EACB Comments

An organic approach to proportionality

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The **European Association of Co-operative Banks** (EACB) is the voice of the co-operative banks in Europe. It represents, promotes and defends the common interests of its 31 member institutions and of co-operative banks in general. Co-operative banks form decentralised networks which are subject to banking as well as co-operative legislation. Democracy, transparency and proximity are the three key characteristics of the co-operative banks' business model. With 4.200 locally operating banks and 68.000 outlets co-operative banks are widely represented throughout the enlarged European Union, playing a major role in the financial and economic system. They have a long tradition in serving 205 million customers, mainly consumers, retailers and communities. The co-operative banks in Europe represent 78 million members and 860.000 employees and have a total average market share of about 20%.

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PROPORTIONALITY AND THE RETAIL FOCUS OF THE COOPERATIVE/MUTUAL BUSINESS MODEL

In a context of increased regulatory complexity, in which assessing the full scale of interactions among regulatory products, supervisory actions and global initiatives to reduce risk and harmonise as much as possible the prudential environment, the appropriate and concrete application of the principle of proportionality needs constant focus.

A regulatory framework that takes the diversity of the European banking landscape sufficiently into account also promotes competition, innovation and productivity. It also supports the provision of a wider range of banking products for customers, helping to preserve the diversity, and thus the stability, of the financial system.

The dimensions of proportionality always need to be kept present: i.e. suitability of measures (the ability to address the risk), subsidiarity and necessity (meaning a lack of a viable alternative instrument), proportionality *strictu sensu* (meaning that the benefits should outweigh the costs). In this sense, proportionality is not a matter of size of balance sheet of a bank but of scale nature and complexity of the bank's activities and is thus applicable to large banks and has a wider business model perspective. Recital 46 CRR clearly indicates that requirements should be applied in "*a manner proportionate to the nature, scale and complexity of the risks associated with an institution's business model and activities.*" This is further underlined for instance in Art. 77 and 95 CRD IV with reference to credit risk assessment and remuneration committees respectively, mentioning "*nature, scale and complexity of their activities*".

In fact proportionality should also be applied with respect to the specificities of business models, e.g. not-for-profit/long term and retail oriented business and funding profile, core activities, risk appetite, shareholding structure, ties with local economies etc. The latter is in particular relevant for cooperative institutions, which are *entities with particular operating principles that are different from those of other economic agents*, as recalled by Recital 7 of the Statute of European cooperative society.

Cooperative banks are often characterised by less complexity in terms of: flat internal structure, limited number of employees and a basket of simple and relatively low risk banking products offered to retail and SME customers. In fact, the cooperative banks' business model is characterised by an orientation towards non-volatile and less risky activities, a focus on retail customers (loans to private households, SMEs and corporates; residential real estate) and stable funding sources (primarily deposits), a commitment to their members, strong territorial ties and a dedicated support to the growth of local economies.

These particularities are valid for cooperative banks of all sizes and need to be catered for also in the context of regulatory requirements, for instance with respect to capital, liquidity management, group structures, governance arrangements etc. The proportionality principle should embrace diversity, so ensure that certain businesses are not unduly disadvantaged, especially in the case of retail focused institutions engaging in real economy financing. It is not just that "one size fits all" can be too restrictive or far from optimal, but also "one approach fits all". This is a call for a recognition of the value of diversity of corporate forms.

The specific characteristics of cooperative banks should be taken into account when designing regulation. When dealing with cooperative banks and mutual institutions in the EU this could mean dealing with a wide variety of institutions, from central bodies of cooperative groups/networks to regional/middle sized cooperative banks, to local institutions and even facing institutions with balance sheet total below € 20mn.

Many of cooperative institutions are members of cooperative solidarity mechanisms of various sort (networks, institutional protection schemes - IPSs, consolidated groups) in various Member States. Even when part of a group or an IPS each local or regional bank usually maintains its legal autonomy and as such has to cope with many financial and reporting requirements on its own.

