Nordic Financial Unions

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NFU response to the Liikanen report

Summary of main points

- The Liikanen conclusions contain many positive elements with the potential to create more stable financial markets serving the needs of society, consumers and employees. However, impact assessments are needed before making decisions about regulatory initiatives.
- Such impact assessments should focus on the consequences on investments in growth, welfare and employment as well as the potential impact on finance employees.
- Further regulation in the sector should be balanced in order to avoid further job cuts in the sector. Fewer finance employees risk undermining internal risk management procedures and the service provided to customers.
- While the proposals on incentive schemes for bank management are generally positive it should be respected that remuneration as a principle is an issue outside the scope of the EU in accordance with the Treaty (TFEU, Article 153(5)). Remuneration is an issue for the social partners to decide upon. Employees must be seen as stakeholders that can contribute to a more stable financial sector through for example corporate governance arrangements.
- Increased risk weighting on real estate loans should be proportionate and responsive to national specificities, thereby not putting well-functioning national systems at risk.

General remarks

NFU welcomes the work of the Liikanen group, which is of vital importance against the background of the last decade's rapid growth in the European banking sector's balance sheets and the accompanying expansion of its investment and trading activities. Due to the "too big to fail" problem and the funding subsidy captured by large banks, today's banking environment and banking market structure create an uneven playing field for banks of different sizes. The fact that large universal banks derive benefits from moral hazard creates distortion of competition vis-à-vis smaller competitors – the larger the balance sheet, the bigger the need to back up banking activities with taxpayers' money. The incentive to expand trading activities to gain competitive advantage through support from sovereign funds must be mitigated.

Ring-fencing of banks' trading and investment activities is thus a big step towards making the EU banking sector more sustainable and creating a level playing field. Without the implicit guarantee of insured deposits, the share of trading activities that can be profitably financed will decrease. The likelihood of business expansion within the retail and commercial part of the financial sector will increase.

Ring-fencing could furthermore, if implemented in a cost-effective manner, provide an important step for ensuring the effective application of the elements in the banking union proposal. The prospect of the ESM backing up banking sector assets of 350 % of EU GDP is simply not feasible – it is a sector that not only is too big to fail, but too big to save. As is said in the report, the restriction of speculative risk-taking and the limitation of the use of guaranteed deposits to fund or subsidise significant trading activities facilitate the supervision of the largest and most complex banks within a Single Supervisory Mechanism and facilitate the closer linking of deposit guarantee schemes by limiting the risks insured by those schemes. Prudent risk-taking in the EU banking sector must be promoted, and the risk exposure of taxpayers must be minimised.

Specific remarks

Consequences need to be assessed

Erkki Liikanen explicitly states in the letter introducing the report that impact assessments must be made when proposing concrete legal measures as a follow-up to the report. Impact assessments are needed before making decisions about the extent and form of any regulatory initiatives. Also, further regulation in the sector should be balanced in order to avoid further job cuts in the sector. Fewer finance employees risk undermining internal risk management procedures and the service provided to customers.

Such impact assessments should focus on the consequences on investments in growth, welfare and employment as well as the potential impact on finance employees.

NFU thus finds the lack of analysis of the potential consequences of the proposed reforms as highly problematic. First of all, there is a need to carefully evaluate the costs that a ring fencing of banks' trading activities would entail, both financially and administratively. This needs to be done by taking into account national specificities and differences between various parts of the financial sector in Europe. Second, a scenario analysis is needed. What is the added value of a ring-fencing measure if a bank goes bust, given the already existing legal framework and proposals such as the recovery and resolution rules, as well as the banking union/single supervisory mechanism? Third, the added benefits of ring-fencing in relation to the on-going reform of the EU recovery and resolution framework need to be investigated thoroughly and specified explicitly.

