Warsaw, 13.06.2008

European Commission
Internal Market and Service DG
Financial Institutions
Banking and Financial Conglomerates

Polish Banks Association response to the Commission Consultation on possible changes to the Capital Requirements Directive (2006/48/EC and 2006/49/EC)

The Polish Bank Association welcomes the opportunity to respond to the European Commission on changes to the Capital Requirements Directive. It’s very important for the banking industry having the possibility to participate in consultation of CRD Directive amendments.

Firstly, we fully agree with the need for greater harmonisation of the Large Exposures rules. This prudential regulation is substantial for banking industry development and changes in this area will have impact on banks activity. Therefore, changes should be prepared to support the achievement of stable, strong and diversified market and reduction of regulatory burden where possible. In our opinion there is a need to verify Large Exposures policy and to bring the rules more into line with the new risk-sensitive approach towards credit risk requirements, laid out in Basel II and remove differences among individual EU countries according to numerous national discretions (19 options), applied by national supervisory authorities. The lack of consistent Large Exposures rules in EU countries creates an uneven level playing field for banks in EU territory. But in our opinion these changes should be prepared in a way to avoid funding problems and capital shortages in smaller banks. Amendments should be conducted by regulators with guidelines related to treatment of parent and subsidiary exposures. We also would like to state the concern of the requirement for the credit institution to look through to the underlying exposures where it is aware of them in order to determine the existence of a group of connected clients. I our opinion proposed solution will cause problems for banks with obtaining such information and accrue costs connected with such a review.

The second topic of the review of the Capital Requirement Directive is the proposal of changes in architecture of banking supervision in Europe. We fully support the proposal presented by
European Commission. The experience of last financial turmoil has shown the importance of bigger cooperation between home and banking supervisions on developing global financial market. The present exchange of information between supervisors is not sufficient and the broader cooperation is necessary, particularly during the financial squeeze. In our opinion the broader exchange of information by establishing of colleagues of supervisors will create better conditions for development of bigger cooperation between supervisors in near future.

The Polish financial market, as financial markets in many other Central-Eastern Europe countries, is in specific situation. The majority share in total assets of banking sector in Poland have banks, which main shareholders are foreign banks. It is the result of openness of Polish economy for foreign capital for many years. It was the situation completely different from the economic policy of other developed EU countries. This policy resulted in bigger stabilization and development of financial market in our country. But this openness for foreign investors in financial institutions creates also specific problems concerning the maintaining the stability in financial system, when important changes in international structure of banking supervision are proposed by European banking community. The proposals regarding the changes on the scale of tasks for home and host supervisor can be suitable for supervisors from countries where the biggest share in financial market belongs to the domestic banks and the role of foreign banks is not so important as in Poland and they have only limited influence on financial stability in the local market.

In our opinion the problem of future delegation of task for supervisor have to be bound with the problem of delegation of responsibility for banking stability. Any changes in current architecture of banking supervision in Europe can be solved only when the problems as crisis management, lender of last resort, liquidity management, role of central bank or deposit guarantee scheme are solved. The Polish Bank Association attaches particular importance to this problem, especially when the risk of international contagion of crisis situation in financial market is high and is growing rapidly.

Until the safety net on international scale is not yet created, the home supervisor cooperating with host supervisors (suitable for foreign subsidiaries of bank) is our favorite solution. The home supervisor can play the role as lead supervisor organizing the work of colleague of banking supervisors from different countries and promoting the supervision culture and practices on consolidated level. In this model the home supervisor is primus inter pares and the power of this structure will rely on the building the strong level of trust among regulators in different countries. This should be achieved by expanding the work of regulatory colleges to examine how they would work together facing a capital adequacy or liquidity crisis.

Host supervisor can contribute to the supervisory process over banking group, because it has the bigger knowledge of the local banking landscape and local market conditions, not available to home supervisor. Applying one set of rules for all bank activity may cause that some important message are lost.

