FIN-FSA'S ACTION IN RESPONSE TO ICELANDIC BANKING CRISIS

Claims by depositors with Kaupthing Bank, Finnish Branch, were repaid in full owing to financing extended by Finnish banks, without recourse to deposit insurance or government funds. The Finnish Government provided a guarantee against possible legal risks to cover the parties involved in the arrangement.

PILLAR 3 DISCLOSURES OF BANK CAPITAL ADEQUACY ACCORDING TO STANDARD, BUT NEED TO BE MADE MORE INTELLIGIBLE

According to a survey carried out by the Financial Supervision Authority (FIN-FSA), banks that changed over to the revised capital adequacy framework in 2007 disclosed information on their capital positions according to the FIN-FSA's relevant standard. However, the intelligibility and legibility of the information provided need to be enhanced.

LISTED COMPANIES' BASIS FOR OUTLOOK STILL TOO GENERAL

According to a survey carried out by the FIN-FSA, listed companies provide too general a description of their business outlook. Typically, they only provide information about general demand and market elements without addressing company-specific factors. In addition, companies often fail to provide reasons for changes in the outlook.

WHAT ARE CAPITAL-GUARANTEED STRUCTURED NOTES?

Capital-guaranteed structured notes mean that the issuer promises to pay back to the investor the nominal capital of the note on the date of maturity even though no yield has accumulated or it would be negative. The capital guarantee only applies to the nominal capital; for example premium amortisation or subscription fees are not reimbursed.

New proposals for Capital Requirements Directives

EXTENSION PROPOSED TO DECISION-MAKING POWERS OF GROUP-LEVEL SUPERVISOR ON RECAPITALISATION OF SUBSIDIARY BANKS

The purpose of the amendments to the EU Capital Requirements Directive is not to change the respective responsibilities of the supervisory authorities in home and host countries. However, the intention is to give host supervisors more extensive rights to obtain information for the supervision of branches and the right to participate in joint supervision activities. Furthermore, the establishment of colleges of supervisors is to become mandatory and the tasks of these colleges are to be extended from crisis management to supervision in normal times.

FIN-FSA'S ACTION IN RESPONSE TO ICELANDIC BANKING CRISIS

The aim of the Financial Supervision Authority (FIN-FSA) in its response to the Icelandic banking crisis has been the safeguarding of the interests of Finnish depositors and the maintenance of confidence in the functioning of financial markets. Owing to financing provided by large Finnish banks, the claims of the depositors of Kaupthing Bank h.f., Finnish Branch, were reimbursed in full on 31 October, without recourse to deposit insurance or government funds. The Finnish Government provided a guarantee to cover the parties involved in the arrangement against possible legal risks. FIN-FSA wishes to thank the banks, the Icelandic and Finnish authorities and the Finnish Government for their excellent cooperation in achieving this exceptional arrangement.

Large Icelandic banks taken over by Icelandic financial supervisor in early October

The bankruptcy of the investment bank Lehman Brothers on 16 September 2008 led to a deepening of the global financial crisis. Having suffered a loss of confidence among providers of finance, large Icelandic banks rapidly lost their chances to acquire market funding for their operations and headed for a liquidity crisis.

The Icelandic financial supervisor (FME) had to take over the banks, using powers afforded by emergency laws: Glitnir and Landsbanki on 6 October and Kaupthing Bank on 9 October 2008. In these banks, FME exercises supreme, conclusive power of decision, similar to shareholder power, and the separately established 'Resolution Committees' the power similar to those vested in the board of directors. There are plans to divide the above-mentioned three banks into a 'new bank', which is to focus on domestic operations in Iceland, and an 'old bank', which is scheduled to manage foreign asset items and business operations.

In Finland, Glitnir and Kaupthing operated as deposit banks: Glitnir Bank Ltd as a subsidiary with Finnish authorisation and Kaupthing Bank h.f. as a branch. Both also provided a wide range of investment services. In Finland, the Landsbanki branch only had operations related mainly to securities intermediation. Additionally, eQ Bank Ltd operates in Finland under Icelandic ownership, providing investment services and deposit banking (eQ Bank is owned by the investment company Straumur-Burdaras).

