January 2012

AK Position Paper

Basel III - Capital Requirement Directives COM(2011) 453 final (CRD IV) and COM(2011) 452 final (CRR)

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AK EUROPA

About us

The Federal Chamber of Labour is by law representing the interests of about 3.2 million employees and consumers in Austria. It acts for the interests of its members in fields of social-, educational-, economical-, and consumer issues both on the national and on the EU-level in Brussels. Furthermore the Austrian Federal Chamber of Labour is a part of the Austrian social partnership.

The AK EUROPA office in Brussels was established in 1991 to bring forward the interests of all its members directly vis-à-vis the European Institutions.

Organisation and Tasks of the Austrian Federal Chamber of Labour

The Austrian Federal Chamber of Labour is the umbrella organisation of the nine regional Chambers of Labour in Austria, which have together the statutory mandate to represent the interests of their members.

The Chambers of Labour provide their members a broad range of services, including for instance advice on matters of labour law, consumer rights, social insurance and educational matters.

More than three quarters of the 2 million member-consultations carried out each year concern labour-, social insurance- and insolvency law. Furthermore the Austrian Federal Chamber of Labour makes use of its vested right to state its opinion in the legislation process of the European Union and in Austria in order to shape the interests of the employees and consumers towards the legislator.

All Austrian employees are subject to compulsory membership. The member fee is determined by law and is amounting to 0.5% of the members' gross wages or salaries (up to the social security payroll tax cap maximum). 560.000 - amongst others unemployed, persons on maternity (paternity) leave, community- and military service - of the 3.2 million members are exempt from subscription payment, but are entitled to all services provided by the Austrian Federal Chambers of Labour.

Herbert Tumpel
President

Werner Muhm
Director

Executive Summary

The BAK would like to convey the following statement on the proposal of the Commission for a Directive of the European Parliament and of the Council on the access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms and amending Directive 2002/87/EC of the European Parliament and of the Council on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate (CRD IV; COM(2011) 453 final) and on the proposal of the Commission for the Regulation of the European Parliament and the Council on prudential requirements for credit institutions and investment firms (COM(2011) 452 final):

The AK position in detail

The European Commission has submitted on **20 July 2011** a legislative proposal implementing the BâleBâle III accord into European law. The European Parliament and the Council of the European Union have yet to approve the legislative proposal. The Regulations are to be adopted in 2012 and shall come into force on **1. January 2013.**

The reform package replaces the current Capital Requirement Directives **(2006/48/EC and 2006/49/EC)** and consists of these two **acts:**

- **Directive (CRD IV, Directive)** that with regard to achieving objectives allows scope for the implementation into national law. It contains basic rules on requirements for conducting banking activities, the freedom of movement to establish branches or to provide services as well as principles in respect of the new Banking Supervision. Apart from that, the Directive addresses issues such as corporate governance, sanctions and capital buffers.

- **Regulation (CRR, Regulation)** with immediate binding effect for all credit institutions in the EU Member States. The Regulation contains requirements for credit institutions and investment firms and in particular lays down provisions on the areas of **capital definition, liquidity, leverage ratio** and **counterparty credit risk.** Apart from that it includes the implementing rules for the transitional periods in accordance with the BâleBâle III accord. The Regulation is directly applicable; a translation into national law does not apply.

Implementation of Basel III accord

As to content, the publication of the legislative proposal of the European Commission does basically not provide many surprises as it is to a large extent based on BâleBâle III; however, specific regulations in respect of **corporate governance** and **sanctions** have been added, and it lays down procedural standards for supervisory authorities and rules for the cooperation of supervisory authorities. Some - not insignificant - details distinguish themselves clearly from Bâle III; this applies in particular to the **Regulation CRD IV** in the areas of **capital, liquidity coverage ratio (LCR)** and **net stable funding ratio (NSFR),** in respect of the **trading book** and the **leverage ratio.**

Overall, the AK regards the present regulation in connection with the already applicable Directives CRD II and CRD III, which among other regulate the resecuritisation, and the fact that the counter party credit risk has been given greater consideration in the trading book, as being sensible and as the right way forward, because in particular investment banking transactions are subject to relatively stronger capital and liquidity standards as this is the case for commercial banks. In particular the aimed at improvement of the quality of own fund elements has to be rated as positive.