The home supervisor could fulfill the role of unique supervisor for foreign subsidiary of domestic bank only if it takes over simultaneously the full responsibility for results of the supervisor activity. In effect, if the home supervisor will supervise exclusively the banking group (including foreign subsidiaries), making the final decision in supervisory activity, the state, the central bank and the deposit guarantee scheme suitable for home supervisor and for supervised bank should be prepared to bear the full burden of the financial problems occurring in foreign subsidiaries of bank. It is impossible in modern economy to have the
additional rights without taking the responsibility for effects of activity of any institution. This solution is similar to the existing model when bank has the branches abroad.

Maybe the best solution for one financial market in Europe will be the creation of single European supervisory institution in the future (particularly for supervision of international banks). In our opinion this solution can create level playing field for all large banks in Europe. There is easier for one European banking supervisor to cooperate actively with other international institutions which are (or will be) responsible for safety of financial sector in Europe. But many institutional conditions have to be met in structure of safety network before this idea can be realized. We strongly supported and support the review of arrangements in the area of liquidity management, lender of last resort issues, deposit guarantee schemes and winding and bankruptcy proceedings in order to adapt them to meet the needs of one financial market in Europe.

Enclosed please find detailed comments of the PBA to presented proposals.

Yours faithfully,
Polish Banks Association responses to the proposed changes to CRD Directive
(consultations till 16 JUNE 2008)

<table>
<thead>
<tr>
<th>Changes to Directive 2006/48/EC</th>
<th>Comments</th>
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<td>Article 4, paragraph 45</td>
<td>ACCEPT but there are significant implications due to widening of the definition. However, we understand that this is more risk-sensitive approach, which is justified giving the importance of proper risk management.</td>
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<th>Article 106 sec. 3</th>
<th>REJECT-according to problems with obtaining information and costs connected with such review</th>
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<tr>
<td>In respect of exposures referred to in Article 79, paragraph 1, points m, o and p, where there is an exposure to underlying assets, a credit institution shall look through to the underlying exposures where it is aware of them in order to determine the existence of a group of connected clients.</td>
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<td>The Commission services are interested in learning stakeholders’ views on the impact, if any, of the approach suggested above. With regard to interbank exposures, a limit is suggested that represents the higher of 25% of a bank's own funds or Euro &quot;X&quot; million (the Committee of European Banking Supervisors has suggested that &quot;X&quot; should be set at Euro 150 million). Stakeholders' views are sought on the appropriateness of a Euro 150 million limit for exposures to institutions, and on the impact of this suggestion for banks' funding requirements on a day-to-day basis as well as during a contingency.</td>
<td>We do not fully support the changes to the Large Exposures regime. Although the change in definition of 'connected clients' is welcomed and justified from the risk point of view, the changes in the concentration limits calculation are unacceptable. In particular the changes to Articles 111-117. The proposed changes and removal of national discretions are very likely to create funding problems and capital shortages in smaller banks. The capital impact of the proposed changes should be conducted by regulators with guidelines related to treatment of parent and subsidiary exposures.</td>
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**B. HYBRID CAPITAL INSTRUMENTS**

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<th>Do stakeholders agree with:</th>
<th>proposed changes are welcomed</th>
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<td>(i) the Commission services' suggested eligibility criteria and the principle-based approach suggested above?</td>
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<td>(ii) the recognition of dated instruments - with a predetermined minimum original maturity - in firms' original own funds?</td>
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<td>(iii) the quantitative limits suggested? In this respect, the Commission services are also interested in views whether an additional limit would be useful to improve even further the quality of capital e.g. by requiring firms' core capital (equity, reserves and retained earnings) to be higher than a predetermined proportion (e.g. 50%) of minimum capital requirements?</td>
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**C. SUPERVISING ARRANGEMENTS**

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<th>Changes to Directive 2006/48/EC</th>
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<td>Article 4, paragraphs 49</td>
<td>Welcomed changes, aimed at securing the positions of host</td>
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1. In addition to the obligations imposed by the provisions of this Directive, the competent authority responsible for the exercise of supervision on a consolidated basis of EU parent credit institutions and credit institutions controlled by EU parent financial holding companies shall carry out the following tasks:
(a) coordination of the gathering and dissemination of relevant or essential information in going concern and emergency situations;
(b) planning and coordination of supervisory activities in going concern as well as in emergency situations, including in relation to the activities referred to in Articles 123, 124 and points 14 and 15 of Annex V, part 10, in cooperation with the competent authorities involved; and
(c) planning and coordination of supervisory activities in cooperation with the competent authorities involved, and if necessary with central banks, in preparation of and during emergency situations, including adverse developments in credit institutions or in financial markets. This includes exceptional measures referred to in Article 132(3)(b), the preparation of joint assessments, the implementation of contingency plans and communication to the public.