In Finland, Glitnir Bank Ltd acted as a subsidiary with Finnish authorisation and Kaupthing Bank h.f. as a branch, whereas the Landsbanki branch mainly had operations related to securities intermediation. Additionally, eQ Bank Ltd operates in Finland under Icelandic ownership, providing investment services and deposit banking.

FIN-FSA prevented asset transfers abroad and suspended Kaupthing Branch operations

FIN-FSA monitored the situation in Icelandic banks with increased vigilance, as the financial market crisis went on, and had initiated a closer scrutiny of their Finnish units. As liquidity shortfall at the Icelandic parent banks became evident, on the morning of 6 October, FIN-FSA decided to prevent Glitnir Bank, Kaupthing Bank Branch and eQ Bank from transferring assets out of Finland to their respective parent banks or foreign subsidiaries of their parent groups. This measure ensured that cash holdings and other assets in Finland remained as safeguards for claims of Finnish depositors in particular.

On Thursday morning, 9 October, Kaupthing Bank's depositor customers outside Iceland were no longer able to withdraw their deposits, as the parent bank had closed online banking connections. Subsequently, with FME's consent, FIN-FSA immediately suspended the operations of the Finnish Branch. It became indispensable to suspend all branch operations and to take over the branch under close FIN-FSA scrutiny through an appointed administrator. Payout of individual deposits could not be permitted, not even on their due dates, as it was necessary to clarify the branch's possibilities of repayment of all deposits, and depositors could not be treated in a discriminatory manner.

Selling Glitnir Bank to the Finnish senior management (on 14 October), and subsequently reinstating the name FIM, allowed the lifting of the assets transfer ban. Unravelling the situation at Kaupthing enabled a renewed provision of investment services to existing customers (20 October), but otherwise branch operations have remained suspended. As regards eQ Bank, the assets transfer ban continues to be valid.

Repayment of all Finnish Kaupthing deposits maintains confidence in the banking system

The Finnish financial market authorities (FIN-FSA, the Bank of Finland and the Ministry of Finance) started talks on the possibility of organising the repayment of Finnish deposits immediately after suspension of Kaupthing Branch operations. Under the leadership of a mediator appointed by the Deposit Guarantee Fund, detailed discussions were launched among the banks, and the FIN-FSA kept close contact with the Icelandic financial supervisor (FME). The main options that could be considered were ensuring branch liquidity via a loan granted against branch assets or having recourse to the deposit guarantee scheme.

A loan arrangement, clearly a better option for depositors, became feasible, as the three largest Finnish banks, OP-Pohjola group, Nordea Bank Finland and Sampo Bank, committed to organising the requisite loan of about EUR 100 million, which enabled a one-off payout of all depositor (excluding other financial institutions) assets. Total claims, ie deposits with accrued interest, amounted to some EUR 115 million. In security for the funding provided, the banks received the Branch's loan portfolios and other asset items.

The banks committed to bearing the financial risks involved in the arrangement (in the case of inadequate proceeds from the sale of Branch assets to cover loan repayment), but needed a state guarantee against legal risks, though unlikely but possibly substantial if materialised, related to the arrangement. Such risks are associated with potential claims consisting of right of recourse in case of Kaupthing Bank's liquidation. On 24 October, Finnish Parliament provided the required guarantee to the banks participating in the arrangement, and also to depositors, in order to cover these risks. For depositors, state guarantee ensures that any deposits that might be claimed back from depositors will be reimbursed by the state.

As soon as the necessary contractual and technical arrangements were finalised among the banks, the FIN-FSA and the FME, full reimbursement was paid out to Branch depositors under FIN-FSA supervision on 31 October 2008, ie within the previously announced timetable. As, in contractual terms, the interests accrued constitute part of depositor assets, they were also paid simultaneously. If the interests had not been paid, Finnish depositors' interest claims would have remained outside the arrangement and thus remained unresolved.

