



FEDERATION BANCAIRE DE L'UNION EUROPEENNE

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20th MEETING OF THE ASSOCIATES
- Budapest, Hungary, 12 May 2005 -

ITEM 2 OF THE AGENDA: MINUTES OF THE PREVIOUS MEETING

With the agreement of the chairman of the previous meeting of the Associates please find enclosed the minutes of the 19th Meeting of the Associates, held on 9 December 2004 in Brussels.

In case you have any suggestions or amendments to the enclosed minutes, please let the Secretariat know in writing before the meeting.

Enclosures: 1 – Minutes of the previous meeting
2 – List of the participants (enclosure to the Minutes)



FEDERATION BANCAIRE DE L'UNION EUROPEENNE

19th MEETING OF THE ASSOCIATES

- Brussels, Belgium, 9 December 2004 -

MINUTES

ITEM 1 – OPENING AND WELCOME

Mr Zoran BOHACEK, Managing Director of the Croatian Banking Association, chaired the meeting and welcomed the participants of the meeting.

Mr. Tanguy van der WERVE, Secretary General *ad interim* of the FBE welcomed the participants of the meeting to the home of the Federation.

A list of participants is attached (enclosure 1).

ITEM 2 – MINUTES OF THE PREVIOUS MEETING

The members approved the minutes of the 18th Meeting of the Associates, which was held in Dubrovnik, Croatia, on 28 May 2004.

ITEM 3 - EU ENLARGEMENT: A BANKING PERSPECTIVE

- a) "The enlarged EU, the opportunities it provides and challenges it faces and the EIB role with regards to this process"

Mr. Thomas HACKETT, Deputy General Director at the European Investment Bank (EIB) introduced the participants of the meeting to his views on the biggest single enlargement in the EU history and the opportunities it provides and challenges it faces. He also touched upon the EIB role with regards to this process.

His speech went as follows.

Clearly, 2004 has been an important year for European Integration since the European Union has welcomed 10 new Members and may very shortly give the signal to open negotiations with Turkey and Croatia as well as conclude them with Bulgaria and Romania.

A recent article in the International Herald Tribune, described the European Investment Bank (EIB) as "the world's largest and most obscure public bank.....that has ever so discreetly managed to outspend and outborrow the better-known World Bank in Washington". That article at least acknowledged that "without the EIB and its immense resources that enabled more than EUR 42 billion in loans last year, many EU projects would not have flourished".

The EIB tries to focus on certain critical areas for Europe's future, such transport and communications, environment, support for SME's via the banking sector and research and development under the heading of i2i.

In March 2000, Europe's Leaders met in Lisbon and declared their aim to make the EU "the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion". The aim was to achieve this goal by 2010, by adopting what is called the "Lisbon Strategy" of economic and structural reform. So this strategy was to be implemented in parallel with progress to Enlargement.

Enlargement has been accomplished according to the timetable set at the Gothenburg Summit in 2001 and that is already a significant achievement. To use Romano Prodi's words in his farewell address to the European Parliament in October, "Europe's unification -- involving enlargement to embrace ten new members, a clear timetable for the other candidate countries and real prospects of full membership for all countries in the Balkans -- is the greatest contribution the Union could make to stabilising and developing the whole continent -- politically, economically and culturally."

The New Members have been faced with another formidable - and twin - challenge: the challenge of fundamental social transformation and transition to a market economy combined with the specific requirements of EU accession. None of the previous EU candidates has been presented with such a twin challenge.

Still an enormous amount remains to be done at a time when the capacity to pay for this investment is more restricted due to the low rate of EU economic growth and to the other domestic claims on resources. Just to give you some idea, the EU Commission and TINA¹ have estimated that to bring the new EU's main corridors up to an acceptable standard will cost at least EUR 90 billion while a further EUR 260 bn is needed just to catch up on the maintenance backlog in all transportation networks. Only to meet current demand and EU regulations in water supply and treatment would cost a further EUR 50 bn while wastewater and solid waste treatment urgently needs another EUR 25 bn. Against this, the annual budgetary possibilities of the New Member States are some EUR 2.5 bn and the EU Funds package up to 2006 is fixed at around EUR 24 bn, not all of which is for capital investment. From 2007 to 2013, about two thirds of the EU Structural Funds budget of EUR 336 bn are expected to go to the New Member States. Although that seems an enormous amount, it is estimated that, even on an optimistic scenario, it will be another two decades at least for the infrastructure handicap to be overcome.

The investments needed are very large. They are beyond the scope of public resources available to finance them. Where possible private resources in certain sectors can plug part of the gap. However current low tariff levels that users can afford make private investment in infrastructure unattractive for the investor or the tariff adjustment needed would be politically or socially unacceptable.

¹ The Transport Infrastructure Needs Assessment Group

Another sensitive aspect is the limited administrative capacity to implement projects. The governance and the processes to start and complete large complex projects or programmes is still a “work in progress”.

So the requirements are huge, the resources are limited and so is the implementation capacity. Faced with this difficult situation, the “old EU” can help ease the last two constraints through financing of feasibility studies and technical assistance by national administrations and agencies to accelerate and improve project implementation. This assistance can usefully complement the EC contribution and the new EU governments’ efforts to ensure that funds are used quickly and effectively.

Another related area where the old EU can support the new is in transparency. With a few exceptions, the new EU scores poorly in the Transparency International index. In the field of transparency and good governance the NMS are flanked by Nordic countries which are the world leaders in pursuing the highest transparency standards. They are therefore well-placed to help their neighbours to apply their high national standards.

In contrast to the mixed outlook for infrastructure investment, Foreign Direct Investment or FDI has done well.

The prospect of EU membership of the New Members in the region has paved the way for interest in the region resulting in substantial foreign investments in manufacturing and services. The private sector has been quick to penetrate these markets.

FDI will continue to play a crucial role in the economic growth of the NMS, though its pattern is likely gradually to resemble the “old EU” with less focus on growth in capital stock. After the initial wave of privatisation and greenfield investments, future contribution to economic growth is likely to come through the transfer of technology, know-how and best practice. This should raise productivity and lead to spill-overs into the domestic industrial sector and other surrounding economies.

The service sector has been an important field for FDI, notably in retailing and financial activities. The technical and financial support to local banks by their foreign banking shareholders is important to facilitate growth of domestic enterprises.

Technological innovations are global. The real challenge is to commercialise successfully innovations. Most likely increased co-operation across the region including universities and private companies would benefit the whole area in global competition.

The proximity and the natural links between the new EU countries and their neighbours represent a tremendous opportunity to enable the Union to meet the Decade’s Double Challenge. Put very simply for development in the new EU, EU resources are essential. For EU resources to be affordable, we need economic growth. To achieve that growth, the EU Member States need to accomplish the Lisbon Strategy, and for the Lisbon Strategy to succeed across the whole of

Europe we need the development potential of the new EU combined with the strengths of the old EU, such as exist in the Nordic countries.

One of the mechanisms to cement this partnership is co-operation with the bank system. EU-15 banks have invested heavily in acquisitions or internal organic expansion in the NMS. Yet as a share of the national economy, the NMS are still significantly “under-banked” and financial services contribute a relatively small share to GDP compared to even the less advanced EU-15.

Partly due to a risk-averse credit culture in local commercial banks and partly due to their limited local autonomy, the limited access to finance for SME’s and municipalities can be a severe handicap to the full utilisation of the financial support provided by the EU. Accordingly, the EIB (as well its affiliate, the EIF, and other IFI’s such as EBRD and CEB) have been working with the Commission to facilitate access to finance in the NMS with three instruments.

These instruments are:

- Developing a wider network of banks benefiting from global loans, m-t lines of credit to banks for on-lending to SME’s or to municipalities for small infrastructure investments.
- Incentives managed by the EIB and provided by the EC to encourage banks to invest in staff and systems to allow prudent expansion into these sectors.
- Risk-sharing and support for securitisation either on the EIF’s own balance sheet or provided through guarantees backed by the EC.

These programmes have really started in the current year so it’s early to judge results but local affiliates and independent NMS banks have shown considerable interest; the promising outlook is confirmed by the other IFI’s.

The two challenges facing the Union are substantial and the banking system has a crucial responsibility in meeting them. The instruments are present to support the banking system in this task and above all there is sustained readiness on the part of the EIB to co-operate with you to achieve your objectives, which are also ours.

- b) “The future EU enlargements and the relationships with the Wider Europe”
Address by Mr. Maurice GUYADER, Principal Administrator at DG Enlargement,
European Commission

The following points were made.

Although 10 new member states have already joined the EU in May 2004, many of them still have transitional periods in many areas and there is still much to do. As a result further progress in implementation and enforcement of the “acquis communautaire” is expected from all new Member States. A “safeguard clause” might be an additional stimulus to complete this process in due time and manner.