Cooperative banks thus have tools to address stability issues (e.g. mutual guarantees or institutional protection schemes). While this is already recognised in various elements of the legislative framework, further attention could be provided for instance in level 2 legislation. A good example in this sense comes from the attention posed on the analysis of the business model in the context of the SREP.

PROPORTIONALITY – THE ISSUES

For non-complex institutions costs are disproportionally higher against their earnings and regulatory topics are now taking up a substantial amount of time for the Management Board. Numerous Members of EACB report that especially managing directors of very small banks must dedicate more than half of their working hours to regulatory issues. Aggregated cost of compliance and keeping up with the speed of new prudential regulation (e.g. higher capital requirements, bail-in, recovery and resolution obligations) are extremely challenging.

In Europe, the transposition of the Basel international standards (e.g. CRD I-III and the CRD IV/CRR package) has always made reference to all banks (as well as investment firms), while the U.S. adopted a different approach with reference to community banks. However, the total cost of compliance due to an highly complex prudential regulation puts small banks at competitive disadvantages.

Thus, we see that regulation is driving towards "new large banks" as small institutions could be "too small to survive", i.e. to deal, comply and implement the mounting layers of the regulatory framework. A further push for mergers can be expected, while it should be highlighted that the size of cooperative banks is appropriate to their business environment and their territoriality is substantial for the diversity of local economy.

As an evident example of application of proportionality we can mention the area of reporting requirements. Reporting needs are mounting. Small and medium sized, local banks, regardless of their work in local niche and limited staff have still overwhelming reporting requirements, often not adequate to the scale of their operations and the risk entailed.

This poses a clear level playing-field question with respect, for instance, to lenders operating under different prudential regimes putting cooperative banks and building societies at a disadvantage compared to FinTechs and potential new comers.

For instance, also a disproportionate approach to leverage ratio or input/output floors on internal models in IRB-banks could have very adverse impacts on the industry at large, and even more on specialised business models focused on low-risk and high volume business. It could encourage a shift towards riskier and more expensive mortgage lending as well as to jeopardise the existence of some long-standing business models without any obvious benefits in terms of stability or resilience.

Another example can be seen in the context of cooperative banks showing on average higher level of liquidity both in terms of short term and long term funding, due to the nature of their business and structures. This could translate, for instance in no need to draw complex ILAAP planning.

At the same time, we are aware that proportionality should not mean reduced requirements for small institutions. We believe that there is room to elaborate simpler but adequate metrics and calculation methodologies for small/medium sized banks while maintaining the same level of prudence required by regulators and supervisors as for larger institutions. We suggest the regulatory requirements should be proportional to the size and systemic risk footprint of banks of differing dimension, complexity and business model, rather than a reduction of capital or liquidity requirements simply due to the size of the institutions.

What smaller and less complex institutions need is a reduction of the operational and implementation burden of regulatory requirements. It is the appropriate time to consider how to achieve a more proportionate and fit-for-purpose prudential framework, able to offer an equivalent level of protection.

IMPLEMENTING PROPORTIONALITY

When implementing proportionality we understand that more precise scope for application would be of help. The principle is laid down in Article 5 of the TFEU. However, when it comes to new directives, regulations and especially to technical standards, reporting, guidelines by EBA, ESMA a lack of substantial and explicit definitions included included in the level one text creates "grey zones".

Also, being a regionally or locally significant bank cannot be an exit criteria not to apply proportionality disregarding the actual nature and complexity of the institution.

We witness an increasing number of regulations, standards and guidelines: the initial objective to avoid a financial crisis in connection to the "too big to fail" problem may slip away.

We see that also communication should be enhanced among the different regulatory bodies as this could help institution to structure the data in a more appropriate way. This might lead to a reduction of the number of reports to be produced since the same elements could be used by more bodies.

