (including technical guidelines on the measurement and management of interest rate risk and concentration risk), a common supervisory disclosure framework, common procedures and assessment criteria for the recognition of eligible credit assessment institutions, common reporting of financial and prudential information, home-host co-operation, outsourcing, and the validation and stress-testing of internal models for credit risk and operational risk.
15. In developing these tools, CEBS tried to strike an appropriate balance between detailed guidance that promotes legal certainty, and principle-based guidelines that accommodate future developments in risk management practices and provide some flexibility in supervisory approaches. This balanced approach is designed to deliver convergence in outcomes, while recognising that legitimate non-removable differences in national structures and frameworks may require differences in processes.
16. CEBS reported on this achievement in its two previous reports. In 2006, and 2007, the direction of CEBS' work has shifted from design to delivery: from the development of common supervisory approaches through guidelines, to the implementation and application of the commonly agreed principles in day-to-day supervisory practices. CEBS has initiated three main areas of work, which are described in the first part of this report:
  - a. a joint effort with the European Commission to promote consistent interpretation of the Capital Requirements Directive,
  - b. implementation of the common supervisory disclosure guidelines in the form of a web-based framework, as a tool for market and peer pressure, and
  - c. operational networks to foster supervisory co-operation.

17. In late 2006, CEBS commissioned an on-line survey to assess its performance. The survey, which was conducted for CEBS by the market research agency Ipsos MORI, asked the public to comment on CEBS' objectives and the efficiency of its working methods. The results of the survey were generally favourable, and acknowledged the enormous effort made by the European banking supervisory community in the first three years of the committee's existence. However, CEBS is conscious that behind the positive assessment was a clear message that there is room for improvement. Consequently, CEBS is exploring ways in which it can do better.

18. CEBS has initiated work to implement all of the FSC recommendations within the stated timeline, as set out in the second part of this report. In particular,

- a. CEBS has developed a pragmatic and tailored approach to promoting a common supervisory culture targets encouraging short-term secondments.
- b. CEBS has developed a mediation mechanism for resolving potential disputes between banking supervisors. This mechanism, which draws heavily from CESR' existing mechanism, is currently under public consultation and will be finalised at the end of 2007. CEBS has also initiated work on the establishment of a peer review mechanism and has developed, jointly with CEIOPS and CESR, a common methodology for impact assessment.
- c. CEBS strongly believes that disclosure is a key step towards convergence and in that respect has started to publish on its website the ways its guidelines on common reporting of financial and prudential information (COREP and FINREP) have been implemented by its members.
- d. Finally, CEBS has initiated work on making 'colleges of supervisors' work more effectively and on defining the preconditions for delegations of tasks and joint inspections, with the overall goal of improving cross-border supervision.

18. The report elaborates in Part 1.4. on the nature of the obstacles that need to be addressed to allow further progress in the process of convergence. The implementation of the FSC's recommendations, together with the ongoing conduct of supervision under CEBS guidelines, should allow national supervisors to approach the limits of what is possible under current legislation in the way of convergence in supervisory practices. Convergence in supervisory practices should go a long way toward assuring the convergence of outcomes that will promote the Single Market.

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## **Part 1: Progress in fostering supervisory co-operation and convergence: Key initiatives**

19. In the three years since its inception, CEBS has promoted supervisory convergence and co-operation in a variety of ways:

- a. by serving as an open forum for discussion of common supervisory issues;
- b. by striving for consensus on the guidelines that it has issued, and by seeking the maximum commitment to CEBS' objectives on the part of its members;
- c. by involving from the very start market participants in its work, to ensure that the supervisory approaches developed by CEBS address the challenges of increasingly complex market practices and reflect the realities of the market;
- d. by employing a broad range of channels – both formal and informal – to engage market participants;
- e. by giving due consideration to the cross-sectoral aspects and implications of its work, in particular by working closely with CESR and CEIOPS;
- f. by undertaking and delivering tangible products, such as the incorporation of prudential filters into the CRD, reduction in the number of national discretions allowed in the CRD, joint assessment of rating agencies in the context of the CRD, and enhanced transparency and comparability in the way the CRD is implemented; and
- g. by contributing to the Better Regulation Agenda with advice on forthcoming legislative proposals relating to own funds, large exposures, and the commodities business.

20. The CEBS 2006 Annual Report provides a detailed description of all the work pursued or initiated by CEBS in 2006. In this section of the report, CEBS will focus on the key initiatives.

### **1.1. CEBS is working to foster a common understanding of the new capital regime and new accounting standards**

21. The national transposition of the new Capital Regime is not, by itself, sufficient to bring about convergence. In order to achieve convergence in day-to-day supervisory practices, there must also

be a common understanding of the meaning of the rules and how they apply.