State of play for the remaining EU candidate countries:

Technical negotiations were completed with Bulgaria on all chapters in June 2004, but with Romania on December 2004. The competition issue was the most difficult subject for Romania, state aid in particular, but the European Commission decided to move on with this process. In principle both of those countries must join the EU on 1 January 2007, but regarding Romania there is a super-safeguard clause – in case of significant difficulties accession may take place on 1 January 2008.

Croatia applied for the EU membership in 2003. In June 2004 the European Council officially decided to accept Croatia as a candidate. Negotiations might be launched as early as at the beginning of 2005. Most probably Croatia will not join the EU together with Bulgaria and Romania; however it might join before the end of this decade.

In its December 2002 meeting the European Council set the deadline of December 2004 for the decision regarding the opening of negotiations with Turkey. The biggest problem so far has been the political criteria.

On 6 October 2004 the European Commission prepared 3 documents on Turkey – regular progress report, document on political criteria and an impact study on the accession of Turkey to the EU. In general the Commission was in favour of opening negotiations. As a result the final answer of the December 2004 European Council should be more or less positive, however, the final wording of the decision is going to be very important.

In case of a positive decision, the negotiations with Turkey may start at the end of 2005. These could be very long negotiations and the accession of Turkey to the EU might take place after the end of the next EU financial perspective (year 2013).

The former Yugoslavian Republic of Macedonia applied for EU membership in 2004. In principle all Balkan countries should be members of the EU, but the question is how it should happen and when. The situation in the region as a whole should be stabilised beforehand.

With other European countries and countries of Northern Africa the best possible neighbourhood relations and cooperation should be developed, but not in the framework of accession to the EU, at least for the foreseeable future.

Cooperation with those countries should be developed as much as possible, but for the time being without common institutions.

An action plan was proposed recently by the European Commission regarding 7 countries: Ukraine, Moldova, Morocco, Tunisia, Jordan, Israel and Palestine.

The idea of creating and developing a common economic policy and economic space between the European Union and the Russian Federation is also on the agenda.

ITEM 4 - LOBBYING IN BRUSSELS

Mr Stephen FISHER, adviser at the European Banking Federation, started with the introduction of the main EU institutions.

In everyday lobbying work the FBE focuses mainly on the three major institutions – the European Commission and the two parties very often involved in the so-called co-decision procedure - the European Parliament and the Council of the European Union. The main aim of FBE lobbying is to influence successfully the EU legislative process and get the best possible end results.

The European Commission.

This institution is the one which upholds the collective European interest. It is a politically independent body and it acts as the guardian of the Treaties.

The European Commission has the sole right of legislative initiative. There are 25 Commissioners and 36 Directorates General in the Commission. The key Directorate general for FBE lobbying work is DG Internal Market. Besides that the FBE also has active relations with DG Enterprise, DG Competition and DG Health and Consumer Protection.

The Council of the European Union.

This is the main legislative and decision making body in the EU and it represents all EU Member States. It is co-legislator (with the European Parliament) in financial services dossiers under the framework of the co-decision procedure.

The Council of the EU has a rotating presidency. In year 2004 Ireland and Netherlands were the presiding countries of the Council. In 2005 the presidency is going to be handled over to Luxembourg and later to the UK. In 2006 Austria and Finland will take over.

Voting power of the different Member States in the Council is set more or less in accordance with the size of the population of particular countries. So, the biggest EU country – Germany – has 29 votes, medium sized country like Belgium – 12 votes, while one of the smallest EU countries – Malta has only 3 votes.

The European Parliament.

This institution is the EU's primary debating chamber and it represents the citizens of the European Union. Members of Parliament (MEPs) are directly elected by the citizens of the Member States and most of them belong to one of the seven political groups.

Plenary sessions of the Parliament are held in Brussels and Strasbourg.

Parliament is also a co-legislator (with the Council) in financial services dossiers under the framework of the co-decision procedure.

This presentation was followed by Mrs. Burcak INEL, adviser at the FBE, intervention on the Lamfalussy process and FBE lobbying in financial markets.

The evolution of the Lamfalussy Process is itself a product of our own lobbying. The FBE has affected the way the Process is today and the way it is changing. It is therefore a good way to talk about how the FBE is influencing better regulation in the EU.

Nowadays, there is a whole industry of lobbyists in Brussels. According to a WSJ article (entitled "Increasingly, Rules of Global Economy Are Set in Brussels"), there are about 10,000 lobbyists in Brussels representing some 1,400 companies and nonprofit organizations from around the world. These lobbyists are working to make sure that the EU legislation in all possible sectors, in its earliest possible form, when

it just emerges as a faint idea, as an itch, in the minds of a policymaker here, emerges in the best possible way from the perspective of the members whose interests are represented. This is part of democracy, organized interest representation.

Ever since the introduction of the Euro, there has been strong momentum to unify markets – the single market, common standards, freedom to offer services throughout Europe. The goal is to make Europe a truly integrated market and reap all the competitive benefits this implies, for the economy, investors, and employees. The trick is setting the right regulatory framework that hits the right balance, merges the different traditions and market structures into a competitive, efficient, functioning whole.

This goal is achievable only if the regulatory process is transparent and democratic.

The Commission Communication of 11 May 1999 entitled “Implementing the framework for financial markets: action plan” identified a series of actions intended to create a legislative framework to support a single market for financial services. The Lisbon European Council of April 2000 called for the implementation of that action plan by 2005. The Stockholm European Council of March 2001 endorsed the final report of the Committee of Wise Men chaired by Baron Lamfalussy on the regulation of European securities markets.

The Report noted that the regulatory framework:

- was too slow;
- was too rigid and could not react speedily enough to changing market conditions. Every change, however small or technical, required a full blown Commission proposal to be negotiated by co-decision;
- produced too much ambiguity (e.g. Article 11 of the Investment Services Directive concerning conduct of business rules; public versus private offers in the 1980 Directive);
- was implemented ambiguously – partly due to the texts themselves, but also due to the lack of coordination by an effective network of European regulators;
- failed to distinguish between core, enduring, essential framework principles and practical, day to day, implementing rules.

As a solution, the Report proposed the introduction of a four-level approach for securities markets regulation:

- Framework principles (Level 1);
- Implementing measures (Level 2);
- Co-operation among regulators (Level 3); and
- Enforcement (Level 4).

During 2001, while the inter-institutional discussions were going on, the Committee of European Securities Regulators (CESR) was established and started operations. The Commission proposed two Directives (Market Abuse and Prospectus Directives) in May 2001, shortly after the publication of the final Lamfalussy Report, but long before the formalization of the Process that would allow these two Directives to become full Lamfalussy Directives.

In February 2002 the recommendations of the Lamfalussy Report were finally formalised as the new EU regulatory framework for securities legislation, at which point an agreement was finally reached among the three EU institutions. The

breakthrough came when the European Parliament endorsed the Report on the basis of the Commission's declaration regarding the safeguarding of the Parliament's role in the process.

CESR - regulators, in existence since 2001, plays a key role in the new regulatory framework in which technical details are supposed to flow organically from politically decided clear principles. They advise the Commission and also fulfill a role for regulatory/supervisory convergence.

ESC - government officials, they advise the Commission when implementing technical rules.

We have now three important pieces of financial markets legislation that are employing the Lamfalussy Process (Market Abuse Directive, Prospectus Directive and MiFID). No single piece of legislation has gone through the full cycle (all four levels) of the framework. However, we have come as far as "Level 3" of the Process in the Prospectus Directive.

Moreover, the decision was taken to extend the Lamfalussy Process to banking supervision, insurance, occupational pensions and collective investment schemes (UCITS). The European Commission published three decisions on 5 November 2003 establishing the three committees that will be involved in the implementation of the Lamfalussy process in banking and supervision.

Under the new structure, the industry has the chance to influence the outcome at each of the four levels:

- **Pre-legislative** – consultation here very important, this is a standard procedure we have lobbied for and won. Cost-benefit analysis necessary but not yet fully applied. It will be, for C&S.
- **Legislative** – influencing the Parliament and Council, as well as the Commission Here, what is different is that the legislation that is discussed has to be focused on the principles, not the detail. So far, this has proven difficult, but there are at least fewer loopholes now than before.
- **Implementation** – requires the technical implementing measures, prepared by the Commission on the basis of advice from the regulators, and adopted by the ESC.
- **Enforcement** - According to the most recent statistics, around 8.5% of all Internal Market legislation (about 131 measures) are not implemented correctly. This is not only about whether EU legislation is transposed, but whether the rules put in place are correctly applied.

Challenges: some are endemic, some are due to FSAP.