Examples of dimensions of application of proportionality could be:

- Complexity of required calculations: more or less complex methodologies;
- Timeframes for implementation of regulatory products: e.g. transitional periods could be envisaged, sufficient time allocated etc;
- Frequency of revision of regulations: new regulations also require investments for implementation and running of new systems. If frequency is too high, investments become massive and at the margin less and less productive;
- Detail/Size of documentation;
- Reporting standards.

The optimum trade-off between simplicity/complexity and risk sensitivity occurs at very different points along the spectrum between large "Basel banks" and smaller/less complex institutions or specialised lenders. For instance, a large bank not yet applying IRB modelling would still have massive staff resources to devote to a more complex standardised framework that a small cooperative bank/building society does not have.

Level playing field is a term of reference for fair competition in a harmonized single integrated market, and we believe that implementing proportionality should preserve diversity without altering fair competition between all financial actors.

In order to achieve the right balance between the objectives pursued by legislation and the means that are being to be deployed, regulations and technical standards should entail the possibility to apply different level of sophistication, on the line of what was done for instance with Basel II (with the choice between standardised approach and internal models).

This would avoid grey zones of interpretation and discussions about the proportionality principle, while at the same time allowing that regulation and supervision do not aim to impose a one-size-fits-all approach. It should be avoided that level playing field is on the contrary used as an argument to curtail the suitability of the application of the proportionality principle, thus reducing the spirit of the Art. 5 of the Treaty on European Union.

Practical approaches to a more organic view of proportionality could envisage material definition of specific proportionate differentiation levels (e.g. at least € 5bn total assets, non-complex business model, no capital market orientation), and put forward simplicity premia where less complex methodologies and calculations can be exchanged with higher requirements in terms of capital buffers.

Proportionality could also be concretely applied in the design of corporate governance rules (e.g. remuneration rules, fit & proper, committees and) and disclosure (simplification of Pillar 3 requirements), simplification of accounting rules (e.g. allowing n-GAAPs), sensible calibration and harmonisation of MREL/TLAC, reduction of information and documentation requirements to the essentials, and simplification of processes and structures for the purpose of capital and liquidity planning (ICAAP, ILAAP).

Finally, it should be avoided that the implementation of proportionality can be restricted on the basis of diverging national interpretations. Such interpretations can lead to significant market distortions. In particular in a context where, as pointed out by Ms. Nouy in her ordinary hearing as chair of the ECB's Board of the SSM (13.6.16), the aim is to ensure the application of high supervisory standards and a level playing field through SSM, cooperating closely with the national competent authorities so that the options and discretions policy is extended, as appropriate and where possible to less significant institutions.

PROPOSALS FOR ACTION

Reporting System

We see a clear need to address the current costly and complex capital market and supervisory reporting streams and, similarly, the proposal made by the ECB to collect statistical and supervisory data on the basis of transaction-level data ("micro-data"). The reporting requirements put enormous pressure on costs and profitability when they are not proportionate to the business models, to the different sizes and to the complexity of firms supervised.

Not only are the requirements disproportionate, some of the data is collected (and has to be generated) only for regulatory reasons while having no use for business purposes. However, any reduced reporting requirements would have to result in a meaningful reduction in administrative burden: if an institution still has to collate and reconcile its data to ensure it is below a certain reporting threshold, they would still have to do a similar amount of work as if they were completing the full reporting submission.

Before the introduction of Basel III, the "Guidelines on Common Reporting" (COREP) provided for reduced reporting obligations for credit risk for institutions with a balance sheet total below EUR 250 m. This, or a similarly lighter, regime could be introduced for non-complex institutions: e.g. annual COREP report submitted within three months of the year end, and FINREP voluntary for domestic institutions.

In this respect the approach taken with regard to the Additional Liquidity Monitoring Metrics (ALMM) is a good example of reduced reporting requirements for small/medium sized institutions.

In this context, we also see the need for an urgent clarification of the concrete application of proportionality with respect to the implementation of the Anacredit project launched by ECB. In its Regulation from 18th May 2016, the ECB includes certain elements of proportionality to be implemented at discretion of NCAs (which are responsible for the data collection).