The proposed provisions concerning the liquidity standards have yet to be specified in more detail by EBA and are subject to long implementation periods. In view of the liquidity problems - that arose in the course of the financial and banking crisis following the collapse of Lehman Brothers - which in case of some institutions that had operated on the basis of excessive maturity transformation had rapidly led to solvency problems, a swift implementation can only be supported. From the point of view of the AK, it is definitely sensible and possible to implement the calibration, hence the LCR and the NSFR earlier than so far had been planned. The purpose of the planned regulation, according to which institutions have to report data to the regulatory authority to supervise the period transformation, is among others the calibration of standards. As a result, a number of issues cannot yet be assessed finally. In respect of a wide range of technical standards, the present package is in a conundrum between the necessity to deal with certain issues as close as "possible to the market" and not to overload the Directive, and the problem of the lack of democratic legitimation, where regulatory competencies are transferred from the legislative bodies to the supervisory authorities. Hence, the question whether the path of European institutions will lead to a more stable financial system, a stronger weight of general over particular interests and a standard-setting process, which is more oriented towards citizens, remains to be seen in practice. The current crisis is not least a result of the fact that too much attention was paid to what experts from the industry had to say and that too little - not only in the European Union - attention was paid to experts and representatives of other interest groups.

An important point will be how the Union and her Member States will handle the problem of incentive systems. After the comprehensive - and basically sensible and necessary - bank rescue packages the "moral hazard" problem has even intensified because the credit institutions saw that they would be bailed out when push comes to shove. What is therefore required are mechanisms, which get to grips with such incentive problems.

From the point of view of the AK, these include, apart from the important provisions for remuneration systems, corporate governance, improve capital requirement rules including a leverage ratio, also dealing with systemically important financial institutions (SIFI), which until now has not been satisfactorily regulated. In our opinion an approach on two levels would be appropriate:

- adequate treatment of SIFIs in respect of the required level of own funds,

- greater separation of investment and commercial banking risks, for example through separated provision of own funds under company law for both sectors in the group of institutions,

- the separate depiction of portfolios should also be improved within the sectors,

- and a living will in connection with clearer, more defined group structures, which facilitate a oderly market exit (for all institutions).

Draft Directive CRD IV COM(2011) 453

To begin with, the most important new features of the Proposal for a **Directive COM(2011) 453** are presented and assessed from the point of view of the BAK, including the following issues:

(1) **Article 64-70:** supervisory powers and harmonisation of **sanctioning powers** trough competent authorities

(2) **Article 86-91:** improvement of g**overnance arrangements,** requirements on the **management body**

(3) **Article 75-77:** strengthening of **internal ratings** and establishing **risk committees**

(4) **Article 122-131:** implementation of **capital buffers**

(5) **Article 151:** more independence of **external ratings**

To begin with, a critical view has to be taken with regard to the fact that the Directive predominantly - and in particular with respect to governance - remains little specific and rather vague. First, the European Banking Authority (EBA) has to prepare detailed implementation arrangements in form of so-called **regulatory technical standards.** The timetables for this are different; for example, **drafts** in respect of the governance issue should be available by 2015. This creates a time vacuum as it is planned that the regulations already apply from **1 January 2013.**

Apart from that, it has to be pointed out that the Directive exclusively addresses the **management body** and in doing so solely refers to the monistic system whilst the issues concerning the dualistic system, hence supervisory board and management board, are not considered adequately. However, a clear separation of tasks and competences of management and supervision is urgently required. Trustworthy supervision can only be guaranteed if **qualified and independent supervision resp. control** is carried out by non-executive directors and/or members of the supervisory board.