- FSAP Timetables
- Structured consultation – timing; need for good and precise arguments; no privileged access
- Parliament's role - limited to primary legislation and monitoring of technical rules
- Council and ESC: requires great amount of coordination between the contacts among our members and their governments – though arguably we are best placed to do this.

Opportunities: some are not yet tested.

- Transparency – overall endorsement by all institutions, though with varied outcomes. Everyone knows who else is arguing what. Usefulness of targeted coordination and coalitions.
- Separation of principle from detail makes it easier to focus on the merits of the rules
- Leaving technical details to Level 2 also means flexible rules: easier to adapt – though this is not yet tested
- Use of experts: FBE's network
- Consistent application – not yet tested.

ITEM 5 - LATEST DEVELOPMENTS IN THE EU FINANCIAL SERVICES AREA

Mr Elmars KRONBERGS, adviser at the European Banking Federation, started with the presentation of an eighth report on the latest developments in the EU legislation concerning the financial sector.

Altogether 10 pieces of legislation are included in the presentation.

He outlined four recently adopted legislative actions - Regulation endorsing the IAS 39 on Financial Instruments, Recommendation on Directors' remuneration, Recommendation on role of independent Directors and the action plan - strategy to prevent financial and corporate malpractice.

Mr. Kronbergs continued his report on the European Commission's proposals covering the Directive to simplify the formation, maintenance and alteration of public Limited Liability Companies' capital, the four key revisions to the EU's Accounting Directives, New Capital Requirements Framework for banks and investment firms and the update of the Anti-Money Laundering Directive (or 3rd Anti-Money Laundering Directive).

Among the most important European Commission consultations, highlighted in the presentation, were those regarding basic shareholders' rights and the call to CESR for technical advice on possible measures concerning credit rating agencies.

This presentation was followed by an intervention by Mrs. Caitriona O'KELLY, adviser at the FBE, on the latest developments in the BASEL II and Capital Adequacy Directive (CAD3).

The main points were as follows.

It is essential for the benefits of the legislation to be realised as quickly and as prudently as possible. Industry has already prepared itself for the new framework, including significant expenditure on improvement of risk management systems to deliver a safer, more risk-sensitive, banking system.

It is also very important to ensure that the European process is in line with the implementation of the new Basel framework on a global basis, and in particular in the US. A high level of parallelism has been achieved between the CAD3 and the new Basel framework whilst taking account of European specificities. This

parallelism is necessary if European banks are to enjoy a level playing field with their competitors in other jurisdictions, in particular, in the US.

The wider scope of the Directive in the EU is in the interests of both Europe's consumers and its industry at large. A well-managed and well-capitalised banking system will deliver greater stability in the banking sector, providing a sound platform for businesses to expand and innovate. In general, a disparity in the US between banks applying Basel I and those applying the new Basel framework is neither in the interests of industry nor consumers and it does not enhance prudential supervision.

A level playing field across the EU is crucial but the current level of inconsistency in interpretation of the rules will have a material impact on the capital of banks. Industry welcomes the willingness in CEBS to work towards supervisory convergence. Inconsistent implementation within the EU goes beyond the national discretions in the proposal for a Directive.

The three top concerns of European commercial banks are the role of the consolidating supervisor, the level of application of the rules and the risk weighting of intra-group exposures.

Although the consolidating supervisor model is welcomed, there is a strong feeling in the industry that this model does not go far enough in delivering a practical supervisory framework. European banks organise risk management on a centralised group basis. This reality is not reflected in the proposal for a Directive.

The proposal currently requires credit institutions to apply own funds requirements at the level of each entity within the group. It then allows Member States to waive this requirement within the home Member State if the group meets the conditions on the allocation of capital. As a result there is a massive competitive distortion between those banking groups domiciled in Member States whose competent authorities do not choose to apply the waiver and those groups in Member States whose competent authorities do apply the waiver.

Furthermore the proposals are restricted to within single Member States and do not allow banks to apply the rules at the top level within the EU. Again, this is not consistent with Single Market objectives. This limitation will lead to a competitive distortion between, on the one hand, internationally active groups with subsidiaries in host member states and, on the other hand, domestic banks. Internationally active banks would be subject to materially different treatment on the level of application in different jurisdictions.

To summarise the key points in brief, the consolidating supervisor model, combined with the role of CEBS in supervisory convergence, is a step in the right direction. However, the role of the consolidating supervisor should be extended to Pillar 2. The waiver in Article 69 should be applied as a rule at the top level in the EU once the conditions are met and intra-group exposures should be risk-weighted at 0%. On the Trading Book Review we believe that work stream 3 on illiquid assets requires more time.

Delivering a level playing field within the EU would send a positive message to the rest of the world that consistency in application is of paramount importance. If the

objectives of the Lisbon Agenda are to be achieved the EU must be at the forefront in implementing global standards such as the new Basel framework.

ITEM 6 - SUPERVISORY COORDINATION IN THE EU

At the meeting this subject was presented by Mr. Freddy VAN DEN SPIEGEL, Chief Economist at Fortis Bank.

Although there are signs of convergence in thinking in the EU regarding the supervision problem in the financial industry, a unified position has not been reached yet.

The main goal of supervision, to a certain extent also the political goal, is to maintain confidence in the financial system. Supervision is triangle of entities:

- 1) Basel II – prudential supervision;
- 2) Lender of last resort – tool to solve liquidity problems;
- 3) Insurance – deposit insurance.

The most important question is how to organize all these three entities into one, as efficient as possible, system. Inefficiencies often show up as overlaps in the system, but holes are creating dangerous ineffectiveness. Fast reactivity would be essential for supervisors in order to be able to respond properly and in due time to economic realities. In theory it is easy and the key word here is to maintain the solvency of the system.

Eventually a supervisor should prevent bankruptcies. The lender of last resort should help banks in liquidity problems, but not in solvency problems. In reality all three factors are linked: a solvency problem may become liquidity problem and vice versa.

In reality there are huge conflicts of interest between different supervisory authorities (National banks, deposit insurance schemes, etc.). If those authorities are located in different countries, problems multiply. One has to react immediately, on the spot once an incident happens. In the EU there are 52 independent supervisory authorities at the moment. Some of them act as advisers, some negotiate, some even buy up problematic banks... there are many different independent supervisory authorities with different mandates. How can these different authorities solve a cross-border problem in a fast and efficient way once it arises?

In Basel II the home and host country concept has been offered, but those two concepts are very often in collision... The lender of the last resort is always a host country. However, the liquidity problem normally arises within a financial group, often a pan-European entity. In the areas of deposit protection and prudential supervision there is also the question of host and home country. Besides, there is always a question – tax payers of which country (host or home) will pay the bill in case of problems!?

What would be the solution to this, for the time being fortunately only theoretical, problem - the colleague of supervisors with leading one on top; a European FSA?

It is clear that the EU needs a global framework of architecture for modern and efficient financial supervision, but the real discussion regarding the possible solutions has not really started yet...

ITEM 7 - STATE OF INTEGRATION OF EUROPE'S FINANCIAL MARKETS

Mr Tanguy van de WERVE, head of FBE Banking Supervision department presented the conclusions and findings of the FBE report on the state of integration of Europe's financial markets, as follows.

The Financial Services Action Plan (FSAP) has been a success in so far as the 2003/2005 deadlines have broadly been met so far.

The extent to which the FSAP will contribute to the creation of a truly European market for financial services will mainly depend on three factors:

- the correct and timely implementation of the FSAP measures at Member State level;
- convergence of national supervisory practices;
- proper enforcement.

The level 3 Committees need to develop an EU-centric view of policy and promote cooperation between Member States. Industry has to play an active role in identifying and reporting infringements. The FBE supports the Lamfalussy model and also its extension to banking.

Carefully targeted legislation is needed in retail banking where removal of well-identified obstacles would help to open up national markets. The FBE considers the full harmonisation of key retail banking elements as the most effective means of creating a true European internal market for retail banking services.

Other priorities would include the removal of artificial obstacles to further consolidation in the European banking industry, a coherent VAT treatment of financial services, the creation of a market-driven Single Euro Payments Area, a more efficient cross-border clearing and settlement process and the implementation of the Basel II accord.

Policy making should be evidence based. If there is a perceived need for action, options other than regulation should also be considered. Industry consultation must be a feature of all stages of the legislative process.

The creation of a European Single Market for financial services is not an end but rather a means to increase the international competitiveness of the EU. Systematic assessment of the business impact of EU legislation should be carried out.

Given the unprecedented globalization of financial services, there is a need for a strong and united EU voice in the international arena and for a structured dialogue with the main EU partners.

ITEM 8 - IAS

The progress report on the latest developments in the IAS field, and in IAS 39 in particular, was introduced by Mr. Wilfried WILMS, adviser at the FBE, as follows.