We believe that it is fundamental for the industry at large that the introduction of new reporting requirements is always preceded by an ex ante review on the existence of similar obligations and availability of information, for instance at the level of NCAs.

Accounting (Art. 24(2) CRR)

According to Recital 19 and 39 of the SSM regulation, institutions should not be obliged to apply for supervisory purposes other accounting frameworks (e.g. IAS/IFRS) than those, which are applicable according to EU and national law.

Thus, institutions which are currently preparing their annual accounts in accordance with national GAAPs should not be obliged to draw up their balance sheet or to evaluate assets and liabilities according to IFRS. This general rule based on the principle of proportionality could be explicitly included in the CRR.

In this respect, the ECB has determined not to exercise the option set out in Art. 24(2) CRR which allows competent authorities to require credit institutions to require, for prudential purposes, the valuation of assets and off-balance sheet items and the determination of own funds in accordance with IFRS also in cases where the national applicable accounting framework requires the use of n-GAAP[1]).

We appreciate the stance taken by the supervisor.

LCR

The approach to categorise the relative volatility of retail savings under the LCR delegated act is massively over-complicated.

Instead of the five buckets, institutions could have the possibility to choose a much simpler two bucket system for more, or less, “sticky” retail deposits. This would be close to the Type A/Type B categorisation used for instance in the UK from 2009 until the LCR implementation.

We also see inconsistencies in definitions for LCR reports and the ALMM that contribute to increase complexity and operational burden. In Articles 415 et seq. CRR, and in particular in EBA ITS with regard to the LCR, there are no caps on liquidity inflows, whereas the LCR Delegated Act envisages caps (with certain exclusions). In addition, private deposits are treated differently depending on whether banks follow the requirements of the previously valid European EBA Guideline that match the ITS or whether banks follows the LCR Delegated Act.

The competent authorities should use reports on ALMM as part of their supervisory review process, and these reports should also serve as early-warning instruments for ongoing supervision. Given the outlined contradictions, there might arise identification and interpretation issues in this respect.

Finally, we think the EBA proposal for daily calculations of the LCR is unduly excessive, adds unnecessary complexity to the current regulation and does not provide any added value. Monthly calculations would be sufficient and adequate, for all institutions (and thus particularly for small/medium sized banks or banks with a sound liquidity profile). We object the assumption by which the fact that LCR needs to be met at any time justifies an LCR disclosure based on averaged values over daily observations. We think this not only unnecessary from a liquidity perspective in normal situations, but also in sharp contrast

[1] See *ECB*, Draft Addendum to the ECB Guide on Options and National Discretions available in Union Law (May 2016), 4.

with the proportionality principle laid down in the article 414 of the CRR as mentioned by article 4 of the LCR delegated act (…*Until compliance has been restored, the institution shall report the items referred to in Title II or Title III, as appropriate, daily by the end of each business day unless the competent authority authorises a lower reporting frequency and a longer reporting delay. Competent authorities shall only grant such authorisations based on the individual situation of an institution and taking into account the scale and complexity of the institution's activities*. (Art. 414 CRR)).

Credit protection

Eligible providers of unfunded credit protection (Art 201 et seqq. CRR)

Guarantees represent additional safety for institutions and minimize the likelihood of a final loss by proper coverage of the residual risk. Their effect on RWA should be explicitly recognised. For instance, particularly with regard to SME financing, guarantees play an essential role in the form of personal collateral. Guarantees should be acknowledged as risk reducing collateral in the CRR.

We see also an overall need to simplify the methodology by which recognition of CRM in the form of mortgage insurance is granted – e.g. via more of a substitution, rather than a securitisation approach – even if the CRM benefit is somewhat less generous than the complex securitisation route appears to offer. This could be another example of the "simplicity premium".

Pillar 2 and ICAAPs

The ICAAP requirement is over-elaborate. For a small, simple institution the added value of performing a full ICAAP in parallel with carrying out the detailed Pillar 1 calculations, is pretty limited. The buffers now build in a substantial element of conservatism, so the radical proposal would be to disapply Article 73 in revised CRD for an identified category of institutions.