22. In order to develop such a common understanding, CEBS, together with the European Commission, constructed a website facility that permits interested parties to raise questions regarding the interpretation and transposition of the CRD. This facility has demonstrated its usefulness, as measured by the large number of questions addressed.<sup>1</sup> CEBS has also used the website to deepen its understanding on issues of immediate concern, such as the definition of significant credit risk transfer.
23. CEBS has also sought to develop a common understanding on issues that cut across guidelines on different topics. A good example of this is the principle of 'proportionality', which arises in many of the guidelines developed in 2005. Industry responses to CEBS consultation papers repeatedly highlighted the different, and often contradictory, perspectives of small institutions and large, complex banking groups.
24. On 11 January 2007, CEBS organised a workshop on proportionality which brought together banking supervisors and representatives of the main European Banking Federations. The participants concluded that, while there is no magic formula for taking proportionality into account, factors such as the nature, scale, and complexity of the business, and the systemic relevance of the entity could be helpful in addressing the diversity of the European banking sector in a pragmatic fashion.
25. In December 2004, CEBS developed a set of Guidelines on Prudential Filters for Regulatory Capital. These filters are designed to bridge the gap between solvency regime requirements – in particular, regarding own funds regulations – and new international and national financial reporting standards. The more clearly the relationship between financial and prudential reporting can be made explicit, the less reporting burden will ultimately be borne by European institutions.
26. CEBS will continue to monitor the effectiveness of prudential filters in practice. CEBS is currently carrying out an update of its 2005 internal study on the implementation of the Guidelines and their quantitative impact on regulatory capital requirements. This work is intended to identify implementation issues and to explore the need to update or refine the Guidelines.

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<sup>1</sup> Of 230 questions received by the end of April 2007, 34 have been assigned to and responded to by CEBS.

## **1.2. CEBS' supervisory disclosure framework aims at enhancing the transparency and comparability of supervisory rules and practices to all parties**

27. To assist Member States in fulfilling the Directive's requirement for transparency, CEBS has developed a web-based supervisory disclosure framework, consisting of a series of information tables in standard formats.
28. The framework is currently being populated by supervisory authorities. As of end April 2007, 23 CEBS members had connected their websites to the CEBS website. However, only a few of them had fully implemented the framework, due in most cases to delays in the national transposition of the CRD by the Member States, which necessarily has impacted the operational implementation of the framework.
29. CEBS has decided to extend the supervisory disclosure framework to include information on the two reporting frameworks (COREP and FINREP), in order to inform all market participants of the types of information collected by and available at each supervisory authority.
30. CEBS has also begun a review of the implementation of the supervisory disclosure framework, to assess how well this tool is meeting its objectives and where there may be room for improvement.
31. Transparency is a key element in the pursuit of convergence. In particular, the market pressure generated by the disclosure of the ways in which the options and national discretions contained in the CRD are exercised has helped CEBS to identify areas where further convergence in the area of national discretions is necessary and feasible.

## **1.3. CEBS operational networks facilitate co-operation between supervisors of cross-border groups**

32. The extent to which CEBS guidelines contribute to building common practices among EU supervisors can only be measured in terms of the consistency actually achieved in the application of the CRD and CEBS Guidelines to the day-to-day supervision of real-world institutions.
33. In 2006, CEBS launched a pilot project on operational networking, aiming at enhancing the consistency of day-to-day supervision and supporting the exchange of information and experiences between the consolidating and host supervisors of cross-border banking groups.
34. Each operational network consists of line supervisors experienced in the supervision of cross-border banking groups, with adequate representation of both consolidating and host supervisors.



35. The test phase of the project focuses on a limited sample of ten cross-border banking groups. If the exercise is successful, CEBS intends to extend it to other groups with significant cross-border operations.
36. The operational networks adopt a bottom-up approach to:
- (i) identifying issues arising in the day-to-day implementation of Community legislation and CEBS guidelines and in the supervision of cross-border groups, and
  - (ii) engaging groups of experts to develop a catalogue of pragmatic supervisory approaches – which are effective from both the home and the host point of view – for addressing issues, streamlining supervisory practices, processes, and tools, and reducing the compliance burden for cross-border groups.
37. The working methods of the operational networks include conducting surveys of practices, administering questionnaires, and establishing regular dialogue with the ten banking groups to identify issues. In addition, a series of workshops should help in highlighting practical and current issues of interest to the parties involved.
38. The operational networks have identified four issues as priority areas:
- home-host general co-operation issues, including the organisation of the work of Colleges of Supervisors,
  - validation and model implementation issues,
  - Pillar 2 cross-border issues, and
  - issues relating to the common reporting framework
39. A workshop on the first two issues has taken place at CEBS, at which the cross-border groups confirmed their support for the CEBS initiative. Participants shared their experiences with the ongoing validation of advanced approaches, and recognised a range of good practices for the functioning of Colleges of Supervisors.
40. The cross-border banking groups have asked CEBS to find pragmatic solutions to address a number of problems that cross border groups face with the common reporting framework, including differences in remittance dates and in the frequency of prudential reporting.
41. Three further workshops, one on the common reporting framework, one on the future of supervisory reporting and one on Pillar 2 cross-border issues are scheduled, in the course of 2007.
42. The industry has created its own operational networking platform to act as a interlocutor to CEBS' operational networks. The industry platform has generated a list of high-priority issues, and is currently working on a more precise and detailed description of them.