The European Banking Federation industry has been critical of IAS 39 from inception. Our concerns about IAS 39 and, in particular, the inappropriateness of its hedging rules can be traced back to 1999 when the International Accounting Standards Committee (IASC) adopted IAS 39.

During the subsequent years, the International Accounting Standards Board (IASB) – which is the successor of the IASC – took several initiatives aiming at improving IAS 39. However, no significant amendments were made to areas which were key to the European banking industry.

The IASB published the standard on fair value hedge accounting for a portfolio of Interest Rate Risk. The outcome was, however, disappointing mainly because:

- the hedge accounting rules did not enable banks to hedge exposure to changes in interest rates that arise from the behavioural maturity of “core deposits” (i.e. sight and savings deposits);
- the standard put many restrictions on the use of such hedges which made the standard cumbersome to apply in practice and resulted in accounting rules which were not in line with banks’ risk management practices.

As a result, the FBE is currently seeking support from the IASB for its “Interest Margin Hedge” proposal, i.e. a hedging model that focuses on interest margin and in doing so provides a basis more compatible with the way in which banks seek to manage risk. It would, moreover, allow core deposits to be included in the hedged portfolio.

In the meantime, the European Central Bank had severely criticised IAS 39 because it allowed entities to designate any financial asset or financial liability as one to be measured at fair value (“fair value option”).

As a result of the opposition the European Commission endorsed IAS 39 only partially in November 2004. It refused, more particularly, to support its provisions:

- on the use of the fair value option and
- on hedge accounting.

The two ‘carve outs’ are temporary because the Commission expects the IASB to bring forward the necessary amendments to the current full fair value option by December 2004 and to the provisions on hedge accounting by September 2005.

ITEM 9 - MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE

This subject was presented by Mrs. Burcak INEL, adviser at the FBE.

The new Proposal was aimed at closing the loopholes for mutual recognition and establishing a common investor protection regime, above all by establishing a common regime for conduct of business rules for investment firms. This would bring

about more competition, lower costs for the customer, a better range of services across Europe, and higher global competitiveness.

This would increase competition between different trading venues which provide different services to clients with different needs at lower prices.

A short history of the Directive:

- Formal proposal for a Directive submitted to the Parliament and Council: November 2002
- First Reading at the Parliament: March 2003
- Council Common Position: December 2003
- Adoption of the Second Reading at the Parliament: July 2004
- Level 2 work started in January 2004 and is expected to continue until June 2005
- Formal adoption of the Directive: April 2004
- Entry into force of the Directive: May 2006

Key issues for the FBE:

- Ensuring overall an evidence-based approach to legislation
- Establishing a good precedent for the first Lamfalussy Directive
- Making sure that the passport regime is effective, with no loopholes
- Preventing overly prescriptive investor protection rules
- Ensuring a level playing field for cross-border services and providing legal certainty and lower regulatory costs for firms active cross-border
- Allowing the continuation of a range of different services provided to clients, including investment advice and non-advisory services, at globally competitive prices
- Supporting the abolition of the concentration rule
- Striking a balance between the need to introduce legally clear rules for best execution obligation and the need to allow firms sufficient flexibility
- Calibrating the pre- and post-trade transparency rules for intermediaries to demonstrated benefit for the market and clients
- Supporting appropriate grandfathering arrangements and transitional provisions

Key FBE Actions:

- Written responses and oral presentations at all of the consultations conducted by the Commission
- Bilateral meetings with the Commission
- Presentation at the Parliament Expert Panel: February 2003
- Contact with Parliamentarians and Permanent Representations

Next steps: 1st mandate:

Compliance, information and reporting to clients, safeguarding of assets, best execution, pre-trade and post-trade transparency for regulated markets (RMs) and multilateral trading facilities (MTFs), post-trade transparency for intermediaries. Deadline for CESR to deliver to the Commission the advice on most subjects in this mandate: end-January 2005. However, given the need to ensure overall coherence between the different rules designed to ensure a high degree of competition and efficiency in European markets and in particular between the transparency and best execution provisions of the Directive, certain issues are subject to an extended

deadline: Articles 21 (best execution), 28 (post-trade transparency disclosure by investment firms), 29 (pre-trade transparency requirements for MTFs), 30 (post-trade transparency requirements for MTFs), 44 (pre-trade transparency requirements for Regulated Markets) and 45 (post-trade transparency requirements for Regulated Markets) are due at the end of April 2005 (same as the 2nd mandate subjects).

2nd mandate:

Pre-trade transparency for intermediaries (Article 27), investment advice and non-advisory services (Article 19). Deadline for CESR to deliver its advice to the Commission: end-April 2005.

ITEM 10 - EUROPEAN PAYMENTS COUNCIL

Mr Patrick PONCELET, head of FBE payments department reported on the latest developments in the EPC field and in particular on the realisation of the Single Euro Payments area, a roadmap for 2004-2010.

This roadmap has been developed for the EPC Plenary and its communities to provide a description of the way forward for delivery of the Single Euro Payments Area (SEPA) programme.

It provides a refined definition and scope for SEPA, building on the original 2002 vision, and presents the key deliverables and priorities for EPC in the period ahead. A timeline is provided, supported by clear objectives for the six areas of focus represented by the current EPC Working and Support Groups, four responsible for payment instruments and two for supporting the areas of standards and law.

The final section reviews the role of stakeholders in adopting and implementing the SEPA and the pan-European payment instruments that will be delivered. This Roadmap is a 'living' document and will evolve. It will also form the basis for other communication presentations and more detailed descriptions tailored for specific audiences, including a text version.

The main objectives of the roadmap document, to:

- reaffirm the vision set out in the 2002 White Paper '*Euroland, our Single Payment Area*' and in the EPC Charter,
- clarify the SEPA definition and focus,
- establish EPC's priorities and the deliverables that will be required for the realization of SEPA,
- put in place an industry action plan and timetable with milestones for the defined deliverables,
- reinforce cooperation between banks and banking communities in relation to the adoption and implementation of SEPA payment instruments,
- mobilize other players and stakeholders to achieve buy-in and commitment to SEPA objectives,
- provide a toolkit for communication.

Real SEPA will be achieved when people can make payments throughout the whole euro area from one bank account or by using one card as easily and safely as a national payment is made today.

By 2008 the industry has to deliver “SEPA for the citizen” with cross-border and national use of pan-European Instruments such as Credeuro [The interbank convention which promotes the adoption of an efficient, low cost, end to end scheme for basic cross border STP (Straight Through Processing) Credit Transfers in euro by using IBAN]; Prieuro (a priority payment scheme), Direct Debit and Card Solutions. End-to-End Solutions for initiation and reconciliation also will have to be standardized and deployed.

By 2010 transformation of infrastructures will have to be fully underway either by conversion of national infrastructures into pan-European infrastructures (no parallel domestic & cross-border systems) or their elimination. Several PE-ACH (Pan-European Automated Clearing House framework) operators would gradually absorb payment volumes across Europe.

During the discussion phase of the item the question was raised by the chairman of the meeting, representing also Croatia, on the expected actions from the EU candidates with regards to the activities of the EPC. In answering this question Mr. Poncelet indicated that once new countries join the EU, they will have automatically a seat in the EPC. However, even before that, it would be wise for countries moving towards membership in the EU to start following more closely the EPC’s work and recommendations. The formalisation of the circulation of EPC information to the Banking Associations of the EU candidate countries might be worth considering.

ITEM 11 - ANY OTHER BUSINESS

Nothing was raised under this item during the meeting.

ITEM 12 - PREPARATION OF THE NEXT MEETING

It was decided and announced that the next “Brussels” meeting of the Associates will be held in Brussels on Thursday, 8 December 2005, a day before the FBE Executive Committee meeting.

The FBE Executive Committee members will be invited to participate in the meeting.

There is still a possibility to hold an “outside” meeting of the FBE Associates with the participation of the FBE Executive Committee members in late spring or early summer 2005. However, this will depend on the availability of the potential host of the meeting.