2. In the case of applications for the permissions referred to in Articles 84(1), 87(9) and 105 and in Annex III, Part 6, respectively, submitted by an EU parent credit institution and its subsidiaries, or jointly by the subsidiaries of an EU parent financial holding company, the competent authorities shall work together, in full consultation, to decide whether or not to grant the permission sought and to determine the terms and conditions, if any, to which such permission should be subject.
An application as referred to in the first subparagraph shall be submitted only to the competent authority referred to in paragraph 1.
The competent authorities shall do everything within their power to reach a joint decision on the application within six months. This joint decision shall be set out in a document containing the fully reasoned decision which shall be provided to the applicant by the competent authority referred to in paragraph 1.
The period referred to in subparagraph 3 shall begin on the date of receipt of the complete application by the competent authority referred to in paragraph 1. The competent authority referred to in paragraph 1 shall forward the complete application to the other competent authorities without delay.
During the period referred to in subparagraph 3, the consolidating supervisor shall, at the request of the applicant, or of any of the other competent authorities concerned, consult the Committee of European Banking Supervisors. The consolidating supervisor may consult the Committee on its own initiative.
When the Committee is consulted, the period referred to in the third subparagraph shall be extended by two months. Where the Committee has been consulted, the competent authorities concerned shall duly consider such advice before taking their joint decision.
In the absence of a joint decision between the competent authorities within 6 months within the periods referred to in the third and fifth subparagraphs, the competent authority referred to in paragraph 1 shall make its own decision on the application.
The decision shall be set out in a document containing the fully reasoned decision and shall take into account the views and reservations of the other competent authorities expressed during the periods referred to in the third and fifth subparagraphs. The decision shall be provided to the applicant and the other competent authorities by the competent authority referred to in paragraph 1. The decisions referred to in the third and sixth fifth subparagraphs shall be recognised as determinative and applied by the competent authorities in the Member States concerned.

3. The consolidating supervisor shall establish colleges of supervisors to facilitate the exercise of its tasks referred to in the first and second paragraph and in Article 130. The establishment and functioning of colleges shall be based on the written arrangements referred to in Article 131. The Committee of European Banking Supervisors shall elaborate guidelines for the operational functioning of colleges.

The competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company and the competent authorities of a host country where systemically relevant branches are established may participate in colleges of supervisors. The consolidating supervisor shall chair the meetings of the college and shall decide which competent authority participates in a meeting or in an activity of the college. This decision shall take account of the relevance of the supervisory activity to be planned or coordinated for those authorities, and the obligations referred to in Articles 40(3) and 42(3). The competent authorities participating in the college shall apply Article 129(1)(c) having full regard to the work of other forums that may be established in this area.

The competent authorities participating in the colleges shall agree on the entrustment of tasks and delegation of responsibilities and cooperate closely, having regard to the obligations in Articles 40(3), 42 and 132.

The consolidating supervisor and the competent authority responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company in a certain Member State, shall, within a reasonable period of time, do everything within their power to reach an agreement on the application of Articles 72(2) (Disclosure requirements for 'significant' subsidiaries), 74(2) (reporting for the calculation of minimum capital requirements), 113(1)(c) (treatment of intra-group exposures for large exposures purposes) and 136(2) (own funds requirements in excess of the minimum level) to these subsidiaries. Where these competent authorities disagree, the matter shall be referred for consultation to the Committee of European Banking Supervisors, which shall give its advice within two months. The competent authorities shall duly consider such advice before taking its final decision in accordance with their responsibilities under this Directive. This shall not affect the rights and responsibilities of the competent authorities under this Directive.

The consolidating supervisor shall inform the Committee of European Banking Supervisors of the activities of the college of supervisors, including in emergency situations.

The Commission services seek views on the proposed amendments relating to crisis management and home/host issues. In particular, views are sought on the definition of a systemically relevant branch and an appropriate level for the threshold in Article 42(2).

