

UNI-Europa Finance meeting with DG Internal Market and Services

Brussels, 17 November 2008
Briefing Note

31.10.08

0 Introduction

The purpose of this briefing note is to create a common platform for UNI-Europa Finance participants and to allow Commission representatives time to prepare relevant contributions and responses to our questions.

Overall objective of the meeting:

To influence decision-making, to create understanding and to work for results that are in line with UNI-Europa Finance policies. Our ambition is that the meetings should be of a win-win character.

Purpose of the meeting:

- *Receive relevant information on the content and impact of EU initiatives*
- *Receive information and advice on decision-making processes/state-of-play/political play*
 - *Who is involved*
 - *Progress*
 - *Obstacles*
 - *What can UNI-Europa/affiliates do*
- *Meet people who can take our views on board.*
- *Give advice and share in-depth knowledge about financial services, employment and social issues*
- *Give in-depth presentations on issues of particular interest or concern*

1 Financial crisis

1.1 Recent developments including Accounting

Background on the adopted changes to Accounting standards

The European Commission has adopted amendments to accounting standards. The intention is to mitigate the consequences of the recent turbulence in financial markets. The amendments ensure that EU companies have the same flexibility as their American competitors to reclassify assets held-for-trading into the held-to-maturity category. In these circumstances, financial institutions in the EU would no longer have to reflect market fluctuation in their financial statements for these kinds of assets.

Questions to the Commission:

- Where are we standing in the revision of accounting rules, i.e. what are the possibilities of reclassifying assets from the trading book to the banking book?

1.2 Revision of bank capital requirements rules to reinforce financial stability

Background:

The revision of the rules on capital requirement is a direct follow-up of the Roadmap agreed by ECOFIN in Autumn 2007 to address the turmoil in financial markets. The revision of the rules on capital requirements for banks is designed to reinforce the stability of the financial system, reduce risk exposure and improve supervision of banks that operate in more than one EU country. Under the new rules, banks will be restricted in lending beyond a certain limit to any one party, while national supervisory authorities will have a better overview of the activities of cross-border banking groups.

The purpose of the Capital Requirements Directives is to ensure the financial soundness of banks and investment firms. Together they stipulate how much of their own financial resources banks and investment firms must have in order to cover their risks and protect their depositors. The main changes comprised in the proposal are:

- Improving the management of large exposures
- Improving supervision of cross-border banking groups
- Improving the quality of banks' capital
- Improving liquidity risk management
- Improving risk management for securitised products

The provisions reflect the on-going work at the Basel Committee on Banking Supervision and the Committee of European Banking Supervisors.

http://ec.europa.eu/internal_market/bank/regcapital/index_en.htm

UNI-Europa Finance position:

UNI-Europa Finance welcomes the revision of the rules on capital requirement. It is clear that all loans and credit liabilities must be backed by adequate equity. High risks must be supported by higher capital adequacy ratios to avoid destabilisation of markets as with the recent turmoil.

UNI-Europa Finance equally welcomes the initiatives to improving cross-border financial supervision and cooperation. Banking groups operating across borders must of course be subject to financial supervision following the same structures.

- What is the state of play for the revision?
- Is the Commission convinced that this revision will be sufficient to avoid a recurrence of the current crisis situation?
- What is being done to remedy the pro-cyclical effect of the current Basel II ratio?

1.3 Credit Rating Agencies (CRA)

Background

It is generally agreed that the Credit Rating Agencies (CRA) have played a crucial role in the triggering of the current financial crisis by their underestimation of the credit risk of credit products. The CRAs are not independent agencies with an impartial assessment of the risk level. They have an economic interest in the ratings, and the ratings are therefore not the reliable, accurate and precise piece of information required by investors when they make their investments. There is an inherent conflict of interest in the current functioning of the rating market. Furthermore, the market is dominated by few, major agencies making it difficult for new agencies to enter the market.

Commissioner McCreevy has stated that he is convinced of the need to legislate in this area at EU level and that the crisis has shown that self-regulation has not worked. CRAs will be obliged to deal with conflicts of interest, have sound rating methodologies and increase the transparency of their rating activities. He intends to present a proposal to the Commission for adoption this autumn. In June 2008, the ESME Expert Group issued a report to the Commission on the role of CRAs. The report addresses the general questions of the role of CRAs in financial markets, the current regulation and whether regulation can solve some of the current problems. Furthermore, it answers a range of concrete questions set out in the mandate by the Commission.