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Enclosure: 1



FEDERATION BANCAIRE DE L'UNION EUROPEENNE

19th MEETING OF THE ASSOCIATES

- Brussels, Belgium, 9 December 2004

LIST OF PARTICIPANTS

<u>Chairman:</u>	Mr	Zoran BOHACEK
<u>FBE Secretariat:</u>	Mr	Tanguy VAN DE WERVE
	Mr	Elmars KRONBERGS
Associates:		
<u>Albania</u>	Mr	Paul LIND
<u>Bulgaria</u>	Mrs	Eleonora HRISTOFOROVA IVANOVA
<u>Croatia</u>	Mr	Zoran BOHACEK
<u>Latvia</u>	Mr	-
<u>Lithuania</u>	Mr	-
<u>Romania</u>	Mr	Radu NEGREA
<u>Russia</u>	Mr	Oleg PREKSIN
<u>Turkey</u>	Mr	Ekrem KESKIN
Executive Committee:		
<u>Cyprus</u>	Mr	Georgios Hadji ANASTASSIOU
<u>Czech Republic</u>	Mr	Petr SPACEK
<u>Estonia</u>	Mrs	Katrin TALIHARM
<u>Germany</u>	Mr	Bernd BRABANDER
<u>Italy</u>	Mr	Enrico GRANATA
<u>Netherlands</u>	Mr	Hein G. M. BLOCKS
<u>Norway</u>	Mr	Arne SKAUGE
<u>Poland</u>	Mr	Pawel PNIEWSKI
<u>Slovenia</u>	Mr	Dusan HOCEVAR

Guest speakers:

Deputy General Director at the European Investment Bank:	Mr	Thomas HACKETT
Principal Administrator, DG Enlargement, European Commission:	Mr	Maurice GUYADER
Chief Economist, Fortis Bank:	Mr	Freddy VAN DEN SPIEGEL
Head of payments department, FBE	Mr	Patrick PONCELET
Adviser, FBE	Mrs	Burcak INEL
Adviser, FBE	Mrs	Caitriona O'KELLY
Adviser, FBE	Mr	Stephen FISHER
Adviser, FBE	Mr	Wilfried WILMS

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FEDERATION BANCAIRE DE L'UNION EUROPEENNE

19th MEETING OF THE ASSOCIATES

- Brussels, Belgium, 9 December 2004 -

MINUTES

ITEM 1 – OPENING AND WELCOME

Mr Zoran BOHACEK, Managing Director of the Croatian Banking Association, chaired the meeting and welcomed the participants of the meeting.

Mr. Tanguy van der WERVE, Secretary General *ad interim* of the FBE welcomed the participants of the meeting to the home of the Federation.

A list of participants is attached (enclosure 1).

ITEM 2 – MINUTES OF THE PREVIOUS MEETING

The members approved the minutes of the 18th Meeting of the Associates, which was held in Dubrovnik, Croatia, on 28 May 2004.

ITEM 3 - EU ENLARGEMENT: A BANKING PERSPECTIVE

- a) "The enlarged EU, the opportunities it provides and challenges it faces and the EIB role with regards to this process"

Mr. Thomas HACKETT, Deputy General Director at the European Investment Bank (EIB) introduced the participants of the meeting to his views on the biggest single enlargement in the EU history and the opportunities it provides and challenges it faces. He also touched upon the EIB role with regards to this process.

His speech went as follows.

Clearly, 2004 has been an important year for European Integration since the European Union has welcomed 10 new Members and may very shortly give the signal to open negotiations with Turkey and Croatia as well as conclude them with Bulgaria and Romania.

A recent article in the International Herald Tribune, described the European Investment Bank (EIB) as "the world's largest and most obscure public bank.....that has ever so discreetly managed to outspend and outborrow the better-known World Bank in Washington". That article at least acknowledged that "without the EIB and its immense resources that enabled more than EUR 42 billion in loans last year, many EU projects would not have flourished".

The EIB tries to focus on certain critical areas for Europe's future, such transport and communications, environment, support for SME's via the banking sector and research and development under the heading of i2i.

In March 2000, Europe's Leaders met in Lisbon and declared their aim to make the EU "the most competitive and dynamic knowledge-based economy in the world, capable of sustainable economic growth with more and better jobs and greater social cohesion". The aim was to achieve this goal by 2010, by adopting what is called the "Lisbon Strategy" of economic and structural reform. So this strategy was to be implemented in parallel with progress to Enlargement.

Enlargement has been accomplished according to the timetable set at the Gothenburg Summit in 2001 and that is already a significant achievement. To use Romano Prodi's words in his farewell address to the European Parliament in October, "Europe's unification -- involving enlargement to embrace ten new members, a clear timetable for the other candidate countries and real prospects of full membership for all countries in the Balkans -- is the greatest contribution the Union could make to stabilising and developing the whole continent -- politically, economically and culturally."

The New Members have been faced with another formidable - and twin - challenge: the challenge of fundamental social transformation and transition to a market economy combined with the specific requirements of EU accession. None of the previous EU candidates has been presented with such a twin challenge.

Still an enormous amount remains to be done at a time when the capacity to pay for this investment is more restricted due to the low rate of EU economic growth and to the other domestic claims on resources. Just to give you some idea, the EU Commission and TINA¹ have estimated that to bring the new EU's main corridors up to an acceptable standard will cost at least EUR 90 billion while a further EUR 260 bn is needed just to catch up on the maintenance backlog in all transportation networks. Only to meet current demand and EU regulations in water supply and treatment would cost a further EUR 50 bn while wastewater and solid waste treatment urgently needs another EUR 25 bn. Against this, the annual budgetary possibilities of the New Member States are some EUR 2.5 bn and the EU Funds package up to 2006 is fixed at around EUR 24 bn, not all of which is for capital investment. From 2007 to 2013, about two thirds of the EU Structural Funds budget of EUR 336 bn are expected to go to the New Member States. Although that seems an enormous amount, it is estimated that, even on an optimistic scenario, it will be another two decades at least for the infrastructure handicap to be overcome.

The investments needed are very large. They are beyond the scope of public resources available to finance them. Where possible private resources in certain sectors can plug part of the gap. However current low tariff levels that users can afford make private investment in infrastructure unattractive for the investor or the tariff adjustment needed would be politically or socially unacceptable.

¹ The Transport Infrastructure Needs Assessment Group

Another sensitive aspect is the limited administrative capacity to implement projects. The governance and the processes to start and complete large complex projects or programmes is still a “work in progress”.

So the requirements are huge, the resources are limited and so is the implementation capacity. Faced with this difficult situation, the “old EU” can help ease the last two constraints through financing of feasibility studies and technical assistance by national administrations and agencies to accelerate and improve project implementation. This assistance can usefully complement the EC contribution and the new EU governments’ efforts to ensure that funds are used quickly and effectively.

Another related area where the old EU can support the new is in transparency. With a few exceptions, the new EU scores poorly in the Transparency International index. In the field of transparency and good governance the NMS are flanked by Nordic countries which are the world leaders in pursuing the highest transparency standards. They are therefore well-placed to help their neighbours to apply their high national standards.

In contrast to the mixed outlook for infrastructure investment, Foreign Direct Investment or FDI has done well.

The prospect of EU membership of the New Members in the region has paved the way for interest in the region resulting in substantial foreign investments in manufacturing and services. The private sector has been quick to penetrate these markets.

FDI will continue to play a crucial role in the economic growth of the NMS, though its pattern is likely gradually to resemble the “old EU” with less focus on growth in capital stock. After the initial wave of privatisation and greenfield investments, future contribution to economic growth is likely to come through the transfer of technology, know-how and best practice. This should raise productivity and lead to spill-overs into the domestic industrial sector and other surrounding economies.

The service sector has been an important field for FDI, notably in retailing and financial activities. The technical and financial support to local banks by their foreign banking shareholders is important to facilitate growth of domestic enterprises.

Technological innovations are global. The real challenge is to commercialise successfully innovations. Most likely increased co-operation across the region including universities and private companies would benefit the whole area in global competition.

The proximity and the natural links between the new EU countries and their neighbours represent a tremendous opportunity to enable the Union to meet the Decade’s Double Challenge. Put very simply for development in the new EU, EU resources are essential. For EU resources to be affordable, we need economic growth. To achieve that growth, the EU Member States need to accomplish the Lisbon Strategy, and for the Lisbon Strategy to succeed across the whole of

Europe we need the development potential of the new EU combined with the strengths of the old EU, such as exist in the Nordic countries.

One of the mechanisms to cement this partnership is co-operation with the bank system. EU-15 banks have invested heavily in acquisitions or internal organic expansion in the NMS. Yet as a share of the national economy, the NMS are still significantly “under-banked” and financial services contribute a relatively small share to GDP compared to even the less advanced EU-15.

Partly due to a risk-averse credit culture in local commercial banks and partly due to their limited local autonomy, the limited access to finance for SME’s and municipalities can be a severe handicap to the full utilisation of the financial support provided by the EU. Accordingly, the EIB (as well its affiliate, the EIF, and other IFI’s such as EBRD and CEB) have been working with the Commission to facilitate access to finance in the NMS with three instruments.

These instruments are:

- Developing a wider network of banks benefiting from global loans, m-t lines of credit to banks for on-lending to SME’s or to municipalities for small infrastructure investments.
- Incentives managed by the EIB and provided by the EC to encourage banks to invest in staff and systems to allow prudent expansion into these sectors.
- Risk-sharing and support for securitisation either on the EIF’s own balance sheet or provided through guarantees backed by the EC.