The proposed closer cooperation between home and host regulators will improve the approval processes and supervisory reviews. The threshold should be set in relation to total deposits in a Member State; 1% is relevant.
### E. TECHNICAL AMENDMENTS TO DIRECTIVE 2006/48/EC

#### Art. 95

1. Where significant credit risk associated with securitised exposures has been transferred from the originator credit institution in accordance with the terms of Annex IX, Part 2, that credit institution may:

   (a) in the case of a traditional securitisation, exclude from its calculation of risk-weighted exposure amounts, and, as relevant, expected loss amounts, the exposures which it has securitised; and

   (b) in the case of a synthetic securitisation, calculate risk-weighted exposure amounts, and, as relevant, expected loss amounts, in respect of the securitised exposures in accordance with Annex IX, Part 2.

2. Where paragraph 1 applies, the originator credit institution shall calculate the risk-weighted exposure amounts prescribed in Annex IX for the positions that it may hold in the securitisation. The risk-weighted exposure amounts for the originator credit institution shall not be less than [15%] of the risk-weighted exposure amounts of the securitised exposures. Where the originator credit institution fails to transfer significant credit risk in accordance with paragraph 1, it need not calculate risk-weighted exposure amounts for any positions it may have in the securitisation in question.

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<td>Please consider applying the rule also to credit derivatives in trading book purchased in order to protect a CCR exposure. As a result we recommend removing the terms “not including in the trading books” from the last sentence.</td>
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**Suggested stipulation**
The credit derivatives purchased as a protection against a CCR exposure in trading book are classified also to the trading book. According to the proposed changes in this case the credit institution might not include the credit derivatives for purpose of calculating capital requirements for CCR. |

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<tr>
<th>Annex III/ Part 3 &amp; Part 4</th>
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<tr>
<td>Please consider distinguishing the percentages for purpose of calculating the potential credit exposure for deliverable and non-deliverable derivatives. Our suggestion is to use the percentages actually given in Directive for calculating the future potential credit exposure for deliverable derivatives and set up new, lower percentages for non-deliverable derivatives.</td>
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**Suggested stipulation**
Credit risk of non-deliverable derivatives is significantly lower than credit risk generated by deliverable derivatives what should be taken into account in the capital charge calculation. |

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<th>Annexes V, VI, VII, VIII, IX, X and XII of Directive 2006/48/EC</th>
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<td><strong>Annex VI, Part 1, p. 6.4.29 and 6.4.31</strong></td>
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<td>W związku z wprowadzeniem zmian do Załącznika VI, Część 1, punkt 6.4.29 i punkt 6.4.31, należałoby wprowadzić analogiczne zmiany dotyczące rezydualnego, a nie pierwotnego terminu zapadalności w punkcie</td>
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(8) Annex VIII, Part 2, is amended as follows:

(a) Point 1.8.2.13 is replaced by the following:

"Life insurance is not eligible in Poland"

"13. For life insurance policies pledged to the lending credit institution to be recognised the following conditions shall be met:
(a) the company providing the life insurance may be recognised as an eligible unfunded credit protection provider under Part I, point 26;
(b) the company providing the life insurance policy is openly pledged or assigned to the lending credit institution;
(c) the company providing the life insurance is notified of the pledge or assignment and as a result may not pay amounts payable under the contract without the consent of the lending credit institution;
(d) the declared surrender value of the policy is non-reducible;
(e) the lending credit institution must have the right to cancel the policy and receive the surrender value in a timely way in the event of the default of the borrower;
(f) the lending credit institution is informed of any non-payments under the policy by the policy-holder;
(g) the credit protection must be provided for the maturity of the loan.
Where this is not possible because the insurance relationship ends before the loan relationship expires, the credit institution must ensure that the amount deriving from the insurance contract serves the credit institution as security until the end of the duration of the credit agreement; and
(h) the pledge or assignment must be legally effective and enforceable in all jurisdictions which are relevant at the time of the conclusion of the credit agreement.