Disclosure (e.g. Art. 431 et seqq. CRR)

Pillar 3 disclosures, and the market discipline they bring, are mainly designed for listed, shareholder-driven institutions. For small local or medium sized regional domestic cooperative institutions, the information is largely irrelevant.

Pillar 3 requires disproportionate amount of time and resources for smaller institutions and their customers.

The radical solution would be for the defined population of smaller institutions to disapply the entirety of the current and proposed Pillar 3 requirements, and instead require only the annual publication of the following set of simple regulatory information: CET 1 ratio, total capital ratio, LCR, encumbrance level, and one single figure for loan loss provisions.

According to Art. 432(1) CRR, "institutions may omit one or more disclosures if the information provided by such disclosures is not regarded as material", except for certain disclosures required by Art. 435, 437 and 450 CRR.

The existing disclosure requirements are far too detailed and lead to high implementation costs, which are disproportionate to the benefits of the disclosed data.

Art. 433 CRR could foresee allowing non-complex institutions to disclose their governance arrangements every five years instead of annually (Art. 435(2) CRR.

Funding plan requirement for non-capital-market-oriented banks

According to Article 413 CRR in connection with EBA Guidelines on harmonised definitions and templates for funding plans of credit institutions, banks are obliged to provide extensive information and data on funding activities and plans for subsequent years on an annual basis. The responsible supervisory authorities are required to compile funding plans that cover at least 75% of a banking system's total consolidated assets.

Due to the implementation of the 75% requirement, there are included also institutions whose funding is anyway guaranteed at all times. This holds true particularly for cooperative through their membership in an IPS, a consolidated group or a liquidity network, which makes them independent from capital market's funding. This fact is not taken into sufficient consideration by the EBA Guidelines. In addition, there is no harmonisation between FINREP reporting and the obligations to present funding plans, what creates uncertainties and additional complexity for all institutions, and results in an inconsistent database. The extended reporting requirements of funding plans do not offer any additional benefit.

While an overall consistency check is needed, small and medium-sized institutions or less relevant group entities with no systemic relevance could be exempted from the planned additional reporting requirements.

Only the information required for the FINREP reports for each bank category (e.g. data points) should be submitted. It should not be the case that institutions are forced to become full FINREP adopters due to the funding plan report.

Fit & Proper requirements

According to Art. 23(1)(b) in conjunction with Art. 91(1) CRD IV executive directors and non-executive directors of boards/members of supervisory boards must have sufficient knowledge, skills and experience for the proper discharge of their functions. Which kind of knowledge is considered as "appropriate", will - based on the principle of proportionality - depend on nature, size and complexity of the business as well as, to a certain extent, on the legal form of the institution.

We could highlight for instance the specific election process of executive directors and non-executive directors of the board/members of supervisory board in certain cooperative banks. The future board members are proposed by the local or regional cooperative banks and afterwards there is a formal vote at the general members' (shareholders') meeting, to appoint the members of the different cooperative structures to the relevant board (i.e. board of directors or supervisory board). In light of this, the point of collective knowledge as provided for by Art. 91(7) CRD IV should be well reflected. This should also be considered as a key element to ensure the diversity of the board, as provided by Art. 91(10).

These aspects will become even more important if, for instance, also the local boards have to fulfil the fit and proper conditions.

In this context, there is a material difference between the challenges for executive directors and non executive directors of the board/members of the supervisory board operating in a big institution or banking group with international activities and for those responsible for a regional bank with exclusively domestic operations. Knowledge and experience required from executive directors or non-executive directors of the board/members of the supervisory board of regionally operating institutions differs from those responsible for globally active and systemically relevant institution.

