

**Presentation by Jonathan Taylor, EC Hearing on EC Communication  
“Driving European Recovery” and de Larosière Report, 7<sup>th</sup> May 2009**

Thank you for inviting me to say a few words at this conference. This is an important and serious debate, and if I may, I would like to begin by noting a few important themes and principles.

First, I think it is clear in the light of the market turmoil that there is a need for substantial improvements to regulation, supervision and to European and global cooperation in these areas. The Commission’s Communication and the de Larosière report are among the most important texts that have emerged in response to the turmoil. There is a great deal in them with which the industry wholeheartedly agrees.

But second, and turning to the cross-border cooperation arrangements which are the main subject of this hearing, it is also clear that there is a range of views on the Commission’s and de Larosière’s proposals. We have seen various reactions from the official sector in different countries, some supportive, some more querying. There are variations also among firms. This is not surprising. Different authorities, and different firms, have different experiences of the financial turmoil, and different priorities. International groups are structured in different ways. Some groups have more of an EU focus; for others the EU is part of a wider global presence. The latter attach particular importance to global as well as EU coherence. So if the EU is to remain a truly international financial centre, we need to accommodate all these different views. There are no simple answers.

Third, from firms’ point of view, a crucial issue is I think not so much the structure of EU arrangements, but their quality. There is a lot of hard work to be done to raise supervisory standards and to improve financial stability cooperation. Structures are important, but what really matters is doing things better: not just preventing a recurrence of the problems we have experienced, but being alert to a broad range of possible problems in future. We must not allow too much focus on structure to distract from this central objective.

Fourth, some crucial details of the Commission’s and de Larosière’s ideas, particularly in the regulatory and supervisory area, are still quite roughly sketched out and we look forward to studying the Commission’s more detailed ideas in its further Communication later this month. We need to be hard-headed and practical in making decisions with a clear understanding of what is proposed and the risks and consequences.

Fifth, while EU coordination is essential, the EU is not an island. As the Commission Communication and de Larosière report recognise, we must also always work towards global cooperation, coordination, and consistency. The EU has a leading role to play in developing global consensus, especially now that the Commission participates in global standard-setting bodies, but we

have a responsibility to lead in a consensual way, and not push in directions that will lead to global divergence.

Turning to the specific proposals in the Commission's Communication and the de Larosière report:

We agree in principle with the proposal for a macro-prudential **Risk Council**. But we need to ensure three things:

(1) The Risk Council's analysis must take advantage of micro-prudential as well as macro-prudential information, but in a way that respects and preserves the confidentiality of that information;

(2) There must be streamlined mechanisms to ensure that, having due regard to national autonomy, supervisors respond to the Risk Council's conclusions; and

(3) We need to be clear about what macroprudential risks we are guarding against, and how we will do so. The Risk Council's analysis must take account of risks wherever they arise: in the banking, securities, or insurance sectors.

The Commission and de Larosière propose a Risk Council that would be composed mainly of central bankers. There should be more balanced representation in the Risk Council between:

(1) supervisors as well as central banks; and

(2) securities market and insurance authorities as well as banking authorities.

Two other features are also essential:

(1) There needs to be close linkage between the Risk Council and the Member State finance ministers who will have ultimate responsibility for responding to its conclusions.

(2) As proposed, the Risk Council needs to be strongly linked to the global macro-prudential analysis mechanisms which are being established under the London Summit action plan through the IMF and Financial Stability Board, however that works out, and we must not treat the EU as a self-contained island of risk.

And the Risk Council needs robust arrangements for making sure its conclusions are taken notice of and followed up. A comply or explain approach seems a sensibly robust approach which also respects national autonomy.