In end July 2008, the Commission set off a consultation round with two consultation documents. The first one a "Proposal for a regulatory framework for CRAs", and the second "Policy options to address the problem of excessive reliance on ratings". Furthermore, the consultation papers suggest two options: The first option is based on a reinforced co-ordination role for the Committee of European Securities Regulators (CESR) and strong regulatory co-operation between national regulators; the second is to combine the establishment of a European Agency (either CESR or a new agency) for the EU-wide registration of CRAs and the reliance on national regulators for the supervision of CRA activities. The consultation period ended on 5 September.

http://ec.europa.eu/internal_market/securities/esme/index_en.htm

http://ec.europa.eu/internal_market/securities/agencies/index_en.htm

UNI-Europa Finance position:

UNI-Europa Finance highly shares these concerns of the conflict of interest inherent in the current role of Credit Rating Agencies and the oligopolistic market structure with a few agencies dominating the rating market. Credit Rating Agencies should not work on the development of financial products and subsequently issue a creditworthiness rating for the same products. Such conflict of interest is damaging.

A system must be developed where rating agencies are rated themselves. We need a body to monitor the monitors, to ensure the compliance with financial trends. UNI-Europa Finance supports the idea of establishing independent/public rating agencies that do not – cannot – carry out rating on the basis of economic interest.

Questions to the Commission:

- Can the Commission tell something about the conclusions in the ESME report, how the Commission assesses the report and how the conclusions will inspire coming proposals from the Commission?
- Can the Commission, at this stage, say something about the results of the consultation round that was closed on 5 September?
- Can the Commission comment on which measures will be contained in the coming proposal?
- Is the establishment of an independent CRA at EU level part of the Commission's plans?

1.4 Deposit Guarantee Schemes

Background:

The European Commission has put forward a revision of EU rules on deposit guarantee schemes that puts into action the commitments made by EU Finance Ministers on 7 October 2008. The purpose of the Directive on Deposit Guarantee Schemes is to protect a portion of depositors' savings and to ensure confidence into the banking sector, in order to avoid bank runs leading to severe economic consequences.

Under the new rules, the minimum level of coverage for deposits will be increased within one year from €20,000 to €100,000, and initially to €50,000 in the intervening period. Individual Member States can choose to add to these minimum levels. In addition, the payout period in the event of bank failure will be reduced from three months to three days, and co-insurance (i.e. where the depositor bears part of the losses) will be abandoned. It is furthermore the intention to further the cooperation between the deposit guarantee schemes in the individual member states.

The proposal now passes to the European Parliament and the Council of Ministers for consideration.

UNI-Europa Finance position:

UNI-Europa Finance welcomes this initiative protecting consumers against bankruptcies and thereby contributing to re-establishing confidence in the financial system. However, it is important that guarantees do not attain a level that tempts banks to irresponsible actions with the covering of the state.

Questions to the Commission:

What is the state of play in this field?

1.5 Supervision/Crisis management

Background:

It is commonly agreed that the current crisis provides clear evidence of the need to improve supervisory measures in the financial markets. Supervision is essential not only in order to maintain stability and integrity in financial markets, but also to protect the interests of depositors, investors and consumers and ensure the proper functioning of business transactions. The continuous integration of global financial markets makes cooperation and convergence of financial supervision very important.

The Commission is currently reviewing the supervision structures in financial markets as a part of the follow-up actions to the ECOFIN Road Map to assess and combat the financial crisis. The review addresses the need of improved supervision and increased cooperation and convergence of the financial supervision in the EU. Among the initiatives are a number of improvements to the functioning of the Committees of Supervisors that are soon to be implemented. It comprises giving more clear, homogenous and comprehensive frameworks for their activities.

Solvency II (for insurance) and the Capital Requirement Directive (for banks) regulate the cross-border-supervision in the EU.

The European Parliament is currently debating the future of supervision.

