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Regulating Europe's Banking Market in the Age of the Euro

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José María Roldán
Director General of Banking Regulation – Banco de España
Chairman of the Committee of European Banking Supervisors

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Chair, Committee of European Banking Supervisors

EU specificities – what makes the EU special?

- We have a common objective to achieve a single market, and we have made a lot of progress towards that goal (not least with the successful introduction of the euro).

- In the banking sector specifically, we have a set of well-established banking directives that form the basis of the single market in the banking sector, and which give EU banks the right to operate across borders and through establishments in other Member States.

- And, even though each Member State has its own national arrangements and responsibilities for banking supervision, the directives lay down a set of common minimum prudential standards and rules that legally have to be applied by all of them.

- And finally, we have recently had a very important political initiative – the Financial Services Action Plan - a package of measures designed in the late 1990s to give a push to the completion of the single market in the financial services sector. The FSAP includes two key legislative initiatives that I want to focus on today: Basel II and International Accounting Standards.

Basel II and IAS as an opportunity for convergence

- Both initiatives present enormous opportunities for enhancing convergence of approach. This will, in turn, enhance efficiency and facilitate the completion of the single market.

- *IAS*

    - The EU has decided that IAS will apply to all listed companies from 1 January 2005 - this means that all EU listed companies will be speaking the same language in their financial reporting.

    - Let me stress that the tool that the EU has decided to use for this purpose is the strongest tool in its toolkit – the Regulation. This makes the application of IAS a legal obligation and one that applies directly to listed companies. Neither the European Commission nor the Member States have the possibility to make changes to the standards.

    - My own institution, Banco de España, which is the accounting regulator for Spanish banks, has extended the principles of IAS to individual balance sheet items (and it is possible that they will in the future be applicable for tax purposes).

- *Basel II*

    - Basel II has many benefits, even if we need sometimes to step back from the detail to fully appreciate them.

    - One of the most important benefits from the banks' perspective is that it brings regulatory capital closer to economic capital, thus reducing the possibility for regulatory distortions to their business, and thereby enhancing efficiency.

- o But its full advantages can only be realised if it is implemented effectively and consistently across countries.

- o The fact that Basel II means wide-ranging changes to the way that we supervise banks presents us with the ideal conditions for achieving this consistency or "convergence" as we call it.

- o Given that we all have to change our practices, we have a real incentive to work together to find the best ways of implementing the new framework.

- Both initiatives provide us with a window of opportunity for achieving greater convergence. We shouldn't miss it.

Institutional developments that allow the EU to seize this opportunity

- The extension of the "Lamfalussy approach" for regulation and supervision to the banking sector, and more particularly the creation of the Committee of European Supervisors (CEBS) have given us the right tools to take advantage of this opportunity at the right moment.

- CEBS is a committee of high-level representatives from all of the banking supervisory authorities and central banks of the EU, and has three important tasks assigned to it:

    - o Advising the Commission on matters of EU banking

    - o Promoting convergence in implementation of EU legislation and in supervisory practices

    - o Promoting cooperation and information-sharing between supervisory authorities

- The latter two tasks are key with respect to the two initiatives already mentioned, and CEBS is working hard to develop common thinking and consistent approaches

- More generally, our aim in CEBS is to develop a strong system of cooperation and coordination among national authorities and to build a common supervisory culture. CEBS operates through consensus.

What specific initiatives is CEBS taking?

- *IAS:*
    - o "Prudential filters" to avoid unwanted distortions to regulatory capital
    - o Common formats for financial reporting.

- *Basel II*
    - o Supervisory review "pillar 2" based on the principles of proportionality of supervisory actions and dialogue between supervisor and institution
    - o Validation of advanced approaches
    - o Common reporting for the solvency ratio
    - o Home-host coordination

- Regarding the common reporting projects in relation to IAS and Basel II: this is the first time that such an initiative has been proposed to have a single set of reporting requirements for banks' solvency and accounting data for regulatory purposes.

Is it going to work? The keys to success

- As already mentioned, CEBS works by consensus. This makes decision-making more difficult, of course, but the end result is one that is supported by everyone (another example is the Basel Committee).

- The possibility to agree common/consistent approaches ex ante presents a far better opportunity for convergence than trying to do the same after everyone has already designed their own individual approaches. In this respect, as I said earlier, Basel II and IAS present us with a window of opportunity.

- Market discipline works for supervisors too. The proposed directive to implement Basel II imposes obligations on supervisors to explain publicly how they are applying Basel II (also known as "supervisory disclosure"). Supervisory disclosure will be an important tool for demonstrating to the outside world the real level of convergence we have reached, and will act as a driver for greater consistency. CEBS is currently consulting on a framework for supervisory disclosure under Basel II, and we have made strenuous efforts to ensure that our proposal promotes the highest degree of transparency and usefulness.

How do the new countries fit in?

- Fears have been voiced that the incorporation of such a large number of new Member States will slow down the process of integration. From CEBS' perspective, this couldn't be further from reality.

- We all have to make changes to implement Basel II and IAS, so we are all in the same boat. And we are aiming to arrive at the same port at the same time.

- Furthermore, some of our most important convergence initiatives in CEBS have stemmed from proposals from the new countries (and these proposals have been very close to the finished product).

- Our experience so far has been very positive and better than even we expected.