## 1.4. The broader context of convergence and the role of CEBS

43. Since its inception, CEBS has consistently sought to develop tools and projects that promote convergence in supervisory practices. Practical convergence towards a more consistent supervisory environment should reduce unnecessary administrative burden and allow banks to conduct their cross-border activities more cost-effectively.
44. However, CEBS continues to work under the same structural constraints that have been in place since its creation, and on which CEBS commented in its previous two reports to the FSC.
45. The most significant of these impediments to convergence are:
- i. The absence of a Single Market in some markets. For example, the mortgage market is still highly localised, and consequently attempts to arrive at a convergent view on how mortgages should be supervised may be premature or even counter-productive.
  - ii. Differences in national laws in general areas that are relevant to banking (such as commercial and company law, bankruptcy legislation, and tax law). Such differences may, despite harmonisation in banking rules, impede the adoption of common standards for banking regulation and supervision. They have, for example, been identified as constraints to convergence in the area of own funds.
  - iii. Differences adopted through the political process and already embodied in the Directives, such as the national discretions in the CRD. Such differences make convergence more difficult.
  - iv. Institutional differences in the mandates provided to supervisory authorities by Member States, and differences in the traditions and models embodied in such mandates, as highlighted in the letter to the IIMG. For example, supervisory reporting is a function of the internal organisation of supervision, including the relative reliance on on-site versus off-site surveillance, the use of early warning systems, and the recourse to peer-group analysis. Further evolution in supervisory models is one of the prerequisites to the convergence and harmonisation in cross-border reporting requirements requested by the industry. An external review<sup>2</sup> commissioned by CEBS to assess its progress in its first years of work indicates that the range of diversity – which was substantial when CEBS began its work – has narrowed, but that more needs to be done.

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<sup>2</sup> Please refer to the report of IPSOS MORI on CEBS performance assessment

46. CEBS and its members are committed to achieving convergence within the constraints of the impediments listed above. CEBS offers the following observations:

- a. Supervisory practices evolve over time, and value added is not always easy to measure in the short term.
- b. The pragmatic approach used by CEBS should be measured in terms of its ability to respond to the evolution of market practices and consolidation in the banking sector.
- c. improvements to CEBS' functioning and decision-making processes could stimulate greater progress in convergence
- d. CEBS can use tools such as supervisory disclosure or impact assessment to identify the need for and feasibility of regulatory and supervisory changes.
- e. The full the full exploitation of the potential of the Lamfalussy process will depend on a clear political commitment of national governments, including with a view to crisis situations,
- f. An assessment should be made of the likely costs and benefits of more profound and longer term structural changes

## **Part 2: Implementation of the FSC recommendations**

47. In the following sections, CEBS reports on the initiatives undertaken to implement the FSC's Recommendations and the progress achieved thus far. A more detailed description of these initiatives can be found in the 2006 Annual Report.

48. Implementation of the FSC's recommendations has been a top priority in CEBS' work programme for 2006 and 2007. As of mid-2007, work has commenced in all areas, in accordance with the timeline set out by the FSC.

### **2.1. Fostering convergence via an extended 'convergence tool kit'**

#### **2.1.1 Enhancing European Supervisory Culture through regular common training and staff exchanges targeted at the supervision of cross-border groups**

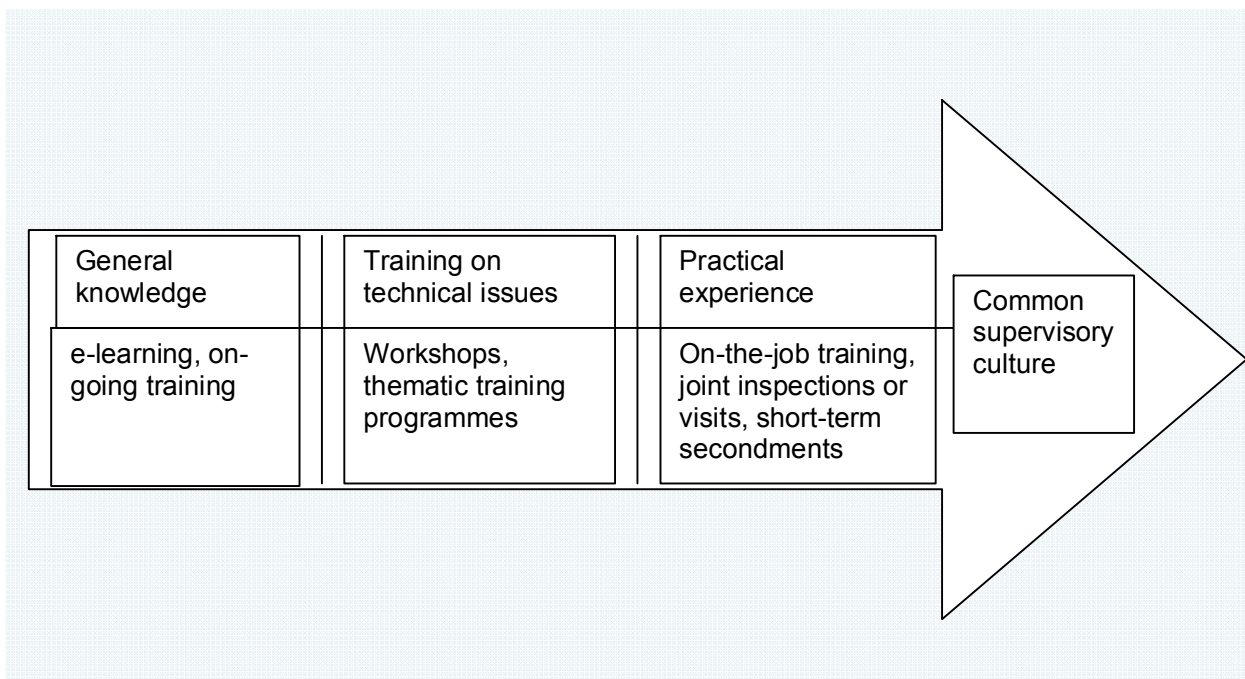
<b>FSC Recommendation 2:</b> For tools aimed at fostering a <b>European supervisory culture</b> – and which are already in place – each Level 3
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Committee could provide, in its regular reporting on supervisory convergence beginning in 2007, an assessment on their functioning and indicate any ways to help them work better.