These programmes have really started in the current year so it’s early to judge results but local affiliates and independent NMS banks have shown considerable interest; the promising outlook is confirmed by the other IFI’s.

The two challenges facing the Union are substantial and the banking system has a crucial responsibility in meeting them. The instruments are present to support the banking system in this task and above all there is sustained readiness on the part of the EIB to co-operate with you to achieve your objectives, which are also ours.

- b) “The future EU enlargements and the relationships with the Wider Europe”
Address by Mr. Maurice GUYADER, Principal Administrator at DG Enlargement,
European Commission

The following points were made.

Although 10 new member states have already joined the EU in May 2004, many of them still have transitional periods in many areas and there is still much to do. As a result further progress in implementation and enforcement of the “acquis communautaire” is expected from all new Member States. A “safeguard clause” might be an additional stimulus to complete this process in due time and manner.

State of play for the remaining EU candidate countries:

Technical negotiations were completed with Bulgaria on all chapters in June 2004, but with Romania on December 2004. The competition issue was the most difficult subject for Romania, state aid in particular, but the European Commission decided to move on with this process. In principle both of those countries must join the EU on 1 January 2007, but regarding Romania there is a super-safeguard clause – in case of significant difficulties accession may take place on 1 January 2008.

Croatia applied for the EU membership in 2003. In June 2004 the European Council officially decided to accept Croatia as a candidate. Negotiations might be launched as early as at the beginning of 2005. Most probably Croatia will not join the EU together with Bulgaria and Romania; however it might join before the end of this decade.

In its December 2002 meeting the European Council set the deadline of December 2004 for the decision regarding the opening of negotiations with Turkey. The biggest problem so far has been the political criteria.

On 6 October 2004 the European Commission prepared 3 documents on Turkey – regular progress report, document on political criteria and an impact study on the accession of Turkey to the EU. In general the Commission was in favour of opening negotiations. As a result the final answer of the December 2004 European Council should be more or less positive, however, the final wording of the decision is going to be very important.

In case of a positive decision, the negotiations with Turkey may start at the end of 2005. These could be very long negotiations and the accession of Turkey to the EU might take place after the end of the next EU financial perspective (year 2013).

The former Yugoslavian Republic of Macedonia applied for EU membership in 2004. In principle all Balkan countries should be members of the EU, but the question is how it should happen and when. The situation in the region as a whole should be stabilised beforehand.

With other European countries and countries of Northern Africa the best possible neighbourhood relations and cooperation should be developed, but not in the framework of accession to the EU, at least for the foreseeable future.

Cooperation with those countries should be developed as much as possible, but for the time being without common institutions.

An action plan was proposed recently by the European Commission regarding 7 countries: Ukraine, Moldova, Morocco, Tunisia, Jordan, Israel and Palestine.

The idea of creating and developing a common economic policy and economic space between the European Union and the Russian Federation is also on the agenda.

ITEM 4 - LOBBYING IN BRUSSELS

Mr Stephen FISHER, adviser at the European Banking Federation, started with the introduction of the main EU institutions.

In everyday lobbying work the FBE focuses mainly on the three major institutions – the European Commission and the two parties very often involved in the so-called co-decision procedure - the European Parliament and the Council of the European Union. The main aim of FBE lobbying is to influence successfully the EU legislative process and get the best possible end results.

The European Commission.

This institution is the one which upholds the collective European interest. It is a politically independent body and it acts as the guardian of the Treaties.

The European Commission has the sole right of legislative initiative. There are 25 Commissioners and 36 Directorates General in the Commission. The key Directorate general for FBE lobbying work is DG Internal Market. Besides that the FBE also has active relations with DG Enterprise, DG Competition and DG Health and Consumer Protection.

The Council of the European Union.

This is the main legislative and decision making body in the EU and it represents all EU Member States. It is co-legislator (with the European Parliament) in financial services dossiers under the framework of the co-decision procedure.

The Council of the EU has a rotating presidency. In year 2004 Ireland and Netherlands were the presiding countries of the Council. In 2005 the presidency is going to be handled over to Luxembourg and later to the UK. In 2006 Austria and Finland will take over.

Voting power of the different Member States in the Council is set more or less in accordance with the size of the population of particular countries. So, the biggest EU country – Germany – has 29 votes, medium sized country like Belgium – 12 votes, while one of the smallest EU countries – Malta has only 3 votes.

The European Parliament.

This institution is the EU's primary debating chamber and it represents the citizens of the European Union. Members of Parliament (MEPs) are directly elected by the citizens of the Member States and most of them belong to one of the seven political groups.

Plenary sessions of the Parliament are held in Brussels and Strasbourg.

Parliament is also a co-legislator (with the Council) in financial services dossiers under the framework of the co-decision procedure.

This presentation was followed by Mrs. Burcak INEL, adviser at the FBE, intervention on the Lamfalussy process and FBE lobbying in financial markets.

The evolution of the Lamfalussy Process is itself a product of our own lobbying. The FBE has affected the way the Process is today and the way it is changing. It is therefore a good way to talk about how the FBE is influencing better regulation in the EU.

Nowadays, there is a whole industry of lobbyists in Brussels. According to a WSJ article (entitled "Increasingly, Rules of Global Economy Are Set in Brussels"), there are about 10,000 lobbyists in Brussels representing some 1,400 companies and nonprofit organizations from around the world. These lobbyists are working to make sure that the EU legislation in all possible sectors, in its earliest possible form, when

it just emerges as a faint idea, as an itch, in the minds of a policymaker here, emerges in the best possible way from the perspective of the members whose interests are represented. This is part of democracy, organized interest representation.

Ever since the introduction of the Euro, there has been strong momentum to unify markets – the single market, common standards, freedom to offer services throughout Europe. The goal is to make Europe a truly integrated market and reap all the competitive benefits this implies, for the economy, investors, and employees. The trick is setting the right regulatory framework that hits the right balance, merges the different traditions and market structures into a competitive, efficient, functioning whole.

This goal is achievable only if the regulatory process is transparent and democratic.

The Commission Communication of 11 May 1999 entitled “Implementing the framework for financial markets: action plan” identified a series of actions intended to create a legislative framework to support a single market for financial services. The Lisbon European Council of April 2000 called for the implementation of that action plan by 2005. The Stockholm European Council of March 2001 endorsed the final report of the Committee of Wise Men chaired by Baron Lamfalussy on the regulation of European securities markets.

The Report noted that the regulatory framework:

- was too slow;
- was too rigid and could not react speedily enough to changing market conditions. Every change, however small or technical, required a full blown Commission proposal to be negotiated by co-decision;
- produced too much ambiguity (e.g. Article 11 of the Investment Services Directive concerning conduct of business rules; public versus private offers in the 1980 Directive);
- was implemented ambiguously – partly due to the texts themselves, but also due to the lack of coordination by an effective network of European regulators;
- failed to distinguish between core, enduring, essential framework principles and practical, day to day, implementing rules.

As a solution, the Report proposed the introduction of a four-level approach for securities markets regulation:

- Framework principles (Level 1);
- Implementing measures (Level 2);
- Co-operation among regulators (Level 3); and
- Enforcement (Level 4).

During 2001, while the inter-institutional discussions were going on, the Committee of European Securities Regulators (CESR) was established and started operations. The Commission proposed two Directives (Market Abuse and Prospectus Directives) in May 2001, shortly after the publication of the final Lamfalussy Report, but long before the formalization of the Process that would allow these two Directives to become full Lamfalussy Directives.

In February 2002 the recommendations of the Lamfalussy Report were finally formalised as the new EU regulatory framework for securities legislation, at which point an agreement was finally reached among the three EU institutions. The

breakthrough came when the European Parliament endorsed the Report on the basis of the Commission's declaration regarding the safeguarding of the Parliament's role in the process.

CESR - regulators, in existence since 2001, plays a key role in the new regulatory framework in which technical details are supposed to flow organically from politically decided clear principles. They advise the Commission and also fulfill a role for regulatory/supervisory convergence.

ESC - government officials, they advise the Commission when implementing technical rules.

We have now three important pieces of financial markets legislation that are employing the Lamfalussy Process (Market Abuse Directive, Prospectus Directive and MiFID). No single piece of legislation has gone through the full cycle (all four levels) of the framework. However, we have come as far as "Level 3" of the Process in the Prospectus Directive.

Moreover, the decision was taken to extend the Lamfalussy Process to banking supervision, insurance, occupational pensions and collective investment schemes (UCITS). The European Commission published three decisions on 5 November 2003 establishing the three committees that will be involved in the implementation of the Lamfalussy process in banking and supervision.