UNI-Europa position:

UNI-Europa Finance welcomes the initiatives for improving financial supervision and cooperation. It must be ensured that all companies in the EU are supervised according to the same criteria, wherever they are based. The supervisory authorities in different countries must enhance their cooperation, and international supervision standards must be regularly updated to keep up with new requirements and with the innovativeness of the

industry. Furthermore, central banks must be at the centre of any system of financial supervision, not least with their responsibility for providing liquidity.

On 11 September 2008, Commissioner McCreevy stated, "Some stakeholders consider that there would be merit in proposing further institutional changes. I have advocated an evolution rather than a revolutionary approach. We also have to be pragmatic about what is achievable now. It is crucial we make progress on strengthening our supervisory co-operation. Maybe at some point in time in the future we will have some form of EU level supervision for the largest financial institutions. But I don't believe we have the necessary conditions today for such a fundamental change".

Questions to the Commission

- Do the Commission still believe that an evolutionary approach to revising supervisory systems in Europe is sufficient – bearing in mind the recent months' dramatic development within financial?
- What is the state of play of these supervision revisions?
- Is the Commission convinced that this revision will be sufficient to avoid a recurrence of the current crisis?
- Are there at this stage considerations of establishing a European finance inspection?

1.6 UNI-Europa Finance approach to financial crisis

The current global financial crisis has sparked an intense debate about what went wrong in the financial markets and how to remedy to their shortcomings. Following political pressure to act, regulators, supervisors and advisory forums have published a great number of recommendations on how to improve the functioning of global financial markets. The question is now to assess if the important issues are being addressed by all market players.

UNI Finance has been calling for a re-think of the world's financial system since the beginning of the crisis last summer. In a statement, it set out 13 proposals on the regulation of financial markets. They include increasing the transparency of financial services companies, reviewing capital adequacy and bankers' pay systems rules as well as enhancing regulation of unregulated players (hedge funds, sovereign wealth funds and private equity firms).

A key demand for UNI Finance is in particular that "Finance sector employees are those that make the industry function. Regulators and companies must ensure that working conditions and pay incentives promote rather than hinder regulatory objectives and excellent customer service". Finance employees want to be rewarded for providing good service and quality advice, rather than for selling inappropriate products to customers.

This last issue is particularly important, as the current financial crisis has had unprecedented consequences on workers and consumers. Because of finance institutions' irresponsible behaviour, huge losses were made leading to the closure of firms or divisions of firms and to ten thousands of layoffs. In addition, predatory lending practices by mortgage lenders - including misrepresenting the terms of loans, making loans without regard to consumers' ability to repay, or packing loans with undisclosed charges and fees – have had a devastating effect on home buyers. Millions of people are now struggling to meet their home loans or have lost their house.

An assessment of the current financial regulation debate shows that the issues of consumer protection and the working conditions of finance employees are not being debated in a satisfactory way among regulators and supervisors. Worse, as a result of the crisis and the greater pressure faced by financial institutions to make profits, some banks are even setting more aggressive sales targets for their employees. This means threatening their workers with less pay or dismissal if they do not sell. Qualitative advice and the customers' interests become secondary. Some banks thus intensify policies of undue risk taking that led to the financial crisis and huge losses for their shareholders. They have not learnt their lesson and regulators still ignore such behaviour.

The current business model of the financial industry has failed. The primary purposes of a bank or insurance company are to provide good service, good jobs as well as good and sustainable return to shareholders. What we

have seen instead is a scorched earth policy of maximising profits for short-term investors and yearly incomes for top managers. It is time for regulators to stop these excesses. Regulators must take up the 13 demands of UNI Finance. They must ensure that financial companies act responsibly towards the economy, their shareholders, their customers and their employees.

<http://www.uniglobalunion.org/UNIFinance.nsf/By+Date/E96DD0CCD7253585C1257362004C24EC>

<http://www.uniglobalunion.org/UNIFinance.nsf/By+Date/AB77E3B42FB399CFC125736200422D9E?OpenDocument>

<http://www.uniglobalunion.org/UNIFinance.nsf/By+Date/036A280F58FB4DEAC12574670051635B?OpenDocument>

2 Company law

2.1 SE-directive / shelf companies / employee representation rules

Background

Since the SE Directive entered into force in 2004, almost 200 SE-companies have been established. However, the majority of these around 200 companies are not 'real' companies, as they have no business activities and no employees. Only 45 'normal' SEs with activities and employees exist, whereas the rest are 'virtual' constructions. A great part of these 'virtual' companies are the so called 'shelf companies', which are set up often by specialist companies offering their shelf SEs to sale, so that these can enter into business very quickly.