Supervisory powers and sanctions

Article 64 of the CRD IV Draft lays down the supervisory powers of the Member States as minimum standards. In accordance with Article 64 (a), the Member States are entitled to require the institutions to hold own funds related to elements of risks (laid down in the Regulation). The correct approach would be to stricter separate the risks within institutions (groups of institutions) resp. to make them more separable. To insert "separated according to risks" into the phrase "... hold specific own funds related to elements of risks and risks not covered separated according to risks…" would provide the option to isolate the commercial banking risk better from the investment banking risk, which would facilitate rehabilitation and handling in case of crisis, thereby reducing the risk for the economy as a whole and the taxpayer. Such a provision would also facilitate a planned "living will", apart from meeting a request for clearer structures, as it has been demanded by the de Larosière report. However, it would not go as far as the Volcker Rule proposed by the Dodd-Frank Act (DFA).

The obligation of the Member States to impose appropriate, deterrent and effective sanctions in case of breaches of law is - as is the fundamental obligation to publish such breaches - to be welcomed. However, some aspects have to be clarified before this takes concrete shape.

In some cases, facts and sanctions are defined as minimum requirements for national laws within an upper limit, whereby there are differences between the English and the German version of the text. The English version of Article 66 (2) lit e reads "up to twice the amount of the benefit derived from the breach where that benefit can be determined", whilst the provision in the German version talks of "administrative fines equal to twice the amount of the benefit derived from the breach, as far as that benefit can be quantified".

The Directive does not separately determine the form of the **publication** of the breaches. In any case, the form of publication should be official and appropriate. Apart from that, it is possible to refrain from the publication if it would jeopardize the stability of the financial markets. Furthermore, the publication may be anonymous when it would cause a 'disproportionate damage' to the parties involved. This requires a clearer restriction of the first provision. When considering the interests, the public interest in a more transparent and fair capital market that conforms to the rules has to be given priority over the private (profit-related) interest of the institution infringing the rules. Otherwise it has to be feared that trust in the capital market and the institutions overall will be undermined even further.

Article 69 determines the criteria the competent authorities have to apply for determining the type of administrative sanction. It should be clarified that "losses for third parties caused by the breach" must also include indirect monetary losses. The fact that in accordance with Article 70 appropriate protection is provided to employees of institutions who denounce breaches committed within the institutions must be expressly welcome from the employees' point of view.

AK position:

- Own funds within a group of institutions should be kept separate under company law and divided into types of risk (at least commercial banking and investment banking) in order to avoid the risk of contamination between the sectors and to facilitate restructuring or orderly market exit (in view of a "living will"), thereby reducing the risk for the taxpayer (ring-fencing).

- A provision, committing the Member States in cases affected by Articles 66 and 67 of the Directive, to determine **a minimum level of penalties** on the one hand in order not to miss the intended deterrent effect and to provide as little as possible incentives for supervisory arbitrage on the other.

- The definition of clear criteria in Article 68, when the publication of a breach might jeopardize the *stability of the financial markets.* In any case, when considering the interests, the public interest in a more transparent and fair capital market that conforms to the rules has to be given priority over the private (profit) interest of the institution infringing the rules. Otherwise it has to be feared that trust in the capital market and the institutions overall will be undermined even further.

- The deletion of the option to publish sanctions on an **anonymous basis** in the last sentence of Articles 68, as this contradicts the basic intention of the legislative initiative.

Independence of external ratings

Article 76 of the Directive determines that institutions have to undertake credit risk assessments which do not rely solely or mechanistically on external ratings. Institutions "with material risk exposure or a significant number of counterparties" have to take appropriate steps to use internal models to calculate own funds requirements.