(g) the surrender value is declared by the company providing the life insurance and is non-reducible.
(h) the surrender value is to be paid in a timely manner upon request,
(i) the surrender value cannot be requested without the consent of the credit institution,
(j) the company providing the life insurance is subject to the Directives 2002/83/EC of the European Parliament and of the Council of 5 November 2002 concerning life assurance and 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the reorganisation and winding-up of insurance undertakings or is subject to supervision by a competent authority of a third country which applies supervisory and regulatory arrangements at least equivalent to those applied in the Community, and
(k) the company providing the life insurance holds assets over which the beneficiaries have a claim that is prior to any other claims when the company defaults on liabilities that are due and whose time value is at least as high as the sum of the declared surrender values of the outstanding policies."

(f) Point 1.7.2.80 is replaced by the following:

"Where the conditions set out in Part 2, point 13 are satisfied,
credit protection falling within the terms of Part I, point 24 may be treated as a guarantee by the company providing the life insurance. The value of the credit protection recognised shall be the current surrender value of the life insurance policy, the portion of the exposure collateralised by the current surrender value of credit protection falling within the terms of Part I, point 24 shall be
- subject to the risk weights specified in point 80 bis where the exposure is subject to Articles 78 to 83; or
- assigned an LGD of 40% where the exposure is subject to Articles 84 to 89 but not subject to the credit institution's own estimates of LGD."

(g) A new point 1.7.2.80 bis is added: "80 bis. For purposes of the first indent in point 80, the following risk weights shall be assigned on the basis of the risk weight assigned to a senior unsecured exposure to the company providing the life insurance:
(a) if the senior unsecured exposure to the company providing the life insurance is assigned a risk weight of 20%, a risk weight of 20%;
(b) if the senior unsecured exposure to the company providing the life insurance is assigned a risk weight of 50%, a risk weight of 35%;
(c) if the senior unsecured exposure to the company providing the life insurance is assigned a risk weight of 100%, a risk weight of 70%;
(d) if the senior unsecured exposure to the company providing the life insurance is assigned a risk weight of 150%, a risk weight of 150%.
In case of a currency mismatch, the above risk weights shall be subject to an adjustment as set out in points 84 and 85.

(13) Annex X, Part 3, is amended as follows:
(a) Point 1.2.2.14 is replaced by the following: "1.2.2.14. "Credit institutions must be able to map their historical internal loss data into the business lines defined in Part 2 and into the event types defined in Part 5, and to provide these data to competent authorities upon request. Loss events which affect the entire institution may be allocated to an additional business line 'corporate items' due to exceptional circumstances. There must be documented, objective criteria for allocating losses to the specified business lines and event types. The operational risk losses that are related to credit risk and have historically been included in the internal credit risk databases must be recorded in the operational risk databases and be separately identified. Such losses will not be subject to the operational risk charge, as long as they continue to be treated as credit risk for the purposes of calculating minimum capital requirements. Operational risk losses that are related to market risks shall be included in the scope of the capital requirement for operational risk.""

In our opinion there are several incidents that may result in operational losses, and this is impossible or time/cost consuming to allocate them to the particular line. The example of such a loss: a branch car crash, it is impossible to decide to which line the loss should be allocated as branch business is split into different lines of business. We think that "exceptional circumstances" could be changed into "circumstances that are well reasoned".

F. TECHNICAL AMENDMENTS TO DIRECTIVE 2006/49/EC

| The Commission Services seek views on the above technical changes and if they achieve the aim of clarifying or correcting the respective provisions of the directive. In particular, views are sought on the adjusted treatments for: CIUs under the IRB in Article 87(11) and (12) and in particular on the calibration of the factors in square | The requirement to “look through” for CIUs underlying instruments will require more additional information, which is not always justified from the risk management point of view. Life insurance is not eligible in Poland. |
brackets;
Life insurance as collateral and whether the risk weights and supervisory LGD are commensurate with the additional protection due to the preferential status of a life insurance claim compared to a "normal" claim on the insurance provider.
In the context of securitisation, views are sought on the effectiveness of the proposed changes in improving risk management and making appropriate adjustments to certain capital treatments.

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At the beginning of this section there are numbers of annexes listed to which the changes apply, i. a. Annex V. But in the subsequent detailed description of amendments there are no changes related to Annex V.

**Suggested stipulation**
On the list of the proposed amendments there is point (2) related to Annex II followed by point (4) related to Annex VII (point 3 is missing).