In the setting up of the employee-free SE construction, no negotiation on worker involvement can of course take place. As the SE Directive only concerns the moment of foundation of the legal structure, it is legally unclear what will happen if employees, at a later stage, are transferred into an empty SE, or if an empty SE is bought by a normal company with employees.

UNI-Europa Finance position

The lack of legal clarity in the case of transition from a shelf SE to a 'real' SE as regards the negotiation of employee involvement structures is of course problematic. The rules on employee involvement in European companies must apply in all companies. If the use of shelf companies cannot be prevented – or this is not wanted – there must be a clarification of what happens in the case where no employees were in the company when the negotiation of employee involvement structures should have taken place, i.e. during the initial, legal establishment of the SE.

Questions to the Commission

- Does the Commission recognise that this lack of clarity is problematic?
- Is anything done to legally clarify the circumstances of negotiation of employee involvement structures in shelf SEs?
- Is anything done to legally prevent, or in other ways combat the use of shelf SEs?

2.2 Cross-border mergers and acquisitions (simplification of rules)

A simplification of the rules on mergers and acquisitions is underway as to ensure a competitive business environment for European enterprises. The Commission has made a proposal aiming at reducing administrative

burdens for enterprises in relation to mergers and acquisitions. The proposal contains proposals of reducing the reporting requirements of companies in the case of mergers and divisions, avoiding double reporting where reporting requirements also result from other EU rules, and introducing the possibility for companies to use the Internet and electronic mail in order to publish the draft terms of merger or division and to provide shareholders with the documentation required.

UNI-Europa Finance position

UNI-Europa Finance would like the Commission's assessment of the implications of this proposal.

Questions to the Commission

- What is the state of play of this proposal?
- Will the proposal have any impact on employees? Or other important implications?

2.3 European Private Companies

Background

In June 2008, the Commission presented a proposal for a Statute on a European Private Company (SPE). The introduction of a European Private Company Statute is part of the Action Plan of the European Commission on modernisation of Company law and Enhancement of Corporate Governance. It is the intention to provide a uniform but flexible legal form for small and medium sized enterprises (SME), as it is the case for the European Companies (SE) but with a lower requirement of minimum capital. The SPE will mean that SMEs can set up their company in the same form, no matter if they do business in their own Member State or in another.

The proposed SPE Statute does not create specific participation rights for workers, but the SPE is subject to rules on employees' rights applying in the Member State where the SPE has its registered office. The registered office does not have to be in the same country as the central administration or where the principle business activities are carried out. Hence, the SPE can choose any country for the registered office, though the company and its activities are in practices based elsewhere.

UNI-Europa Finance position

UNI-Europa Finance's position on this is based on the assessments of the ETUC. Establishing uniform legal structures to simplify business activities for SMEs across Europe is a good initiative that will contribute to the competitiveness of SMEs in Europe. However, the workers' participation rights contained in the proposal represents a step backwards compared to what was achieved for the European Company (SE). First of all, the proposal should contain minimum rules on workers participation rights that apply for the SPE no matter in what member state it is situated or operating. The same rules that apply for SEs should also apply for SPEs. Having minimum rules on workers participation rights in the SPEs Statute will contribute to increasing standards in participation rights in Member States with poor or no worker participation rights for SMEs. Second, the option of placing the registered office of the SPE in another Member State than the administrative office and practical business activities is an invitation for business to circumvent national workers' participation rules as well as other company law, taxation rules and supervisory regulation (in case of financial institutions). By placing the registered office in the Member State with the weakest rules on participation, taxation and supervision, the SPE can run its business as usual with the administrative office in one Member State but avoid the rules that apply in this Member State.

An obvious invitation to circumvent national legislation like this is of course not acceptable. European regulation should contribute to heightening standards across Europe, not create loopholes that undermine rights obtained in countries with high standards.

Questions to the Commission:

- Will the Commission do something to abolish these loopholes inviting to circumvent national rules on workers participation?
- Do the Commission plan to complete the SPE Statute with rules on workers participation rights in line with what applies in European Companies (SE)?
- What is the Commission's position?