The Commission determines the definition and restriction of these institutions in Article 126 (3) by delegated act at the proposal of EBA. No sanction mechanisms and concrete details exist for this provision so that the current proposal is primarily equivalent to a - undoubtedly welcome - declaration of will by the Commission.

From the point of view of the AK, risk assessment is at the heart of banking, even constituting its very existence. Economic theorists regard banks first and foremost as efficient institutions because they, when checking the credit worthiness in particular of those borrowers, who are too small for financing without intermediary, because collecting information about them would be too time-consuming for market participants. However, the more credit institutions outsource this unique information function of an intermediary, the more they put their own institutional function in question. As a result, in particular checking the credit worthiness of small to medium-sized enterprises represents an important function of smaller credit institutions. Institutions should therefore refrain from engaging in transactions, whose risk cannot be assessed internally, or limit them to such an extent that they cannot pose a significant risk to them. If data for sufficient internal rating scores is not available to the credit institution, investments should be limited within the scope of a very low exposure limit.

In accordance with Article 150 (2), from 2014 onwards a report will be published biannually about the extent legislation of Member States referring to **external ratings** and about steps taken by Member States to reduce such references. This report shall also evaluate the action of competent authorities with regard to establishing internal ratings and internal steps. A more timely solution would be welcome.

AK position:

- **Sanction mechanisms** for credit institutions that demonstrably fail to take appropriate internal steps in accordance with Article 76 should also be included in the Directive.

- This seems to be necessary as the report, in accordance with Article 150 (2), only refers to the obligations of the competent authorities and not to those of the institutions. Therefore, a reduction and gradual decrease of claims, whose risk assessment is exclusively based on external ratings, could be undertaken by annually downgrading solely externally assessed assets by one risk category when no internal risk assessment exists.

• Institutions, whose claims in absolute terms are not significant, but who at the same do not have a number of significant counterparties, should be able to use simplified statistical models, or, if they belong to a sectoral grouping, be able to outsource this function to the next highest level instead to external ratings.

• In view of the role rating agencies have played since the start of the financial crisis (see for example the FCIC Report, the IMF Global Stability Report and the de Larosière Report to name but a few), the BAK is extremely concerned that credit institutions should be able to continue relying on external ratings. The assessment of the risk is the very own core competence of credit institutions and it should not be permitted that it is outsourced in its entirety. If a credit institution (or another professional investor) is not able to adequately assess the risk, it should refrain from handling this transaction. The Financial Stability Board states: "Banks, market participants and institutional investors should be expected to make their own credit assessment, and not rely solely or mechanistically on CRA ratings" (Financial Stability Board 2010, Principles for Reducing Reliance on CRA ratings, p. 2). Hence, external rating can only be one of many variables in respect of risk assessment.

• Smaller institutions should be able to use a simplified internal rating model. Relying exclusively on external ratings for regulatory purposes should not be permitted in general.

• No automatic contract terms in respect of subsequent changes of external ratings: all contract terms should be legally cancelled that include automatic consequences (e.g. interest rate increases for borrowers, higher level of securities, due dates of receivables) based on later changes of external ratings.

Governance (Article 86-91)

To begin with, the AK suggests for the text to strengthen more the fact that companies in the Member States are subject to two different governance systems: monistic (one tier board) and dual (two tier board). The AK recommends in this context a **clear differentiation** of the responsibilities and competences of the chairman of the supervisory board resp. the Chief Executive Officer. In contrast to the monistic system, the roles assumed by supervisory board and executive board in the dualistic system (two tier board) are clearer defined: Germany, Denmark, Finland and the Netherlands as well as Austria have adopted relevant binding legal provisions. The advantage of the dualistic system is that executive board and supervisory board belong to separate committees and that legislative bases exit for the respective assignment. A clear separation of tasks and competences of governance and supervision is essential, as reliable supervision can only be guaranteed through **qualified, independent supervision resp. control** carried out by non-executive directors resp. members of the supervisory board.