49. A variety of tools are already in place to help build a common supervisory culture. They include:

- the informal networking and exchanges of experiences and views that take place at the meetings of various CEBS Technical Working Groups held on CEBS' premises;
- the hosting of seminars discussing case studies relating to specific aspects of banking legislation;
- joint visits by home and host supervisors to banks engaged in cross-border activities;
- on-the-job training; and
- short-term secondments.

50. All of these initiatives are intended to equip supervisory staff with the expertise and common understanding necessary for them to respond to the EU-wide challenges posed by the implementation of the CRD and the increasing integration of cross-border groups. The combination of experience and training should result in an improved set of cross-EU supervisory skills, as illustrated in the following graphic:



51. CEBS is concentrating its efforts on the following objectives:

- a. Meeting targets: each year a minimum number of staff from CEBS member organisations should take part in joint training exercises,
- b. Developing cross-sectoral training programmes jointly with CESR and CEIOPS, and
- c. Promoting staff exchanges in the context of the supervision of cross-border groups.

#### **a) Meeting targets for joint training**

##### ***Progress to date***

- 52. Building on past experience, CEBS is developing internal processes and procedures to provide joint training on a larger and more systematic scale.
- 53. A variety of tools are being used, including opening up national training programmes to fellow national authorities, joint training courses organised by several national supervisors, and seminars organised by CEBS with the assistance of the Basel Financial Stability Institute (FSI). CEBS is using its members-only website to inform national authorities of these initiatives and to advertise offers to their staff members.
- 54. In 2007, at least 100 staff members from national supervisory authorities are expected to attend seven training seminars advertised by CEBS.<sup>3</sup> These seminars will focus on supervisors' current needs, covering Basel II implementation issues such as capital allocation, securitisation, asset-backed securities, credit derivatives, Pillar 2 in the context of institutions using advanced-models, and operational risk. They have been scheduled so as to be spread evenly over the year.

##### ***Work in progress***

- 55. CEBS will explore the possibility of making FSI-Connect, a set of on-line tutorials developed by the FSI, available to all CEBS members at reduced or no cost.
- 56. CEBS' website is currently being redesigned. One objective of this project is to ensure that information on training is publicly available.

#### **b) Developing joint cross-sectoral training programmes**

##### ***Progress to date***

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<sup>3</sup> These include national training programmes opened up to fellow colleagues, and seminars organised by (or jointly with) the FSI.

57. Jointly with CESR (which initiated the project) and CEIOPS, CEBS is developing a common European framework for training in financial supervision by year-end 2007.

58. A joint 3L3 Steering Committee was recently established with a mandate to work out the governance structure and the logistical and financial arrangements for a common training framework, to identify training needs, and to explore partnerships with academic institutions, standards for qualification of the trainees, and possible certification of the training sessions.

### ***Work in progress***

59. A series of test seminars will be organised in the near future.

### **c) Promoting staff exchanges**

60. Cross-fertilisation and the exchange of ideas between supervisors is the key to effective supervision of cross-border groups. It is essential that the staff of CEBS member authorities be exposed to the working procedures and approaches of other EU supervisory authorities. This is already occurring on a bilateral basis, but should also be encouraged on a broader scale.

61. The free movement of staff between competent authorities can be hindered by the same obstacles that impede the movement of people within the EU more generally. For example, secondments or exchanges of supervisory personnel can be impeded by tax and social security issues, or by differences in the cost of living between newer and older Member States.

62. CEBS has begun to work on ways to encourage the use of secondments lasting less than six months. The administrative difficulties and the tax and legal issues raised by such short-term secondments would be much more manageable, and they could be an effective means of mobilising supervisory staff to perform tasks relating to the supervision of a cross-border group or conglomerate, for example in the context of the Supervisory Colleges referred to in section 1.3. above.

63. Since different national authorities are likely to encounter the same administrative difficulties, CEBS is currently devising a common framework to deal with these difficulties.