Finnish approach unique

The Finnish private-sector solution is exceptional compared to the solutions instituted elsewhere in Europe. In other EU countries where branches of Kaupthing or other Icelandic banks are located, recourse to deposit guarantee has been the main rule, with the exception of Sweden. The deposit guarantee option involves a much later reimbursement to depositors (eg in Finland about after 4 months from the occurrence of insolvency) and only to the upper limit of the deposit protection provided. The Icelandic deposit guarantee scheme is responsible for deposits up to EUR 20,800 per depositor, with the Finnish scheme affording the additional coverage in excess of this amount, ie according to current regulations up to EUR 25,000. Of the deposits held with Kaupthing Bank's Finnish Branch, about EUR 67 million would have fallen within the Icelandic deposit guarantee scheme and about EUR 3 million within the Finnish scheme. In other countries, the respective governments have committed to reimbursing deposits according to deposit guarantee schemes or in full, which may require granting of a loan by the state concerned to the Icelandic Deposit Guarantee Fund for meeting its responsibilities. Given that the matter was settled in Finland without recourse to the deposit guarantee scheme, the Kaupthing special arrangement does not alter Finnish deposit protection principles.

In Finland, it was possible to come to an arrangement under which depositors received their funds quickly and in full, because the banks shared the authorities' aim to maintain confidence in deposits in Finland. FIN-FSA also acted in accordance with its primary goal of maintaining Finnish financial market stability and confidence in market operations. If assets of Kaupthing's depositors had been lost and depositor confidence might have been shaken significantly in a situation sensitised by the financial market crisis. Stable deposit funding conditions are also important for banks in the current market situation. The arrangement came about, underpinned by the Icelandic supervisor's close interaction with the FIN-FSA over a period of about three weeks, providing an innovative, albeit demanding, approach to the problem.

Branch structure proved problematic in crisis situations

Within the EU framework, branch supervision differs markedly from subsidiary supervision, as the main supervisory responsibility lies with the parent bank's home country supervisor. The independent powers of the host country supervisor are considerably narrower than in the case of subsidiaries, both in ongoing supervision and in crisis situations. FIN-FSA does not have the independent right to inspect a branch, relying, in respect of a bank as a whole and its branch, mainly on information received from the home country supervisor. In addition, in the current crisis involving the branch of Kaupthing Bank, the FIN-FSA has been able to act only on the basis of detailed powers allocated by the FME. If the views of FME and the FIN-FSA on the resolution of the problem had diverged, no such arrangement as was now achieved could have come into existence. A branch constitutes an integral element of its parent bank, and therefore cannot be sold as an integrated whole as easily as a subsidiary. This makes crisis management through private-sector solutions increasingly complex.

Consequently, the FIN-FSA considers it important that branch supervisors may participate in cooperation between supervisors and conduct local inspections, either in cooperation with, or empowered by, the home country supervisor, in the similar manner as in the supervision of a bank operating as a subsidiary. This is naturally of particular relevance when large banks change into branches. This issue is duly taken into account in the guidelines of the Committee of European Banking Supervisors (CEBS) on supervisory cooperation, but it should also be given appropriate attention at the level of EU legislation. For the purposes of crisis management, directive-level EU regulation should ensure the host country's access to information and right to participate in the supervisory process and discussion on key supervisory decisions. These are among the main tasks of 'colleges of supervisors'. In order to intensify supervisory work, the coordinating role of all home country supervisors also needs to be enhanced.

FIN-FSA takes the view that legislation concerning Finland's new financial and insurance supervisory authority should clearly focus on extending the objective of financial market stability and efforts to achieve it through supervisory work to also cover banks operating as branches. On top of this, in order to foster the stability objective, the right to obtain information should be as extensive as permitted under EU legislation.

FIN-FSA will consider the ways of further developing operative crisis management on the basis of experience gained from this crisis.