The Directive urges the Member States to ensure a strengthening of corporate governance in the institutions. The relevant governance rules should be based on the following:

- defined **responsibilities** concerning the **approval** and **effective supervision** of among other strategic targets, risk strategy as well as of internal governance

- the chairman of the management body does **not at the same time assume the function of the CEO** (unless this is justified and approved of by the competent authorities).

Apart from that the management body has

- to **monitor,**

- regularly **assess** the governance regulations and in case

- of deficits take appropriate remedial action.

A **nomination committee,** which shall be made up of non-executive directors, presents the management body with proposals to fill mandates that are becoming vacant and recommends candidates. In respect of succession planning, the committee will focus on **balance and diversity** of knowledge, skills and experiences; it will assess the **time commitment** and apart from that deal with structure, size, composition and performance of the management body. Establishing a nomination committee may not be necessary in view of size and complexity.

AK position:

Nomination committee

The AK demands clarification as to the request that Labour representatives have to be part of the nomination committee in accordance with national employee participation regulations.

Management body

Article 87 specifies the **requirement profile** (good repute, knowledge, skills, experiences, etc.) of the management body. The following **combination of functions** is permitted **in the management body:**

- one executive directorship and two non-executive directorships

- four non-executive directorships

However, this does **not apply within the same Group;** apart from that the supervisory authority may permit additional **multiple mandates** (if complexity and/or scope allow it). **Diversity** in relation to gender, age etc. shall be promoted.

EBA will provide the Commission by 2015 with **binding technical standards (regulatory standards such as time commitment)** for the evaluation of suitability of members of management and supervisory bodies, as well as with a benchmarking for handling diversity practices.

AK position:

Initially, it has to be criticised that the present Directive proposal with regard to the issue of governance only refers to the monistic board system (one tier board); through reference is made to the management body. The issues concerning the dualistic system (two tier board) with the clear separation of supervisory board and management board, which applies in different forms among other in Germany, Denmark, Finland or Austria, are not taken into account.

Combination of functions/supervisory board

The AK is decidedly in favour of a restriction of mandates which can be held by board members resp. members of the supervisory board: the number of functions held shall not exceed **maximal four non-executive directorships** in other institutions or in supervisory bodies of institutions with comparable requirements, whereby the **chairmanship of the supervisory board counts double.** It has to be emphasised in particular that this mandate restriction should also apply to **Group internal supervisory board functions.** However, restricting the mandates would not only **increase the frequency of meetings attended** but certainly also mean **more time** and associated with this **more quality** for the Group-internal supervisory bodies.

Gender diversity

The share of women employees in credit institutions is comparatively high; now the share of women in managerial positions has to increase. The AK already demanded in the Green Paper on "Corporate Governance" the immediate preparation of an EU Regulation, which requires a **uniform gender quota of 40 %** with regard to filling non-executive directorships **by 2015 at the latest.** To accompany the process, the implementation of **specific measures to promote women;** apart from that an international database consisting of candidates for supervisory board and administrative board functions might be useful.

Apart from that, the AK demands the transparent, informative and comprehensive publication of the **diversity strategy** adopted by credit institutions. Mandatory diversity reports within the business reports would be one way to achieve this. In this report, institutions should clearly explain concrete measures they have taken to achieve more diversity in their employment structure, in particular in the management bodies of the European industry. The publication of measures concerning the promotion of diversity is necessary to achieve a balance with regard to age, gender and internationality.

Implementation of precise regulatory standards by EBA

In many cases, the Directive is lacking necessary concrete details. An example is the recommended *"time commitment of a member of the management body to perform his functions"* as well as *"Competent authorities shall require institutions to take into account diversity as one of the criteria for the selection of the management body".* EBA has been requested to submit respective drafts by the **end of 2015.** However, the provisions already have to be implemented on 1.1.2013; hence quick solutions are required as otherwise the implementation could be as vague and little concrete as the related content of the Directive.