To ensure that executive directors and non-executive directors of the board/members of the supervisory board can dedicate sufficient time to their controlling functions within the institution, Art. 91(2)-(5) CRD IV limits the number of mandates in significant institutions. This term ("significant") should allow a differentiated approach. Given the diversified legal and structural frameworks in the various EU Members States, the local regulators may successfully adapt EU rules on fit and proper only if they are given certain discretion by way of sustaining the principle of proportionality. Particularly in view of any future review of the EBA Fit & Proper Guidelines, it is recommended to leave it to the members states to set certain thresholds for a binding waiver in the context of Art. 23 and 91 CRD IV.

<u>Requirements to establish and option to integrate committees</u>

Art. 88(2) CRD IV requires institutions significant in terms of their size, internal organisation and the nature, scope and complexity of their activities to establish a nomination committee. In Austria, such a nomination committee is mandatory for institutions with a balance sheet above EUR 1 bn.

The same applies to the risk committee, which is, required for institutions that are significant due to their size, internal organisation and the nature, scope and complexity of their activities (Art. 76(3) and (4) CRD IV).

Both cases are an example of how the threshold of a balance sheet of at least € 5bn could be explicitly included in CRD IV, ensuring consistent application of the committee requirements throughout the EU.

Similarly, Art. 63a para. 4 of the Austrian Banking Act requires an audit committee for institutions with a balance sheet of above EUR 1 bn. On the other hand, Art. 76(3) and (4) CRD IV allows significant institutions to merge the risk and audit committee. The ECB assumes that institutions with a balance sheet above € 5bn are significant for this purpose. Therefore and in line with the principle of proportionality, CRD IV should be adapted accordingly.

Last but not least, the threshold is relevant also for remuneration committees. We would recommend to include the threshold for a binding waiver of at least EUR 5bn total assets also in Art. 95 CRD IV.

Remuneration

Recital 66 CRD IV explicitly requires that the remuneration arrangements of CRD IV consider the differences between varying types of institutions in a proportionate manner, taking into account their size, internal organisation and the nature, scope and complexity of their activities.

The intention of the EU legislator regarding the proportional application of remuneration provisions should be explicitly included in Articles 92 and seq. CRD IV. In line with this, non-complex institutions as well as lower levels of variable remuneration should be exempted from deferral and payout of variable remuneration components in non-cash instruments as provided in article 94 CRDIV.

NSFR

We believe that proportionality is to be explicitly implemented in the NSFR framework, both in order to avoid restrictive interpretations of provisions from supervisors and to leave room for measures such as those provided in the context of the LCR (e.g. fallback treatment of retail deposits subject to higher outflows, Art. 25 Delegated Regulation 2015/61).

A simplified metric such as the core funding ratio along the lines of the measure implemented in New Zealand , could be a good starting point.

Also in the USA the Agencies (Federal Reserve System, FDIC, Treasury) are consulting on the NSFR implementation. The proposals put forward introduce a twofold differentiation. On the one hand they aim to exclude certain institutions from the scope of the NSFR .

On the other hand they suggest also a modified NSFR that is 70% of the full ratio for other institutions within the scope of the requirement but that still need a more proportionate measure. However, the latter simple adjustment may still not be sufficient for less complex EU institutions as they would still be subject to the same operational requirements (in terms of calculations and disclosure for instance).

However, the differentiated approach undertaken in the USA provides further elements to stimulate the design of rules that do not disproportionately hit the EU markets and institutions.

It also has to be taken into account that intragroup transactions as well as transactions among the member banks of a cooperative network/group would be disproportionately burdened by the NSFR. Where the liquidity flows are centralized within a banking group or cooperative network, there is a cascade effect on the liquidity needs of each single member bank. The centralized liquidity steering within a group or cooperative network might become virtually unaffordable such endangering the group/network structure as such.

Level of application: consolidated vs solo basis

To avoid detrimental impacts, the NSFR requirement should be applied only at a consolidated level (as conceived by the Basel Committee) and not also on a solo basis.