The proposed **System of supervision** is more complicated.

de Larosière's **Stage 1** - improving the quality of EU supervision and supervisory coordination - is the most immediate and important priority. There seems to be general, perhaps universal, agreement that it is important to do it, and to do it urgently. But we should not short-circuit these important tasks, as the Commission suggests, by moving immediately to set up new structures, and hoping that the new structures will sort out the problems. We surely need to ensure that there is trust between national authorities, based on mutual confidence in the quality and coherence of what they do, **before** we transfer powers from national to EU authorities. Among the most important tasks that need to be done as part of Stage 1 are:

(1) That the harmonised core rules in EU legislation should be fully and consistently implemented by Member States and enforced under Lamfalussy Level 4. The separate initiatives proposed by the Commission and de Larosière to reduce national discretions and align national enforcement are important elements of this work.

(2) Ensuring that regulatory staff have the right skill sets and detailed knowledge and understanding of different markets.

(3) Analysing what degree of convergence is appropriate in different supervisory tasks, how far supervisory flexibility is valid or necessary, recognising that the optimal level of integration may need to differ in different areas, and also taking into account that there must be alignment between regulatory or supervisory decision-making and fiscal support.

(4) Streamlining how colleges operate, with EU arrangements well integrated into global colleges, so that coherence of supervisory strategy, exchanging information, and coordinating supervisory activity, on an equal basis within the EU and with third country authorities, is a matter of routine.

As noted earlier there is some uncertainty surrounding de Larosière's **Stage 2**, and how it is proposed that the EU authorities would be constituted, what they would, do, and how they would work. We look forward to the Commission's forthcoming Communication. We have recommended in our response to the Commission's consultation that an EU authority would need to have a series of defining characteristics. Among the most important of these are the following:

(1) The governance must have specific regard to the wholesale and global character of cross-border markets. It must ensure that all those who are interested in what the authority does can have their voice heard. It must be clear who it is answerable to, how the quality of its performance will be measured, and what sanctions will be applied if it fails. Objective governance arrangements are clearly essential.

(2) There must be clear demarcation of boundaries of competence between the EU authority and national authorities. We would need to be clear about what the role of an EU authority would be in helping the Commission to

achieve consistent effective Level 4 implementation of EU legislation; what was the appropriate scope for differential implementation of an agreed regulatory outcome; the scope for national autonomy over supervisory approaches, technical decisions, and issues not harmonised at EU level, and about the use of comply or explain procedures. Supervisors should, in any event, be closely linked to the markets they are supervising. We also need a clearer understanding of what terms like “binding mediation” and “binding technical decisions” mean, and of how the demarcation of decision-making power would dovetail with fiscal responsibility.

(3) The regulatory philosophy should be outcome-focused, aimed at achieving defined and agreed public policy needs.

(4) In whatever we do, we must embed effective regulation disciplines, especially market failure analysis, impact analysis, and cost-benefit analysis, diligent consultation, and genuine dialogue with regulated entities and other interested parties, as standard and automatic procedure.

(5) The governing body and staff should need to be technically expert, market-aware, alert and rapidly responsive to market developments.

(6) There should be explicit attention paid to the different needs of different markets and sectors: not just the sectoral distinction between banking, securities, and insurance; but also wholesale and retail; prudential, conduct of business, and market supervision; and perhaps other dimensions as well. In each case, the scope of the EU authority’s responsibility should be made clear. This might differ from one sector or task to another.

(7) Proximity to the EU’s key global markets would be vital for an EU authority so that it could have close interaction and dialogue with market experts, and draw on strong pools of technical talent for its own staff.

In any event, it remains vital that EU rule-making takes place within the global standard-setting framework established in the London Summit, and that supervisory coordination at EU level takes place within the context of global coordination. The Commission’s participation in the Financial Stability Board and other global standard-setting bodies means that it is well placed, alongside Member State participants, to influence global standard-setting.

We are all committed to making progress: indeed, not to do so would be dereliction of duty. We look forward to the commission’s detailed proposals, and to playing our part in taking the discussion forward.

Thank you again for inviting me to comment.

6<sup>th</sup> May  
J Taylor