Evaluation of the functioning of the supervisory board (administrative board)

The actual effectiveness of the work of the supervisory board can only be ensured by carrying out **regular efficiency reviews** (external assessment and self-evaluation) and a report covering the findings presented in the general meeting.

External evaluation (biannually)

The AK considers an external evaluation to be necessary and proposes to carry out such an evaluation every two years: this concerns in particular - based on an objective and impartial point of view - the working out of measures to increase efficiency and the development of improvement potentials for the committee work. Practice shows that a particular need for action exits to improve communication and to develop a constructive meeting and discussion culture. To view the system 'supervisory board' with the eyes of competent third parties looking in from the outside benefits the professionalism of the work - only then blind spots can be uncovered, which remain hidden to the internal view.

Self-evaluation (annually)

Apart from the external assessment of the functioning of the supervisory board, it would be advisable that the supervisory board carries out a self-evaluation **on an annual basis.** Thereby, special consideration has to be given to the procedures of the supervisory board, the flow of information between the committees and the plenum as well as the timely and in terms of content sufficient supply of information to the supervisory board. The interaction between **external and self-evaluation** is a central element for professionalising the functioning of the supervisory board; apart from that it makes a significant contribution to increase the **efficiency of information, interaction and time.**

Continued development of company law instead of extending voluntary codices

With regard to the efforts to strengthen the governance regulations the approach adopted concerning their **implementation** is of significant importance: so far, similar provisions were above all implemented in form of voluntary codices, which are interpreted differently from Member State to Member State. These regulations are based on the principle of voluntariness and the self-commitment of companies. However, as demonstrated by evaluations and studies carried out across Europe, these often fail to have the desired effect. What is needed, are appropriate standards and sanctions to achieve success. The AK therefore demands the urgent specification of requirements for the implementation in form of concrete provisions and the departure from the idea of voluntary codices.

Risk committes

The present Directive commits institutions to establish risk committees and risk management functions, both of which shall be fully independent. In the event that the nature, scale and complexity of a credit institution's activities would not justify it, the competent authority may authorise an institution not to establish such a committee. There is also no need to establish a separate risk management function if nature, scale and complexity a credit institution's activities would not justify it whereby in this case no separate authorisation by the competent authority is required. Risk management and risk control are central aspects of the governance of credit institutions, which should be a fixed central element of all institution, so that these exemptions should not be considered.

AK position:

- Due to the high relevance of risk mangement in credit institutions, the **possibility of opting out** of the requirement to establish the risk committee and the risk management function **by way of exception should not be enshrined in the text of the Directive.** Instead, it has to be ensured that each credit institution has an adequate risk management in place, which would render the committee and the management function necessary.

Capital buffers and capital conservation measures (Article 122-132)

Capital conservation buffers and countercyclical capital buffers (Article 122-124)

In addition to the mandatory own funds requirements provided for in the Regulation, the Directive requests a capital conservation buffer at a level of 2.5 % (Article 123) of their total risk exposure amount as well as an institution specific countercyclical capital buffer between 0 % and 2.5 % of the total risk exposure.

Due to the fact that valuation models, external ratings and risk models are normally not in a position to depict systemic risk, and because models on the one hand depend on assumptions and on historical time series on the other, which can only provide a rather incomplete picture of reality, a capital conservation buffer dedicated to cover these risks, is regarded as a sensible solution.

Countercyclical capital buffers (Article 125-130)

The relevant authorities of the Member States must set the rate for the countercyclical capital buffers based on the credit/GDP rate, the expansion of credit (compared to other Member States) and the recommendations of the ESRB in 0.25 %-steps. In certain cases it is also possible to set a rate of more than 2.5 % that are to be recognised by other Member States. In general, 12 months have to pass from declaration to applicability. In addition, the authorities have to - non-binding - to declare a period in which this rate is expected not to rise.