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PILLAR 3 DISCLOSURES OF BANK CAPITAL ADEQUACY ACCORDING TO STANDARD, BUT NEED TO BE MADE MORE INTELLIGIBLE

This year, banks for the first time published information on their capital positions in accordance with the requirements of the revised capital adequacy framework (Basel II, Pillar 3). However, the manner of presenting the information and the choice of priorities diverged considerably from each other. Going forward, efforts need to be made to enhance the legibility and intelligibility of disclosed information.

FIN-FSA reviewed the disclosures of capital adequacy (Pillar 3) by the banks that migrated to revised capital regulation and supervision in 2007. Overall, it can be noted that the banks have disclosed information on their capital positions as required under Pillar 3. The authenticity of disclosures was not examined separately, as validation had been ensured by auditors in connection with auditing procedures. Only disclosed information on capital adequacy was analysed for making an assessment of whether the bank had published the matters required under the FIN-FSA standard 4.5. These include risk management and risk assessment processes, internal capital adequacy assessment processes and the minimum level of own funds, various risks and risk management principles for various risk areas, and overall information on capital adequacy.

Intelligibility of information needs to be improved

There were major divergences in how banks presented their information and what they emphasised. This is understandable, considering the abstract nature of disclosed information, differences in bank size and distinctions between the nature and scope of bank operations (eg geographically).

Under the revised framework for capital regulation and supervision, banks and investment firms disclose more extensive information on their capital adequacy for the markets than before.

Banks still need to pay attention to the legibility and intelligibility of disclosed information. The language used by banks is often strongly flavoured market jargon, which only professionals manage to understand. Accordingly, Pillar 3 requirements challenge the banks to abandon opacity and use instead a language that is understandable to all.

Intelligibility of information includes the requirement that information must be as comprehensive, adequate and topical as possible in order to enable stakeholder representatives to make reasoned and timely decisions on transactions on the basis of the information they receive.

Pillar 3 aims at market transparency and market discipline

Pillar 3 disclosure requirements seek to increase market transparency. Transparency, in turn, contributes to market discipline: If depositors, investors and other stakeholders acting in the markets have information on the quality and level of various banks' capital resources, risk management and other factors related to capital adequacy, they will be able to invest in, and place deposits with, banks they consider as being the best. Transparency will be possible only if the information provided is comparable.

In the current situation, an effective comparison of information is rather difficult, purely because only part of the banks disclose information on their capital adequacy according to Pillar 3. Comparison is also impaired by the fact that Pillar 3 disclosures have only been made once. Not until in a few years' time will we have enough information available to permit effective comparability.

International harmonisation of disclosure practices as a goal

Last year, the Committee of European Banking Supervisors (CEBS) launched a project aimed at harmonising Pillar 3 disclosure practices in its member states. Perhaps the most challenging element of the project focuses on clarifying the relationship, and reaching closer alignment, between accounting regulation and Pillar 3 requirements. The ball is now in the court of the sector, which has also undertaken Pillar 3 analyses under the auspices of the European Banking Federation (EBF).

Finnish banks should also make use of these analyses. Wider national cooperation is worthwhile for harmonisation of Pillar 3 practices in the Finnish financial markets, too, so as to achieve greater convergence between national and international practices.

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WHAT IS PILLAR 3?

Under the revised capital adequacy framework (BASEL II), banks and investment firms disclose more extensive information on their capital adequacy for the markets than previously. The requirements for disclosure of capital adequacy (Pillar 3) complement the first and second Pillars of the capital adequacy framework and promote market transparency in respect of information related to supervised entities' capital positions. The information that needs to be disclosed concerns, on the one hand, supervised entities' capital management such as the level, quality and adequacy of own funds and, on the other hand, risk management and risk exposures.

LISTED COMPANIES' BASIS FOR OUTLOOK STILL TOO GENERAL

According to a survey carried out by the FIN-FSA, listed companies provide too general a description of their business outlook. Typically, they only provide information about general demand and market conditions without addressing company-specific factors and reasons for a change in the outlook are not always provided. The grounds for outlook were not always given for the entire corporation but for each business sector. In addition, performance forecasts given in connection with the business outlook were not always unequivocal.