The BCBS intended the NSFR to be applied only at the consolidated level, and has calibrated the requirement taking into account a form of diversification of the banking activities. Moreover, the NSFR should work as a long-term structural ratio aiming at limiting excess maturity transformation risk in the banking sector, while the LCR represents a survival test during a liquidity crisis: this also justifies a different scope of application of these two complementary requirements.

An EU transposition of the NSFR requirement at the solo entity level would be too stringent. Consequently, it should not be considered without a thorough QIS taking into account the diversified organisations and structures of the banking groups in the European Union. Indeed, the application of the NSFR at subsidiary level of a consolidated group might result in additional stable funding requirements beyond what has been estimated in the Basel QIS.

If not applied at the consolidated level, the European transposition of the NSFR at solo level with current asymmetric ASF and RSF factors would lead to an uneven playing field to the detriment of banking groups, institutional protection schemes (IPS), and networks organizing their capital markets activities or their trade finance/factoring activities within different entities (which cannot benefit from any diversification effect) instead of one operating company.

Indeed, to minimize this detrimental impact and in order to allow the transfer of liquidity resources from an entity to another within the same Group/IPS/network, the introduction of fair and symmetric adjustments should be considered to deal with intra-group transactions as it has been done for the LCR. However, if these adjustments are necessary to avoid undue NSFR shortfall at a solo level, it should be reminded that liquidity transfers from an entity to another will be necessarily performed at market price; as a consequence, the very stringent calibrations applicable to market activities will remain a burden for the entities specialized in these activities and should be reviewed. We believe that it should be allowed to apply symmetric weight on an automatic way (without a systematic prior approval of the competent authority), based on the compliance with objective criteria such as when the transactions are dealt by entities within a group of entities qualifying for the treatment set out in Article 113(6) or (7) of Regulation (EU) No 575/2013.

Not to disadvantage European banking groups, we recommend introducing fair, automatic and symmetric ASF and RSF factors for intragroup operations (including balance-sheet and off balance-sheet operations), whereby ASF for the borrowing entity would be equal to the RSF for the providing entity.

Leverage Ratio

With regard to the leverage ratio, the preliminary findings presented by the EBA for the EU did not seem to indicate whether differentiation would be introduced. We are aware that the Commission shall assess carefully EU specificities and adopt a proportionate approach. However, the dimensions and associated quantitative indicators included in the EBA analysis do not provide a complete picture nor mechanically translate into a risk of excessive leverage.

Such indicators should only provide the starting point for further investigation especially with regard to cooperative and mutual business models. We believe that a few very selective indicators have been chosen based on experience from universal banks performance without taking into account elements such as well established measures of funding, risk management and legal frameworks. Given the limited availability of data on the level of the institution it is important not to give excessive prominence on the results of such indicators. Indeed supervisory dialogue and discretion plays an important role especially for specific business models.

Moreover, it should be given proper consideration to the specific situation of banking groups made up by local (often small) co-operative banks and their central institutions, whereby the former do not have a direct access to the Central Bank and the payment and settlement systems and capital/money markets. Thus, the central institutions perform central bank refinancing operations and other secured funding transactions on behalf of the local co-operative banks.

Furthermore, cooperative and mutual institutions are focused on serving their Members meaning that their main aim is not maximisation of short-term profit. Profit is necessary to sustain the business and better serve Members. As a result these institutions are more stable over time. In general, the key source of capital is retained profit, thus cooperative and mutual institutions very clearly take into account the gradual nature of raising new capital. This constitutes a natural brake on excessive leverage. It also necessarily involves taking a long-term approach to strategic planning and business model analysis. Wider qualitative analysis is therefore necessary.

A uniform treatment of balance sheet risks may imply that hedge fund investments is comparable with fully secured mortgage lending. This might create incentives to engage in higher risk lending practices and produce adverse effects for conservative business models, i.e. driving low risk mortgage lenders into riskier businesses with a significant cost impact for consumers. In this context the leverage ratio might reveal itself as the main binding capital driver for low-risk business models rather than a capital backstop.