The institution-specific factor is calculated on basis of the rates of the Member States and the weighted average of the regional receivable diversity of the respective institution. Institutions may not pay any dividends associated with the core capital, which would have the effect that the combined capital buffer could no longer be achieved so that this - always dependent on the economic situation - would form a variable lower limit that is not allowed to fall below.

At the same time, institutions, which do not achieve the combined capital buffer, are on the one hand subject to a qualitatively more comprehensive restriction (apart from the ban on paying dividends, they are not permitted to pay variable remunerations or discretionary pension benefits or payments from additional core capital instruments), which, however, is quantitatively less restricted on the other, as a maximum payout ratio is calculated for this institution. This maximum payout ratio is calculated on the basis of interim and year-end profits, which do not result from the core capital, as well as a rate that depends on the level of compliance with the capital buffer. Whilst the limit of the capital buffer is absolute for institutions that already comply with it, institutions that cannot comply with the buffer can make limited payouts.

In view of the general pro-cyclicality of credit institutions' activities, which is reinforced by assessment provisions and risk models and also by external ratings, the AK expressly welcomes countercyclical capital buffers as a contribution to contain pro-cyclicality. Although this does not completely solve the basic problem, the countercyclical capital buffers seem to be a feasible compromise to depict the risk in a timely manner and as close to the market as possible, and to prevent excessive fluctuations at the same time. The concrete implementation and enforcement against short-term interests, which will not always be easy for the competent authorities, will strongly depend on how easy to understand the rules are, how much knowledge can flow in based on regional circumstances, and how well the rules and the setting of the applicable limits are enshrined in the European framework. Hence, it makes sense to entrust the competent authorities with setting the concrete requirements for the buffers on the one hand, and to furnish these authorities with methods for the calculation of the buffers, which have been formulated at European level on the other, and also to provide the ESRB with options to make recommendations for competent authorities.

The variables laid down in Article 126 (2), i.e. credit growth and the credit-to-GDP ratio appear to be the correct key variables as they also fulfil the criterion of being easy to understand. Taking the credit-to-GDP ratio into account also ensures that not only credit growth itself, but also the economic level can be taken into consideration as well as the fact that an economic "oversupply" of credit might already exist. With regard to the concrete calculation it would make sense to include credit equivalents of derivative instruments to get a better idea of the actual risk and to prevent evasive reactions.

This results in the fact that the regulation proposed in Article 126 (3) c) makes sense, but that other variables can also be applied, which so far have not been covered by the Directive; however, this should take place within the European framework - in agreement with EBA and after consultations with ESRB. Such a variable could be the ratio of credit granted to deposits.

Article 128 authorizes the ESRB to issue a recommendation to the designated authorities on the appropriate countercyclical buffer rate for exposures to that third country where a) a countercyclical buffer rate has not been set and published by the relevant third country authority for the third country or where b) the ESRB considers that a countercyclical buffer rate which has been set and published by the third country authority for a third country is not sufficient to protect Union institutions appropriately from the risks of excessive credit growth in that country.

From the point of view of the BAK, a designated authority that receives such a recommendation should be obliged to substantiate and to publish its decision in respect of the ratio in a third country, if it deviates from the ESRB's recommendation.

Capital conservation measures (Article 131-132)

In accordance with Article 131, credit institutions are subject to distribution restrictions (distributions and variable remunerations) if they fail to meet the combined buffer requirement, if in accordance with paragraph (1) the distribution would result in the fact that the buffer requirement is undercut. Paragraphs 3-4 regulate the distribution restrictions for credit institutions, which have already undercut by them, divided into quartiles of the level of achievement. This regulation is insofar worth supporting as it gives the principle of capital conservation priority over dividend pays and variable remuneration elements. However, the regulation should be supplemented in such a way that in particular the variable remuneration elements should be differentiated in accordance with their influence on the risk; if a factor exits that is different from zero, it should not be possible to combine the measures arbitrarily but a clear hierarchy should be specified: first, dividends and then the variable remuneration elements for those employees, who have a decisive influence on the overall risk of the institution, should be restricted. That because, these variable payments are also closer linked to relevant incentives for the risk management.