### **2.1.2. CEBS has launched a public consultation on a mediation mechanism to resolve potential disputes between banking supervisors**

<p><b>FSC Recommendation 3:</b> Preconditions to the establishment of a mediation mechanism should be explored – especially as regards the potential areas of application and the practical functioning of this mechanism – and, where</p>
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appropriate, a mechanism tested in the Securities field in 2006 and in the banking and insurance fields no later than by the beginning of 2008.

### ***Progress to date***

64. CEBS has developed a mediation mechanism based on the main features of the mechanism already in place at CESR, with some adaptation to the subject matter and the context of CEBS' work. Its objectives are to support existing tools for co-operation between supervisors, such as CEBS Guidelines on validation and home/host co-operation, and to ensure as much consistency as possible across sectors.
65. CEBS' mechanism, like CESR's, is a peer mechanism aimed at improving co-operation and convergence among CEBS Members. It will operate on a voluntary basis, but CEBS members have expressed a strong commitment to participate in the process on an 'accept or explain' basis (i.e., members agree either to accept mediation, or to explain the reasons for rejecting mediation). It is expected that other usual forms of co-operation will first have been exhausted, before resorting to mediation.
66. The CEBS mediation mechanism focuses primarily on the Capital Requirements Directive and related CEBS Guidelines, since competent supervisory authorities are currently occupied primarily with issues arising from the implementation of Basel II, and therefore that is where disputes are most likely to arise.
67. No specific articles of the CRD have been excluded at the outset from the scope of mediation. Potential areas where mediation may be useful in resolving tensions or disputes include the processes for consultation with other relevant competent authorities in advance of decision-taking by a specific competent authority, the exchange of information, processes for joint agreement or joint decision-taking between competent authorities, and other areas relating to co-operation between competent authorities (for example, in the context of Pillar 2).
68. As in CESR's mediation mechanism, only CEBS members will be able to initiate the mediation process. However, market participants will be able to be involved indirectly, by drawing the attention of their national CEBS Member, the CEBS Consultative Panel, or a meeting of an operational network, to areas in which convergence is not occurring and mediation may be necessary.

### ***Work in progress***

69. CEBS' proposals are currently under public consultation and should be finalised by year-end 2007. A test phase is scheduled for 2008. A review of the mechanism is scheduled for two years after initial implementation.

### **2.1.3. CEBS has initiated work on the establishment of a peer review mechanism in 2008**

#### ***Work in progress***

- 70. The Francq report stated that 'greater co-operation and convergence between supervisors requires evolutionary enhancements to the overall supervisory culture and practices in order to optimize the supervisory framework. The ways and means of developing "peer reviews" should be further explored to ease supervisory convergence.'
- 71. Peer review is a convergence tool in the sense that it should encourage greater similarity in the application by supervisory authorities, at the national level, of the rules implementing EU legislation and Level 3 guidelines.
- 72. Peer review should identify areas of regulation where, for legitimate reasons, convergence is not possible. It should also highlight areas of high consistency and good or best practice.
- 73. CEBS is currently working on the details of the mechanism, benefiting from the experience already gathered at CESR. It is important to note that CEBS has already developed or is already using tools, such as supervisory disclosure and technical workshops and networks that aim at fostering convergence.
- 74. Supervisory disclosure is intended to go a long way in matching the aims and objectives of peer review, in terms of transparency and bringing market pressures to bear on national authorities.
- 75. CEBS intends to finalise its mechanism and put it into practice in 2008.

### **2.2. Enhancing the cost-efficiency of the EU system**

- 76. The Francq report stated that 'supervisory convergence needs to be intensified to implement the FSAP in a consistent manner across the EU and thus, to reap the benefits of the financial services Single Market. The over-arching goal should be to enhance the contribution of the European financial system to the Lisbon strategy, including by ensuring financial stability and by avoiding both overburdening companies operating in Europe with unnecessary supervisory costs - whether direct or indirect - and inhibiting, or restricting, fair competition.'

#### **2.2.1. CEBS is monitoring the implementation of the reporting framework, as a first step towards further streamlining the framework**

<b>FSC Recommendation 5:</b> Supervisors are encouraged to work on common formats before the end of 2007, and to reflect on the
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question of IT data-sharing arrangements before the end of 2008, taking into account the costs and benefits of the different options available (common databases, interlinked national databases, etc.). [...]

77.As acknowledged in the Francq Report, CEBS has already made progress on convergence in supervisory reporting, with the finalisation of CEBS guidelines on common frameworks for prudential reporting (COREP) and financial reporting (FINREP). COREP establishes common data requirements relating to the calculation of the solvency ratio under the regime of Directive 2006/48/EC. FINREP establishes common requirements for reporting consolidated financial data that are consistent with international financial reporting standards (IAS/IFRS).

### ***Progress to date***

78.CEBS is ensuring a smooth implementation of its reporting guidelines:

#### **a) By responding in a timely manner to industry's questions**

79.CEBS has set up a European network of supervisory experts that will respond to industry's questions relating to the FINREP and COREP frameworks and the associated XBRL taxonomies. Institutions can submit questions to CEBS' operational network, which will formulate a co-ordinated answer. This mechanism will help ensure that the reporting frameworks are implemented properly, and in particular will reduce the risk that different national authorities will adopt divergent operation implementations of the reporting frameworks. CEBS website has activated an on-line tool that allow institutions to pose their questions directly and will make the responses publicly available.