3 Money-laundering directive

Background

The Directive applies to the financial and other key services sectors and also covers all providers of goods, when payments are made in cash in excess of €15.000. Those subject to the Directive must cooperate in the fight against money laundering by taking various measures to establish customers' identities, report suspicions and set up preventive systems within their organisations.

The Directive is applicable to the financial sector as well as lawyers, notaries, accountants, real estate agents, casinos, trust and company service providers. Its scope also encompasses all providers of goods, when payments are made in cash in excess of €15.000.

The Directive will have an impact on a great number of employees in the finance industry across Europe. After many years of persistent working by UNI-Europa Finance and its affiliates, the message finally got through: Employees reporting suspicions must be protected. Only thus can the effectiveness of the Directive be ensured. Article 27 states that "Member States shall take all appropriate measures in order to protect employees of the institutions or persons covered by this Directive who report suspicions of money laundering or terrorist financing either internally or to the FIU from being exposed to threats or hostile action". Although not very concrete, this article represents an important step forward.

Member States have agreed to implement the Directive within two years after its publication in the European Union's Official Journal. The deadline for implementation was 15 December 2007.

UNI-Europa Finance position:

The matter of concern for UNI-Europa Finance and its affiliates mainly centres on specific issue, namely the implementation of Art. 27 on employee protection. UNI-Europa Finance has got indications regarding the implementation processes in various member states; regarding the Danish implementation process, the employee protection provided for in Art. 27 of the Directive have been omitted. This matter has been dealt with in the remarks to draft law, whereas it has been omitted in the finalised law text.

UNI-Europa Finance believe it is very problematic that Art. 27 is not fully part of European legislation yet, since this does not give the employees the legal protection they are entitled to according to the Directive. At the moment, it appears that some Member States are of the opinion that existing penal sanctions are enough protection, without the particular employee protection provided for in the Directive.

It is of the utmost importance to ensure that the protection in relation to suspect transaction reporting is effective and enforceable. The work of the Commission, the exchange of information in the forum between UNI-Europa Finance and DG Internal Market, as well as experience from implementation in other member states can support our efforts.

The topic was discussed at the last consultation meeting with DG MARKT on 10 April 2008. At that stage, few countries had implemented the directive, though the deadline was well overdue.

Questions to the Commission:

- What is the state of play regarding the implementation processes in Member States?
- Will the Commission take any measures to ensure that the provisions for employee protection are properly included in national legislation?

4 MiFID – Experiences and feed back from MS**Background:**

The objective of the Markets in Financial Instruments Directive (MiFID) is to integrate European financial services markets by enabling investors to invest and procure investment services across EU borders more easily, removing obstacles to the use of the EU passport by investment firms, and ensuring appropriate levels of protection for investors and consumers of investment services across Europe. The draft measures are being tabled after a very extensive round of intense consultations with all stakeholders over a two years period. They are designed to protect investors and consumers without imposing unnecessary compliance burdens on firms. The measures have been drafted to provide firms with clear and predictable rules and to give greater security to investors and consumers who buy services from foreign companies.

The Directive also contains requirements that appropriate information on financial services products is given to clients, and that the suitability of products for particular clients is assessed. Thus, the MiFID provides basic regulatory measures on the issue of sales and advice.

The MiFID Directive was to be implemented by November 2007.

http://ec.europa.eu/internal_market/securities/isd/index_en.htm

UNI-Europa Finance position:

UNI-Europa Finance welcomes the regulatory introduction of the obligation to give appropriate information to costumers. However, the current system of bonus structures inciting employees to sell products is counterproductive to the aim of protecting costumers and giving prudent and qualified advice. The bonus systems with aggressive sales targets have contributed comprehensively to the current turmoil, triggered by the crisis in the US mortgage market. Bank employees should be rewarded for good service, rather than for selling ever-increasing levels of debt to customers.

It is the hope, however, that the implementation of the MiFID directive will contribute to a more reasonable balance between selling and giving advice, though further steps have to be taken.

Questions to the Commission:

- What is the state of play as regards the implementation of the Directive?
- Has the Commission gathered any experience from the Member States as to whether the Directive has – or will have – an effect on the use of bonus systems undermining the quality of advice?
- Has the Commission considered any further regulation within this area related to the dilemma of sale and advice?