Under the new structure, the industry has the chance to influence the outcome at each of the four levels:

- **Pre-legislative** – consultation here very important, this is a standard procedure we have lobbied for and won. Cost-benefit analysis necessary but not yet fully applied. It will be, for C&S.
- **Legislative** – influencing the Parliament and Council, as well as the Commission Here, what is different is that the legislation that is discussed has to be focused on the principles, not the detail. So far, this has proven difficult, but there are at least fewer loopholes now than before.
- **Implementation** – requires the technical implementing measures, prepared by the Commission on the basis of advice from the regulators, and adopted by the ESC.
- **Enforcement** - According to the most recent statistics, around 8.5% of all Internal Market legislation (about 131 measures) are not implemented correctly. This is not only about whether EU legislation is transposed, but whether the rules put in place are correctly applied.

Challenges: some are endemic, some are due to FSAP.

- FSAP Timetables
- Structured consultation – timing; need for good and precise arguments; no privileged access
- Parliament's role - limited to primary legislation and monitoring of technical rules
- Council and ESC: requires great amount of coordination between the contacts among our members and their governments – though arguably we are best placed to do this.

Opportunities: some are not yet tested.

- Transparency – overall endorsement by all institutions, though with varied outcomes. Everyone knows who else is arguing what. Usefulness of targeted coordination and coalitions.
- Separation of principle from detail makes it easier to focus on the merits of the rules
- Leaving technical details to Level 2 also means flexible rules: easier to adapt – though this is not yet tested
- Use of experts: FBE's network
- Consistent application – not yet tested.

ITEM 5 - LATEST DEVELOPMENTS IN THE EU FINANCIAL SERVICES AREA

Mr Elmars KRONBERGS, adviser at the European Banking Federation, started with the presentation of an eighth report on the latest developments in the EU legislation concerning the financial sector.

Altogether 10 pieces of legislation are included in the presentation.

He outlined four recently adopted legislative actions - Regulation endorsing the IAS 39 on Financial Instruments, Recommendation on Directors' remuneration, Recommendation on role of independent Directors and the action plan - strategy to prevent financial and corporate malpractice.

Mr. Kronbergs continued his report on the European Commission's proposals covering the Directive to simplify the formation, maintenance and alteration of public Limited Liability Companies' capital, the four key revisions to the EU's Accounting Directives, New Capital Requirements Framework for banks and investment firms and the update of the Anti-Money Laundering Directive (or 3rd Anti-Money Laundering Directive).

Among the most important European Commission consultations, highlighted in the presentation, were those regarding basic shareholders' rights and the call to CESR for technical advice on possible measures concerning credit rating agencies.

This presentation was followed by an intervention by Mrs. Caitriona O'KELLY, adviser at the FBE, on the latest developments in the BASEL II and Capital Adequacy Directive (CAD3).

The main points were as follows.

It is essential for the benefits of the legislation to be realised as quickly and as prudently as possible. Industry has already prepared itself for the new framework, including significant expenditure on improvement of risk management systems to deliver a safer, more risk-sensitive, banking system.

It is also very important to ensure that the European process is in line with the implementation of the new Basel framework on a global basis, and in particular in the US. A high level of parallelism has been achieved between the CAD3 and the new Basel framework whilst taking account of European specificities. This

parallelism is necessary if European banks are to enjoy a level playing field with their competitors in other jurisdictions, in particular, in the US.

The wider scope of the Directive in the EU is in the interests of both Europe's consumers and its industry at large. A well-managed and well-capitalised banking system will deliver greater stability in the banking sector, providing a sound platform for businesses to expand and innovate. In general, a disparity in the US between banks applying Basel I and those applying the new Basel framework is neither in the interests of industry nor consumers and it does not enhance prudential supervision.

A level playing field across the EU is crucial but the current level of inconsistency in interpretation of the rules will have a material impact on the capital of banks. Industry welcomes the willingness in CEBS to work towards supervisory convergence. Inconsistent implementation within the EU goes beyond the national discretions in the proposal for a Directive.

The three top concerns of European commercial banks are the role of the consolidating supervisor, the level of application of the rules and the risk weighting of intra-group exposures.

Although the consolidating supervisor model is welcomed, there is a strong feeling in the industry that this model does not go far enough in delivering a practical supervisory framework. European banks organise risk management on a centralised group basis. This reality is not reflected in the proposal for a Directive.

The proposal currently requires credit institutions to apply own funds requirements at the level of each entity within the group. It then allows Member States to waive this requirement within the home Member State if the group meets the conditions on the allocation of capital. As a result there is a massive competitive distortion between those banking groups domiciled in Member States whose competent authorities do not choose to apply the waiver and those groups in Member States whose competent authorities do apply the waiver.

Furthermore the proposals are restricted to within single Member States and do not allow banks to apply the rules at the top level within the EU. Again, this is not consistent with Single Market objectives. This limitation will lead to a competitive distortion between, on the one hand, internationally active groups with subsidiaries in host member states and, on the other hand, domestic banks. Internationally active banks would be subject to materially different treatment on the level of application in different jurisdictions.

To summarise the key points in brief, the consolidating supervisor model, combined with the role of CEBS in supervisory convergence, is a step in the right direction. However, the role of the consolidating supervisor should be extended to Pillar 2. The waiver in Article 69 should be applied as a rule at the top level in the EU once the conditions are met and intra-group exposures should be risk-weighted at 0%. On the Trading Book Review we believe that work stream 3 on illiquid assets requires more time.

Delivering a level playing field within the EU would send a positive message to the rest of the world that consistency in application is of paramount importance. If the

objectives of the Lisbon Agenda are to be achieved the EU must be at the forefront in implementing global standards such as the new Basel framework.

ITEM 6 - SUPERVISORY COORDINATION IN THE EU

At the meeting this subject was presented by Mr. Freddy VAN DEN SPIEGEL, Chief Economist at Fortis Bank.

Although there are signs of convergence in thinking in the EU regarding the supervision problem in the financial industry, a unified position has not been reached yet.

The main goal of supervision, to a certain extent also the political goal, is to maintain confidence in the financial system. Supervision is triangle of entities:

- 1) Basel II – prudential supervision;
- 2) Lender of last resort – tool to solve liquidity problems;
- 3) Insurance – deposit insurance.

The most important question is how to organize all these three entities into one, as efficient as possible, system. Inefficiencies often show up as overlaps in the system, but holes are creating dangerous ineffectiveness. Fast reactivity would be essential for supervisors in order to be able to respond properly and in due time to economic realities. In theory it is easy and the key word here is to maintain the solvency of the system.

Eventually a supervisor should prevent bankruptcies. The lender of last resort should help banks in liquidity problems, but not in solvency problems. In reality all three factors are linked: a solvency problem may become liquidity problem and vice versa.

In reality there are huge conflicts of interest between different supervisory authorities (National banks, deposit insurance schemes, etc.). If those authorities are located in different countries, problems multiply. One has to react immediately, on the spot once an incident happens. In the EU there are 52 independent supervisory authorities at the moment. Some of them act as advisers, some negotiate, some even buy up problematic banks... there are many different independent supervisory authorities with different mandates. How can these different authorities solve a cross-border problem in a fast and efficient way once it arises?

In Basel II the home and host country concept has been offered, but those two concepts are very often in collision... The lender of the last resort is always a host country. However, the liquidity problem normally arises within a financial group, often a pan-European entity. In the areas of deposit protection and prudential supervision there is also the question of host and home country. Besides, there is always a question – tax payers of which country (host or home) will pay the bill in case of problems!?

What would be the solution to this, for the time being fortunately only theoretical, problem - the colleague of supervisors with leading one on top; a European FSA?

It is clear that the EU needs a global framework of architecture for modern and efficient financial supervision, but the real discussion regarding the possible solutions has not really started yet...

ITEM 7 - STATE OF INTEGRATION OF EUROPE'S FINANCIAL MARKETS

Mr Tanguy van de WERVE, head of FBE Banking Supervision department presented the conclusions and findings of the FBE report on the state of integration of Europe's financial markets, as follows.

The Financial Services Action Plan (FSAP) has been a success in so far as the 2003/2005 deadlines have broadly been met so far.

The extent to which the FSAP will contribute to the creation of a truly European market for financial services will mainly depend on three factors:

- the correct and timely implementation of the FSAP measures at Member State level;
- convergence of national supervisory practices;
- proper enforcement.

The level 3 Committees need to develop an EU-centric view of policy and promote cooperation between Member States. Industry has to play an active role in identifying and reporting infringements. The FBE supports the Lamfalussy model and also its extension to banking.

Carefully targeted legislation is needed in retail banking where removal of well-identified obstacles would help to open up national markets. The FBE considers the full harmonisation of key retail banking elements as the most effective means of creating a true European internal market for retail banking services.