The FIN-FSA carried out a survey on 70 listed companies investigating how well they comply with the new requirement, incorporated into the Securities Markets Act in February 2007, of having to provide grounds for their business outlook. The survey also looked into compliance with the recommendations and application guidelines contained in the FIN-FSA Standard 5.2 b. The 70 companies surveyed included 20 large and mid cap companies and 30 small cap companies. The impact of the line of business was not subject to evaluation.

Key results of the survey

Only about a third of all the companies surveyed and half of the large cap companies gave a clear description of their business outlook from the company's own business perspective. The most common shortcoming in the grounds for outlook given by the surveyed companies was their very general nature, ie the outlook was only explained on the basis of the general market outlook with no comment on company-specific factors. Furthermore, the companies often commented only factors affecting future developments. A total of 12 companies evenly from the three groups used only demand and market factors as grounds for their business outlook. Three small cap companies and one mid cap company did not provide any grounds for their business outlook.

Basis for outlook	Small cap (n=30)	Mid cap (n=20)	Large cap (n=20)	Total (n=70)
Demand and market factors	25	16	20	61
Cost development	10	7	9	26
Corporate acquisitions	12	4	4	20
Cost-saving measures	9	4	7	20
Order backlog	11	3	4	18
Price development	3	3	8	14
Investment or increase in capacity	2	3	6	11
Investment in sales, marketing or product development	5	5	1	11
One-off factors	5	1	1	7
Other factors	6	4	3	13

The survey also showed that not nearly all companies provide an explanation for a change in the business outlook.

According to a survey carried out by the FIN-FSA, listed companies provide too general a description of their business outlook.

The FIN-FSA is of the opinion that if a company has given a profit warning with a separate stock exchange release, the business outlook in the next performance report should repeat the reasons for the profit warning and the prior outlook should be announced to the market. Alternatively, reference can be made to the press release where this information was provided.

The survey also showed that some companies presented their business outlook or the reasons for it only for each division separately. The FIN-FSA considers it important that the future outlook and its basis are always presented for the entire corporation in order for the investor to get a truthful picture of the outlook for the corporation as a whole. In addition, if elsewhere in the performance report future prospects are outlined for each division or market area separately, the business outlook should also refer to those parts of the performance report.

67 companies ie 96% of those surveyed included a profit forecast in connection with the business outlook in at least part of the performance reports. Profit forecasts were noticeably often open to interpretation and unclear. The FIN-FSA emphasises that in regular performance reporting it is particularly important to present future prospects and profit forecasts in a clear and consistent manner for each reporting period.

In addition to the shortcomings found in the survey, listed companies should pay attention to the following factors in particular:

- the concept of profit in the profit forecast should be unambiguous
- the terminology used should be consistent and should not leave room for interpretations whether the forecast is a profit forecast or not
- commentaries of the selected key figures should be consistent for each reporting period
- long-term performance objectives and business outlook should be kept firmly apart
- changes in the business outlook should be announced without undue delay.

Survey focused on interim reports, financial statement releases and profit warnings

The survey examined 280 performance reports: 6- and 9-month interim reports and financial statement releases for 2007 and 3-month interim reports for 2008. The survey focused only on what was presented under the heading ‘business outlook’ or similar. In practice, the business outlooks given in the financial statement releases and management reports were uniform, so only one of the reports is included in the total. The survey included the profit warnings issued by the companies in the same period.

The following factors were highlighted in the survey: what kind of reasons were given to justify the business outlook, were changes in the outlook justified, how extensively was the outlook reported and how clear and consistent the companies were in giving profit forecasts.

The shortcomings found have been addressed in the supervisory work conducted by the FIN-FSA.

Details about the survey can be found in the Markkinat 4/2008 release (available only in Finnish).

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REGULATIONS AND INSTRUCTIONS CONCERNING PUBLICATION OFBUSINESS OUTLOOK

According to chapter 3, section 1, of the Accounting Act, the annual report shall contain an estimate of expected future performance.