Taking employees into account

It is furthermore paramount that the European Commission in the impact assessments takes account of the employees as a factor where relevant. Employees must be seen as stakeholders in the same way as shareholders, consumers and taxpayers. They are often the first to bear the consequences not only of the problems in the finance sector but also the attempts to come to terms with these problems in the form of new regulation. It has already become evident that new financial regulation such as CRD IV has a clear impact on employment levels in financial companies. This crucial aspect thus has to be included in future impact assessments, along with the consequences of new proposals in terms of increased administration and changes in the working environment. Any changes in the circumstances for banks also mean changes in the circumstances for bank employees.

Moreover, employees provide an excellent opportunity for balanced governance of financial institutions through their knowledge of the day-to-day reality in the companies. They are the link between the companies and their customers and as such integral to include in the impact assessments in the areas of corporate governance and investor protection.

4.2.1 / 5.3 Evaluating the current reform agenda - Capital

In section 4.2.1 and 5.3 further requirements in the area of regulatory capital is discussed with particular focus on risk weights linked to real estate loans. When addressing this area, it is important to take national specificities into account. In the Nordic area, increased risk weighting for mortgage credit risks having a destabilising effect. The Danish mortgage credit model, for example, is an important driver for the real economy while being at the same time both stable and sustainable. Danish mortgage bonds are attractive due to their high security level, leading to low mortgage rates, and the option of prepaying a loan on favourable terms. Any new capital rules applying to this part of the sector should be made proportionate and be responsive to the role that mortgage credit systems play in the national economies.

5.5.5 Strengthening the governance and control of banks

In relation to proposal 5.5.5, it is vital that the composition of boards reflect a greater diversity of views as well as a bigger versatility of independence. Employee board-level representation needs to be strengthened across Europe. Employee perspectives must be taken into account in corporate governance, preferably via direct board representation for trade union representatives or via indirect information and consultation practices and structures.

Versatility of independence in the board is a key factor for responsible corporate governance; something that the Commission itself has pointed out in the staff working document accompanying the Green Paper on corporate governance in financial institutions. Board members elected by the employees should also be trade union members in order to ensure that the person is supported by an effective network and has links to all employees in all parts of the company.

Section 5.5.5 in the Liikanen report also deals with incentive schemes and remuneration. This is an important area to address, as executive remuneration and incentive systems for management can work to destabilise the financial sector through excessive risk taking.

However, NFU has previously pointed out to the Commission as well as other European institutions that the issue of the European legislator regulating remuneration is of particular interest to the Nordic countries, since this regulation may impose restrictions on the right to free collective bargaining.

The social partners can, and must be allowed to, assume the responsibility of sound and sustainable remuneration principles. NFU strongly supports the idea of remuneration policies and practices that are consistent with and promote sound and effective risk management. However, remuneration policies should be left to the social partners to decide upon, since pay is, according to art. 153.5 in the Treaty on the Functioning of the European Union (TFEU), not for the EU to deal with.

This has also been acknowledged in Recital 14 in the European Parliament legislative resolution of 7 July 2010 on the proposal for a directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations (see below).

Recital 14: The provisions on remuneration should be without prejudice to the full exercise of fundamental rights guaranteed by the Treaties, in particular to the provisions of Article 153(5) of the Treaty on the Functioning of the European Union (TFEU), general principles of national contract and labour law, applicable legislation regarding shareholders' rights and involvement and the general responsibilities of the administrative and supervisory bodies of the institution concerned, as well as the rights, where applicable, of social partners to conclude and enforce collective agreements, in accordance with national laws and traditions.

It must thus be made clear that any legal provisions regarding remuneration policies do not apply to remuneration policies and provisions agreed in a collective agreement. Any proposals following the Liikanen report should be aligned with the wordings in the CRD III, where remuneration provisions only apply to persons within a financial entity who has a material impact on the risk profile of the institution.

About NFU

Nordic Financial Unions (NFU) is the voice of the employees in the Nordic financial sectors. We are an organisation for co-operation between trade unions in the banking, finance and insurance sectors of the Nordic countries. Through our eight affiliated unions in Denmark, Sweden, Norway, Finland and Iceland we represent 160 000 members – a vast majority of the employees in the Nordic financial sectors. Together, we work for sustainable financial sectors.

Yours sincerely,

NORDIC FINANCIAL UNIONS (NFU)

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