Other priorities would include the removal of artificial obstacles to further consolidation in the European banking industry, a coherent VAT treatment of financial services, the creation of a market-driven Single Euro Payments Area, a more efficient cross-border clearing and settlement process and the implementation of the Basel II accord.

Policy making should be evidence based. If there is a perceived need for action, options other than regulation should also be considered. Industry consultation must be a feature of all stages of the legislative process.

The creation of a European Single Market for financial services is not an end but rather a means to increase the international competitiveness of the EU. Systematic assessment of the business impact of EU legislation should be carried out.

Given the unprecedented globalization of financial services, there is a need for a strong and united EU voice in the international arena and for a structured dialogue with the main EU partners.

ITEM 8 - IAS

The progress report on the latest developments in the IAS field, and in IAS 39 in particular, was introduced by Mr. Wilfried WILMS, adviser at the FBE, as follows.

The European Banking Federation industry has been critical of IAS 39 from inception. Our concerns about IAS 39 and, in particular, the inappropriateness of its hedging rules can be traced back to 1999 when the International Accounting Standards Committee (IASC) adopted IAS 39.

During the subsequent years, the International Accounting Standards Board (IASB) – which is the successor of the IASC – took several initiatives aiming at improving IAS 39. However, no significant amendments were made to areas which were key to the European banking industry.

The IASB published the standard on fair value hedge accounting for a portfolio of Interest Rate Risk. The outcome was, however, disappointing mainly because:

- the hedge accounting rules did not enable banks to hedge exposure to changes in interest rates that arise from the behavioural maturity of “core deposits” (i.e. sight and savings deposits);
- the standard put many restrictions on the use of such hedges which made the standard cumbersome to apply in practice and resulted in accounting rules which were not in line with banks’ risk management practices.

As a result, the FBE is currently seeking support from the IASB for its “Interest Margin Hedge” proposal, i.e. a hedging model that focuses on interest margin and in doing so provides a basis more compatible with the way in which banks seek to manage risk. It would, moreover, allow core deposits to be included in the hedged portfolio.

In the meantime, the European Central Bank had severely criticised IAS 39 because it allowed entities to designate any financial asset or financial liability as one to be measured at fair value (“fair value option”).

As a result of the opposition the European Commission endorsed IAS 39 only partially in November 2004. It refused, more particularly, to support its provisions:

- on the use of the fair value option and
- on hedge accounting.

The two ‘carve outs’ are temporary because the Commission expects the IASB to bring forward the necessary amendments to the current full fair value option by December 2004 and to the provisions on hedge accounting by September 2005.

ITEM 9 - MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE

This subject was presented by Mrs. Burcak INEL, adviser at the FBE.

The new Proposal was aimed at closing the loopholes for mutual recognition and establishing a common investor protection regime, above all by establishing a common regime for conduct of business rules for investment firms. This would bring

about more competition, lower costs for the customer, a better range of services across Europe, and higher global competitiveness.

This would increase competition between different trading venues which provide different services to clients with different needs at lower prices.

A short history of the Directive:

- Formal proposal for a Directive submitted to the Parliament and Council: November 2002
- First Reading at the Parliament: March 2003
- Council Common Position: December 2003
- Adoption of the Second Reading at the Parliament: July 2004
- Level 2 work started in January 2004 and is expected to continue until June 2005
- Formal adoption of the Directive: April 2004
- Entry into force of the Directive: May 2006

Key issues for the FBE:

- Ensuring overall an evidence-based approach to legislation
- Establishing a good precedent for the first Lamfalussy Directive
- Making sure that the passport regime is effective, with no loopholes
- Preventing overly prescriptive investor protection rules
- Ensuring a level playing field for cross-border services and providing legal certainty and lower regulatory costs for firms active cross-border
- Allowing the continuation of a range of different services provided to clients, including investment advice and non-advisory services, at globally competitive prices
- Supporting the abolition of the concentration rule
- Striking a balance between the need to introduce legally clear rules for best execution obligation and the need to allow firms sufficient flexibility
- Calibrating the pre- and post-trade transparency rules for intermediaries to demonstrated benefit for the market and clients
- Supporting appropriate grandfathering arrangements and transitional provisions

Key FBE Actions:

- Written responses and oral presentations at all of the consultations conducted by the Commission
- Bilateral meetings with the Commission
- Presentation at the Parliament Expert Panel: February 2003
- Contact with Parliamentarians and Permanent Representations

Next steps: 1st mandate:

Compliance, information and reporting to clients, safeguarding of assets, best execution, pre-trade and post-trade transparency for regulated markets (RMs) and multilateral trading facilities (MTFs), post-trade transparency for intermediaries. Deadline for CESR to deliver to the Commission the advice on most subjects in this mandate: end-January 2005. However, given the need to ensure overall coherence between the different rules designed to ensure a high degree of competition and efficiency in European markets and in particular between the transparency and best execution provisions of the Directive, certain issues are subject to an extended

deadline: Articles 21 (best execution), 28 (post-trade transparency disclosure by investment firms), 29 (pre-trade transparency requirements for MTFs), 30 (post-trade transparency requirements for MTFs), 44 (pre-trade transparency requirements for Regulated Markets) and 45 (post-trade transparency requirements for Regulated Markets) are due at the end of April 2005 (same as the 2nd mandate subjects).

2nd mandate:

Pre-trade transparency for intermediaries (Article 27), investment advice and non-advisory services (Article 19). Deadline for CESR to deliver its advice to the Commission: end-April 2005.

ITEM 10 - EUROPEAN PAYMENTS COUNCIL

Mr Patrick PONCELET, head of FBE payments department reported on the latest developments in the EPC field and in particular on the realisation of the Single Euro Payments area, a roadmap for 2004-2010.

This roadmap has been developed for the EPC Plenary and its communities to provide a description of the way forward for delivery of the Single Euro Payments Area (SEPA) programme.

It provides a refined definition and scope for SEPA, building on the original 2002 vision, and presents the key deliverables and priorities for EPC in the period ahead. A timeline is provided, supported by clear objectives for the six areas of focus represented by the current EPC Working and Support Groups, four responsible for payment instruments and two for supporting the areas of standards and law.

The final section reviews the role of stakeholders in adopting and implementing the SEPA and the pan-European payment instruments that will be delivered. This Roadmap is a 'living' document and will evolve. It will also form the basis for other communication presentations and more detailed descriptions tailored for specific audiences, including a text version.

The main objectives of the roadmap document, to:

- reaffirm the vision set out in the 2002 White Paper '*Euroland, our Single Payment Area*' and in the EPC Charter,
- clarify the SEPA definition and focus,
- establish EPC's priorities and the deliverables that will be required for the realization of SEPA,
- put in place an industry action plan and timetable with milestones for the defined deliverables,
- reinforce cooperation between banks and banking communities in relation to the adoption and implementation of SEPA payment instruments,
- mobilize other players and stakeholders to achieve buy-in and commitment to SEPA objectives,
- provide a toolkit for communication.

Real SEPA will be achieved when people can make payments throughout the whole euro area from one bank account or by using one card as easily and safely as a national payment is made today.

By 2008 the industry has to deliver “SEPA for the citizen” with cross-border and national use of pan-European Instruments such as Credeuro [The interbank convention which promotes the adoption of an efficient, low cost, end to end scheme for basic cross border STP (Straight Through Processing) Credit Transfers in euro by using IBAN]; Prieuro (a priority payment scheme), Direct Debit and Card Solutions. End-to-End Solutions for initiation and reconciliation also will have to be standardized and deployed.

By 2010 transformation of infrastructures will have to be fully underway either by conversion of national infrastructures into pan-European infrastructures (no parallel domestic & cross-border systems) or their elimination. Several PE-ACH (Pan-European Automated Clearing House framework) operators would gradually absorb payment volumes across Europe.

During the discussion phase of the item the question was raised by the chairman of the meeting, representing also Croatia, on the expected actions from the EU candidates with regards to the activities of the EPC. In answering this question Mr. Poncelet indicated that once new countries join the EU, they will have automatically a seat in the EPC. However, even before that, it would be wise for countries moving towards membership in the EU to start following more closely the EPC’s work and recommendations. The formalisation of the circulation of EPC information to the Banking Associations of the EU candidate countries might be worth considering.

ITEM 11 - ANY OTHER BUSINESS

Nothing was raised under this item during the meeting.

ITEM 12 - PREPARATION OF THE NEXT MEETING

It was decided and announced that the next “Brussels” meeting of the Associates will be held in Brussels on Thursday, 8 December 2005, a day before the FBE Executive Committee meeting.

The FBE Executive Committee members will be invited to participate in the meeting.

There is still a possibility to hold an “outside” meeting of the FBE Associates with the participation of the FBE Executive Committee members in late spring or early summer 2005. However, this will depend on the availability of the potential host of the meeting.

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Enclosure: 1