According to chapter 2, sections 5 a and 6 a, of the Securities Markets Act, the commentary of the interim report and financial statements shall give an estimate of probable developments in the current accounting period, to the extent it is possible, as well as provide grounds used as basis for this estimate. The requirements on presenting the basis of estimates were added to the Act in February 2007 in connection with the adoption of the Transparency Directive.

The FIN-FSA standard 5.2b on the disclosure obligation of the issuer and shareholder contains recommendations and application guidelines regarding the presentation of business outlook and publication of profit warnings. The standard states that the estimate of future performance can be a general description of the business outlook or more detailed performance forecasts.

A general description can be the issuer’s estimate of future developments in net sales or a description of market developments. Profit forecasts can be considered to be estimates of future time periods that directly or indirectly specify the probable minimum or maximum level of the issuer’s results. Data that can be used to calculate an approximate level of future earnings or losses is also considered as profit forecasts. These include a mention of future profitability or an estimate of future profits, profit margin or profit for the period.

Profit warnings must be used to announce a change in the issuer’s expected results, development of its financial standing or other factors whose future the issuer has estimated, if the change will have material impact on the value of the issuer’s security. Although the term ‘profit warning’ refers to profit development, it can be considered to refer to all factors whose future development the issuer has estimated.

WHAT ARE CAPITAL-GUARANTEED STRUCTURED NOTES?

Structured notes are often marketed with a capital guarantee, which means that the issuer promises to pay back to the investor the nominal capital of the note on the date of maturity even though no yield has accumulated or it would be negative. Capital guarantees are typical features of structured notes, and by emphasising the capital guarantee issuers wish to illustrate how investment in structured notes differs from direct investment in shares, for example.

Similarly to other bonds, structured notes always carry the risk that the issuer becomes insolvent. The issuer is in a state of insolvency if it cannot meet its obligations, ie payback of the structured note, due to eg bankruptcy. If structured notes are marketed with capital guarantees, the risks involved, ie the so-called issuer risk, should always be made clear.

Structured notes are typically without guarantors. Should the note have a guarantor, they are responsible for paying back the nominal capital should the issuer become insolvent. It is, of course, possible that both the issuer and the guarantor become insolvent. This risk becomes heightened if the guarantor and issuer belong into the same corporation. The conditions of the note specify who the guarantor is. Even though the note is sold by someone else than the issuer, for example a securities broker, the responsibility for paying back the nominal capital always rests with the issuer and possible guarantor.

The capital guarantee only applies to the nominal capital; for example any premium amortisation or subscription fees are not reimbursed. In other words, in respect of notes with a nominal capital of EUR 1,000, issue price of 110% and subscription fee of 1% from the nominal capital and for which the investor has paid EUR 1,110 at the time of subscription, the capital guarantee only applies to EUR 1,000.

The capital guarantee is only valid on the date of maturity of the note. If the investor sells the note before the date of maturity, the transaction takes place at market price which can also be below the nominal value.

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New proposals for Capital Requirements Directives

EXTENSION PROPOSED TO DECISION-MAKING POWERS OF GROUP-LEVEL SUPERVISOR ON RECAPITALISATION OF SUBSIDIARY BANKS

The proposals for amendment of the EU Capital Requirements Directives[1] mainly contain suggestions to develop the supervision of subsidiary banks and branches, new regulation on credit institutions' large customer exposures and own funds (so-called hybrids) as well as certain technical issues relating to capital adequacy calculation. Due to the present situation in the financial markets, the proposal also includes qualitative criteria related to liquidity management and clampdowns concerning securitised assets eg relating to capital adequacy treatment.

The purpose of these amendments is not to change the allocation of main supervisory responsibilities of the home and host supervisors. If the Directive is adopted in its present proposed form, the decision powers of the consolidating supervisor, ie supervisor of the entire group, will, however, be extended to the sufficiency of own funds, determination of additional capital requirement and reporting of the whole group of supervised entities. The FIN-FSA and supervisors of many other countries have opposed to the proposal, since it would in practice change the allocation of responsibilities from the present state.