Promotional loans and cooperative central institutions

Finally, we believe that the specific case of cooperative central institutions has not been recognized in this first impact study yet. Cooperative central institutions act as product and service provider in numerous functions for their network of local cooperative banks. Their very specific business structure and provision of services to local banks includes promotional loans.

LR as a Pillar 2 requirement

The LR in its present design does not act as a backstop, it rather seems a different methodology to calculate minimum own funds requirements. Against this background it seems consistent to introduce the LR as a Pillar 2 requirement, as this allows a flexible implementation.

Trading book

The Fundamental Review of the Trading Book (FRTB) introduces some new concepts to the standardised approach (e.g. use of sensitivities), which are complex and entail a challenging implementation. Building new models, implementing new frameworks and applying new concepts are burdensome and resource-consuming tasks.

In addition, the granularity of data that is required by the FRTB approach is noticeably higher than under the current approach of Art 360 CRR. Hence, apart from implementing the new methodology of calculating the own funds requirements, banks would also have to adapt and considerably expand their data basis. One Member reported that the cost for a bank would be at least € 1 million, which is a very considerable investment for an institution with small trading book activities.

Institutions without a trading book or with a small trading book are executing derivative transactions only for the hedging of their ordinary banking book business. Any models requiring high data (e.g. daily market prices) would require a very demanding implementation and high cost.

In our opinion, the market risk model for small trading books (beyond the thresholds in Art. 94 CRR) in the current CRR should be maintained (instead of the standardized approach), due to its reduced administrative burden and limited regulatory cost. As a second-best alternative, we could imagine the introduction of a standardized approach which is simpler than the one of the FRTB.

The existing thresholds are a crucial element for institutions to benefit from the small trading book derogation according to Art 94 CRR. The absolute amount may in general be considered more constraining. Against this background we believe that a readjustment of the existing thresholds is long overdue and inevitable as they have not been adapted for years. This is even more so required, since more and more products tend to be assigned to the trading book.

As a first suggestion we would recommend updating the absolute threshold to take into account at least the effect of inflation over time. As the current limits were fixed in Article 4(6) Council Directive 93/6/EEC back in 1993, we consider a yearly 2% rate up to 2016. 2% would be consistent with the inflation target of most Central Banks and also with data from Eurostat (1.7% considering the HCPI for the Euro area).

The 15mn "normal" minimum should thus be brought to 23 and the 20mn threshold to 32 million ad minima .

In addition, we propose to extend the scope of the derogations under Article 94. In order to achieve a more proportionate application of the trading book rules, the exemption of

Article 94 (1) CRR should not only have Article 92 (3) (b) CRR in scope, but rather comprise also the entire trading book rules of Articles 102 to 106 CRR. These rules pose an excessive administrative burden to institutions with small and very small trading books while delivering only marginal additional value.

Moreover, for small positions in FX and commodities that are not held for any of the purposes of para 12 of the BCBS market risk standard an additional threshold should be implemented. FX and commodity positions that do not exceed this additional threshold should be exempted from capital requirements for market risk.

A further aspect that needs to be considered for a proportionate implementation of the FRTB relates to the reallocation of instruments to the trading book. If the supervisors require such reallocations, given the expanded scope of instruments to be assigned to the trading book, such reallocation could trigger the requirement to introduce a trading book in certain institutions. However, supervisors should not assume that institutions already manage a trading book. Most small or less complex cooperative banks do not have a trading book. Adequate transitional periods should be granted to institutions, where following a request of the supervisor the establishment of a trading book would become necessary.

Exemptions from prospectus regime

Since the preparation of a prospectus leads to high costs the exemptions within the prospectus regulation should be broadened to facilitate the access to the market for smaller banks and SME's. Alternatively, simplified prospectuses should be explored further.

Implementation deadlines

Especially with regard to less significant institutions and their limited resources, there should always be a minimum implementation period for any new requirement of at least 1 year. For delegated legislation such period should only be counted after the relevant level 1 text (EU regulations or national legislation in the case of directives) has been adopted.