#### **b) By ensuring full transparency and comparability of national reporting requirements**

80.As mentioned in Section 1.2., above, CEBS' web-based framework now includes summary information on the implementation of the prudential reporting frameworks. Full disclosure of the details of their implementation is scheduled for year-end 2007.

81.These disclosures give national supervisory authorities the opportunity to explain the choices they have made due to national circumstances, conditions, and practices. It also makes it easier for supervisors and market participants to compare national reporting requirements.

82.A study is currently under way to assess the degree of commonality achieved in the implementation of CEBS' reporting guidelines. The study also includes a comparison with third countries. The results of the study will enable CEBS to identify the

scope for further streamlining of the frameworks on a cross-border basis.

***Work in progress***

83. On the basis of this work, CEBS will assess the extent to which the reporting guidelines reduce the cost of reporting for cross-border institutions, and will then assess possible further steps.

84. At this stage, CEBS believes that the reporting frameworks will indeed reduce institutions' reporting burden and their cost of modifying their IT-systems, for a variety of reasons:

- a. The supervisory reporting systems are being introduced simultaneously with the introduction of the new capital and accounting regimes, thus avoiding the need for institutions to modify to their systems twice.
- b. Common data definitions will simplify the collection and the exchange of data of cross-border institutions.
- c. For countries that wish to use them, the XBRL-based taxonomies used in both frameworks will give institutions the opportunity to centralise and simplify their procedures for regulatory reporting, by using the same data and definitions.
- d. In response to the industry's request, no major new requirements are planned in the next few years, in order to avoid undue repetitive implementation costs (although CEBS will keep the FINREP framework up to date with changes on IFRS/IAS, so that institutions do not have to use two frameworks: one that is IFRS compliant, and the other that is not. As a rule of thumb, these types of changes will be made on an annual basis).

### **2.2.2. CEBS, jointly with CESR and CEIOPS, will develop a methodology for impact assessment**

85. The 3L3 committees have agreed to work together on guidelines on impact assessment (IA). This work recognises the growing importance that the European Commission attaches to IA as a tool for improving regulation. It also acknowledges the views of the Inter-Institutional Monitoring Group (IIMG), whose First Interim Report suggested that IA should be applied by all parties involved, including the European Parliament and Council (when tabling substantive amendments to Commission proposals) and supervisors (when they give advice to the Commission).
86. The three Level-3 committees have agreed on a set of general IA principles. They have also devised a working methodology, which will be published as a practical handbook, to guide the committees' experts in using IA in their policy analysis and recommendations.
87. The aim is to improve both the content and the processes involved in the production of Level-2 advice and Level-3 measures, from the initial mandate stage through the analysis of various policy options, public consultation, feedback, and ex-post review.
88. This work was mentioned in the joint 3L3 response to the Second Interim Report of the IIMG.
89. The three committees have just issued a joint public consultation paper on the IA methodology, based on the state of the art and current good practice.

### **2.3. Improving cross-border supervision**

90. The Francq report stated that "the growing number of cross-border financial groups and operations in Europe leads to increasing cross-border reallocation of functions within financial groups with some functions centralised in the parent company while others are pursued or outsourced abroad, thus challenging traditional supervisory arrangements. In this respect, the organisation of supervisory arrangements should be able to keep pace with, and respond to, market developments in a flexible way."

#### **2.3.1. CEBS' efforts to make colleges of supervisors work more effectively**

91. The FSC noted 'the additional momentum that setting up colleges of supervisors can bring to cross-border group supervision in terms of supervisory coordination (e.g. for on-site visits or exchange of information), mutual understanding and trust-building. The FSC would like to underline that a collegial approach may prove useful

for fostering delegation, which would be easier to develop under the "umbrella" of colleges of supervisors.'

### ***Progress to date***

92. The practices of colleges of supervisors and home-host relationships for cross-border groups have been investigated through the operational networks mentioned above. Two types of colleges have been identified:
  - a. "longstanding" colleges related to groups with well-established cross-border structure, in which there is a more structured approach to supervisory co-operation;
  - b. recently established colleges focusing initially on the co-operation activities related to Basel 2 implementation, but with the intention of extending their scope to the overall supervisory activity regarding the banking groups concerned.
93. Colleges can also be distinguished according to the types of tools they use for co-operation, which can depend on the organisational structure of the groups.
94. The practical model of cross-border co-operation and the division of duties among the supervisors within the college is generally tailored to the structure of the banking group's decision and control systems.
95. CEBS has assessed the current situation, and is now fleshing out proposals for improving cross-border supervision and ensuring the coordination of supervisory activities related to cross-border groups in colleges. CEBS has concluded that:
  - a. Colleges should be a tool for fostering the exchange of information, in order to allow more efficient supervisory action, avoid duplication of effort, and develop a common understanding on the risk profile of the group.
  - b. The activities taking place within colleges should encompass not only the exchange of information, but also planning and coordination of supervisory activities such as ICAAP requirements and assessments, joint risk and capital adequacy assessments, joint on-site visits, and the allocation of tasks among supervisory authorities.