The objective is to give the host supervisor the right to obtain information in context of supervision of systemically relevant branches and the right to participate in joint supervision activities.

Another significant proposal from the FIN-FSA's perspective is granting the consolidating supervisor the right to decide who are allowed to participate in actual supervision activities and meetings of the colleges of supervisors outside crisis situations. The FIN-FSA's position is that the host supervisor should be able to decide for itself on participation in supervision activities and meetings.

The amendments are intended to enter into force on 31 December 2010.

Main responsibilities in supervision of subsidiary banks and branches unchanged

From the Finnish perspective, significant questions related to supervision include new outlines pertaining to the supervision of subsidiary banks and branches. The importance in Finland of these outlines is further highlighted by the planned structural changes of financial institutions and the present market situation.

1 Amendments to the following Directives: Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (recast) and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions (recast).

The intention is not to change the allocation of main supervisory responsibilities between home and host supervisors. The supervisory responsibility for subsidiary banks would continue to be vested with the supervisors in the country of location of the subsidiary bank, even if the subsidiary were part of a group based in another EU country. However, the supervisor of the home country of the entire group, the so-called consolidating supervisor, would supervise for example the total capital adequacy of the entire group together with the host supervisors of the subsidiaries. The primary supervisory responsibility for branches would belong to the home supervisor.

More decision power proposed for consolidating supervisor in relation to adequacy of own funds

At the last moment, significant change proposals have been included in the directive proposal, which are not fully in line with the original objectives of the directive amendments. A significant last-minute change is the proposal to extend the decision power of the consolidating supervisor to cover the sufficiency of own funds (so-called Pillar 2) of the entire group of supervised entities as well as the determination of additional capital requirement and reporting. This change has been justified by keeping supervisory cooperation sufficiently effective. However, many countries have opposed to the proposal, since in practice it would change the allocation of supervisory responsibilities from the present.

The FIN-FSA considers it important that the allocation of responsibility for solo supervision of subsidiary banks is not changed materially and that the supervisory responsibility pertaining to the recapitalisation of subsidiary banks is not transferred completely to the consolidating supervisor. However, it is necessary to give the consolidating supervisor material and more extensive rights in coordinating the process of determining the financial group's capital requirement (Pillar 2). Likewise, it is necessary to remove overlapping supervisory requirements of the host supervisors eg for reporting and supervision of capital adequacy management. It is appropriate that the consolidating supervisor determines these requirements on a centralised basis. Groups of supervised entities have in many contexts stated an express wish that the process be coordinated.

Host country supervisor to have right to obtain information on systemically relevant branches

The objective of the Directive is to give the host supervisor the right to obtain information in context of supervision of systemically relevant branches and the right to participate in joint supervision activities. In accordance with the definition of the most recent Directive proposal, a systemically relevant branch refers to a branch that either has a sufficient market share in the host country (over 2%), significant influence in the payment and clearing and settlement systems in the host country or otherwise a systemically relevant position in the host country in terms of the number of clients.

In the Directive consultation, many countries have emphasised the right of host supervisors to participate in actual supervision efforts and meetings of colleges of supervisors already before crisis situations. The present proposals, however, are not fully consistent with that aim.

Ultimately the host supervisor may decide, whether a branch is to be considered systemically relevant. In making that decision, the host supervisor must take into account the opinion of the consolidating supervisor as well as the statement, if any, of the Committee of European Banking Supervisors (CEBS). However, the consolidating supervisor has been granted the right to decide who participate in meetings and supervision activities. Finland's position is that the host supervisor should be able to decide for itself on participation in supervision activities and meetings of the college of supervisors.

Colleges of supervisors to be made mandatory and written basis for their activities to be compiled

The Directive proposal suggests that it should be mandatory to establish colleges of supervisors for the supervision of cross-border groups. This would also apply to groups operating with a branch-based structure. This is an issue which has been, and still is, strongly promoted by the FIN-FSA. Written principles are needed regarding the tasks of the colleges of supervisors, which should be in line with activities within the CEBS.

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