The AK therefore suggest the following:

- The variable "credit growth" referred to in Article 126 (2) also should include credit equivalents, which result from derivative positions on the one hand to cover the full risk and to prevent evasive reactions on the other.

- The option provided for in Article 126 (3) c to also use other variables than those referred to in Article 126 (2) should be implemented in agreement with EBA and after consultation with the ESRB.

- The authorisation of the ESRB referred to in Article 128 to issue recommendations to the designated authorities on the appropriate countercyclical buffer rate in third countries should be strengthened by the requirement that a designated authority issuing such a recommendation should be obliged to substantiate and to publish its decision in respect of the rate in a third country, if it deviates from the ESRB's recommendation.

- Article 131 requires distribution restrictions for institutions that fail to meet the combined buffer requirement or would reduce it because of the distribution. This is to be welcomed in accordance with the principle of capital conservation; however, the distribution restriction for variable remunerations should not be linear, but depend on the influence of the overall risk of the institution.

Proposal for a Regulation (COM(2011) 452 final)

Liquidity Coverage Ratio und Stable Funding (Article 400 - 415 CRR)

It is undisputed that apart from risk transformation maturity transformation is one of the essential functions of credit institutions. Nevertheless, the overreliance on constantly available (interbank market) liquidity was one of the main causes that a liquidity crisis based on the dried up and still suboptimal functioning interbank market became a crisis which almost resulted in some institutions becoming insolvent. Together with the originate-to-distribute model, which significantly fuelled the spreading and the deepening of the crisis, the extremely short-term refinancing (on the interbank market) was at the centre of the banking crisis.

As the introduction to the Regulation states correctly, effective and more efficient liquidity standards contribute to the stability of the financial market, and one can therefore assume that the macroeconomic benefit exceeds the amount of microeconomic costs of a more adequate level of liquid assets and the prudential restrictions of maturity transformation.

Having said that, the efforts of reforming and implementing liquidity standards should above all concentrate on reducing the excessive overreliance on the liquidity of the money market by way of regulation, whilst in particular the liquidity, which is based on stable deposits (subject to a deposit guarantee scheme) has to be regarded as relatively more stable.

From the point of view of the AK, it is definitely sensible and possible to implement the calibration and thereby the LCR and the NSFR more swiftly than proposed, as the data should be available by the end of 2012.

Article 409 (outflows on retail deposits)

The separate and preferential treatment of deposits, which are subject to a deposit guarantee scheme, is justified insofar as it is the actual function of deposit guarantee schemes to keep deposits stable by the guarantee. During the crisis, those business models proofed to be more resilient, which were mainly based on taking deposits and granting loans.

Art 409 Z 5 lit b: with regard to deposits with a notice period of more than 30 days, the level of the penalty, which effects that tied deposits are not regarded as overnight deposits, should under no circumstances be higher than permitted by consumer protection provisions. It should be appropriate and in accordance with the provisions of applicable consumer protection law. In order not to solely base a provision on the penalty, empiric evidence and any stress scenarios should also be included as a criterion in order to assess whether tied deposits may be regarded as such or whether they have to be considered overnight deposits.

Leverage Ratio

As the assessment of risk weighted assets is one of the factors that has greatly exacerbated the pro-cyclicality of credit institutions' activities and led to excessive leverage ratios, the implementation of a leverage ratio without risk weighting is an essential component in restoring a solid banking system from the point of view of the AK. In our opinion, regarding the calibration of the leverage ratio one should in particular ensure the adequate coverage of risks deriving from derivatives, in order to depict the actual risk and to prevent evasive reactions, which would thwart the purpose of the standard.

Should you have any further questions
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