### ***Work in progress***

96. CEBS will develop a 'good practices' paper covering topics such as co-operation and exchange of information, sharing of tasks and delegation, the supervisory review process, and mechanisms for resolving issues and divergences. The paper will build upon the existing CEBS Guidelines on Supervisory Co-operation for Cross-Border Banking and Investment Firm Groups.

97. In addition, CEBS will draw up templates to assist supervisors in developing written agreements for banking groups pursuant to the requirements of Article 131 of the CRD.

### 2.3.2. CEBS is defining the preconditions for delegation of tasks and joint inspections

**FSC Recommendation 4:** Preconditions for the use of delegation mechanism in the three sectors should be explored – especially through the use of guidelines – and, where appropriate, arrangements tested before the end of 2007.

98. The Francq report recommended that supervisors develop a framework for delegation of supervisory *tasks* in the banking sector, and asked whether guidelines could be drafted. It also suggested that these guidelines could provide general principles for identifying situations in which delegation could be considered and the broad framework within which delegation arrangements could be developed. The FSC also noted that work on the delegation of *responsibilities* could follow at a later date.

#### ***Progress to date***

99. At this stage, CEBS has considered only the delegation of supervisory *tasks*. As the FSC suggested, it has put aside for the time being the delegation of general supervisory *responsibilities*, which would involve a much deeper debate on the legal basis of supervision at the national level.

100. CEBS believes that enhanced co-operation and coordination of supervisory activities and an efficient division and allocation of resources can contribute significantly to more effective and cost-efficient cross-border supervision.

101. CEBS has conducted a stock-taking exercise on supervisors' experience with delegation. The exercise found that:

- A number of host supervisors have, for some time, delegated the supervision of the liquidity management (of branches) to the home supervisor. CEBS members believe that greater use could be made of this possibility.
- Model validation has and will increasingly give rise to particularly close cooperation and some sort of division of tasks among supervisors. As indicated above, CEBS is discussing how delegation of model validation in the context of Article 129(2) of the CRD could work in practice, especially in the context of supervisory colleges and the working arrangements between consolidating and host supervisors for model validation, such as host supervisors' validating local models.

- Some supervisors have already begun to develop fully integrated approaches to supervisory co-operation, including joint inspections/supervisory visits. These are particularly effective and efficient forms of joint supervisory work, encompassing custom tailored, but informal, arrangements for two-way delegation of tasks between the consolidating and the host supervisors.
102. Delegation can take a variety of forms, ranging from joint inspections, to the assignment of particular tasks to be performed on behalf of other supervisors, to full and formal delegation of responsibility.
103. A co-operative and informal approach in colleges of supervisors, or bilaterally between home and host supervisors, may in some cases be more practical than formal delegation agreements, and may help supervisors realise efficiency gains more quickly. It may be more efficient to assess tasks on a case-by-case basis and to tackle supervisory issues through close co-operation. However, in other cases, it may be useful or necessary to adopt formal agreements.
104. Delegation can be useful in both directions: from the home to the host supervisor, and vice versa.
105. When segments of the banking industry lobby for more delegation, these demands are usually made in the context of seeking more powers for the consolidating or home supervisor. In effect, the industry often sees delegation of tasks and responsibilities as meaning only delegation from the host to the home supervisor. But for some tasks, it may be more efficient and cost effective in practice for delegation to flow in the other direction, from home to host, in order to take advantage of the local knowledge of the host supervisors.

### ***Work in progress***

106. In 2007, CEBS will work on ways to facilitate the use of delegation arrangements, including joint inspections. CEBS will also assess potential practical obstacles to delegation, and suggest ways to eliminate them. CEBS will adopt a broad perspective in its work on delegation, to ensure that the maximum benefit is derived from the concept.
107. Supervisors need to be clearer on when it is appropriate to use formal versus informal forms of delegation, and they need apply the concept of delegation in a consistent and convergent way.
108. Supervisors are likely to become more comfortable with the idea of delegating tasks as they become more familiar with the new CRD framework, and as they build trust and develop closer supervisory co-operation. These developments will help CEBS members to overcome concerns about losing direct control over a

task, and about the reputational risk that may arise when the practical management of a task is separated from the formal legal responsibility for carrying it out.

## **Conclusion**

109. CEBS has devoted a great deal of effort and resources to developing tools that encourage and facilitate convergence, including those envisaged in the FSC recommendations. CEBS, in liaison with CESR and CEIOPS, will continue to explore further developments and to consider suggestions for improving the way it operates, and will communicate the results of this work to the FSC.



## Timeline for implementation of the FSC's recommendations

Action/mandated deliverable, and deadline	2006	2007 H1	2007 H2	2008 H1	2008 H2	2009 H1
<b>1. Monitor convergence of supervisors' powers- ECOFIN Council (via the FSC and the EFC) to provide political impetus for the process of supervisory convergence in FSAP implementation (Francq) FSC report to ECOFIN via EFC (starting in autumn 2006), <u>annually</u></b>						
Regular monitoring (led by FSC in co-operation with 3L3 and Commission)		-	report	-	report	-
<b>2. Fostering a European supervisory culture - assess and improve functioning of tools</b>						
Common Level-3 training systems	Two joint training seminars organised by CEBS jointly with the FSI in 2006	7 CEBS joint training programmes and seminars with a target of 100 members of staff.  Joint 3L3 Steering Committee to develop platform for training with a cross-sectoral focus				
Secondment schemes	Bilateral secondments between supervisory authorities on a variety of general supervisory issues	Common framework for facilitating staff exchanges, with a particular focus on short-term secondments to be used e.g. in the context of model validation of cross-border	Quantitative targets to be defined and met			



Action/mandated deliverable, and deadline	2006	2007 H1	2007 H2	2008 H1	2008 H2	2009 H1
		groups,				
Impact assessment	Joint work with CESR and CEIOPS on key principles and methodology	3L3 Consultation and pilot project	Start using the methodology for future L2 and L3 products	Report to FSC		
Peer review		Feasibility study and design of the mechanism		Pilot project, establishment of the mechanism	Report to FSC	
Joint inspection and supervisory visit teams	See also work on delegation below	Cross-group efforts and exchange of information on the implementation of the CRD, division of labour in colleges of supervisors				
<b>3. Mediation mechanism: Progress report to FSC on steps taken and outstanding obstacles and issues, <u>by end 2008</u></b>						
Tailored mediation - on a sectoral basis, further exploration and, where relevant, pilot test.  Progress report to FSC on steps taken and outstanding obstacles and issues	Dedicated work stream initiated	Proposed framework under public consultation	Finalisation of the proposal	Test phase	Report to FSC	Implement mediation mechanism
<b>4. Delegation of supervisory tasks and, where legally possible, responsibilities</b> <b><u>Guidelines, and progress report by Level 3 Committees to FSC on steps taken to further guidelines and outstanding obstacles and issues, by end-2007</u></b>						
Delegation arrangements explored (incl. guidelines) and tested where possible in each	Stock-take of existing practices and legal issues impacting on delegation	In progress:  work on areas, forms and processes of delegation of tasks.  Detailed Work programme to be agreed including a joint 3L3 approach to work on			Report to FSC	CEBS review implementation

Action/mandated deliverable, and deadline	2006	2007 H1	2007 H2	2008 H1	2008 H2	2009 H1
sector. CEBS guidelines on supervision of cross-border groups (home-host)		common cross-sectoral issues				
Operational networks (colleges of supervisors). Establishment of operational networking arrangements for day-to-day supervision of cross-border groups.	Start-up phase.	Practical experience in cross-border working group: test phase	Test phase reviewed by CEBS	Potential roll-out of the test phase to wider number of banking groups or investigation of alternatives to cross -group operational network project  Where necessary, initiation of the development of guidelines and recommendations on the working of colleges.	On-going CEBS review	
<b>5. Streamlining of reporting and supervisors' data-sharing arrangements</b> <b>Work on formats, <u>by end-2007</u></b> <b>Feasibility report to FSC on possible alternative, <u>by end-2008</u></b>						
Work on common reporting formats. Before the end of 2007	COREP and FINREP guidelines  Information exchange on reporting frameworks (and related IT-support systems) with the other 3L3 committees.	Disclosure of the implementation of FINREP and COREP  Assessment study on convergence on reporting in Q3  On-line facility to address implementation	To be determined			

Action/mandated deliverable, and deadline	2006	2007 H1	2007 H2	2008 H1	2008 H2	2009 H1
		<p>questions from industry</p> <p>Analytical 3L3 report to be endorsed by 2007 H1 on potential overlaps or inconsistencies in reporting requirements stemming from sectoral EU-directive</p> <p>Further 3L3 work depends on outcome of analytical report</p> <p>End-2007 Report to FSC and Commission</p>				
<p>Tailored solutions on IT data-sharing arrangements (e.g. common EU-wide databases or interlinked national databases)</p> <p>Feasibility report to FSC on possible alternatives.</p>	<p>CEBS to advise on information to be shared in normal and crisis times, which should be built into existing or improved information sharing IT platforms in colleges and between supervisory/monetary and ministerial authorities</p> <p>If and when there appears to be a gap which could be filled in the most effective and efficient way by CEBS (for example, the transaction reporting example in CESR's MIFID context), a feasibility study may be contemplated</p>	Joint BSC/CEBS advice to be finalised on data shared in preparation for and in crisis situations	CEBS to discuss the proposals and report to FSC and/or mandate further work	To be determined		
		<p>CEBS to monitor the use of COREP / FINREP taxonomies across countries and to assess the need for IT-based data sharing arrangements in this area</p> <p>CEBS to investigate improving information sharing via its members' website, supporting members in areas such as day-to-day co-operation, policy information</p>		To be determined		

Action/mandated deliverable, and deadline	2006	2007 H1	2007 H2	2008 H1	2008 H2	2009 H1
		sharing, and crisis management				
<b>6. Regular overall assessment of steps taken with respect to the tools proposed in this report - support to Lamfalussy and to supervisors' co-operation and convergence efforts (Francq).</b> <b>FSC report to ECOFIN via the EFC, and possible ECOFIN conclusions, prep. by FSC via EFC, <u>annually</u></b>						