GLOBAL riskupdate
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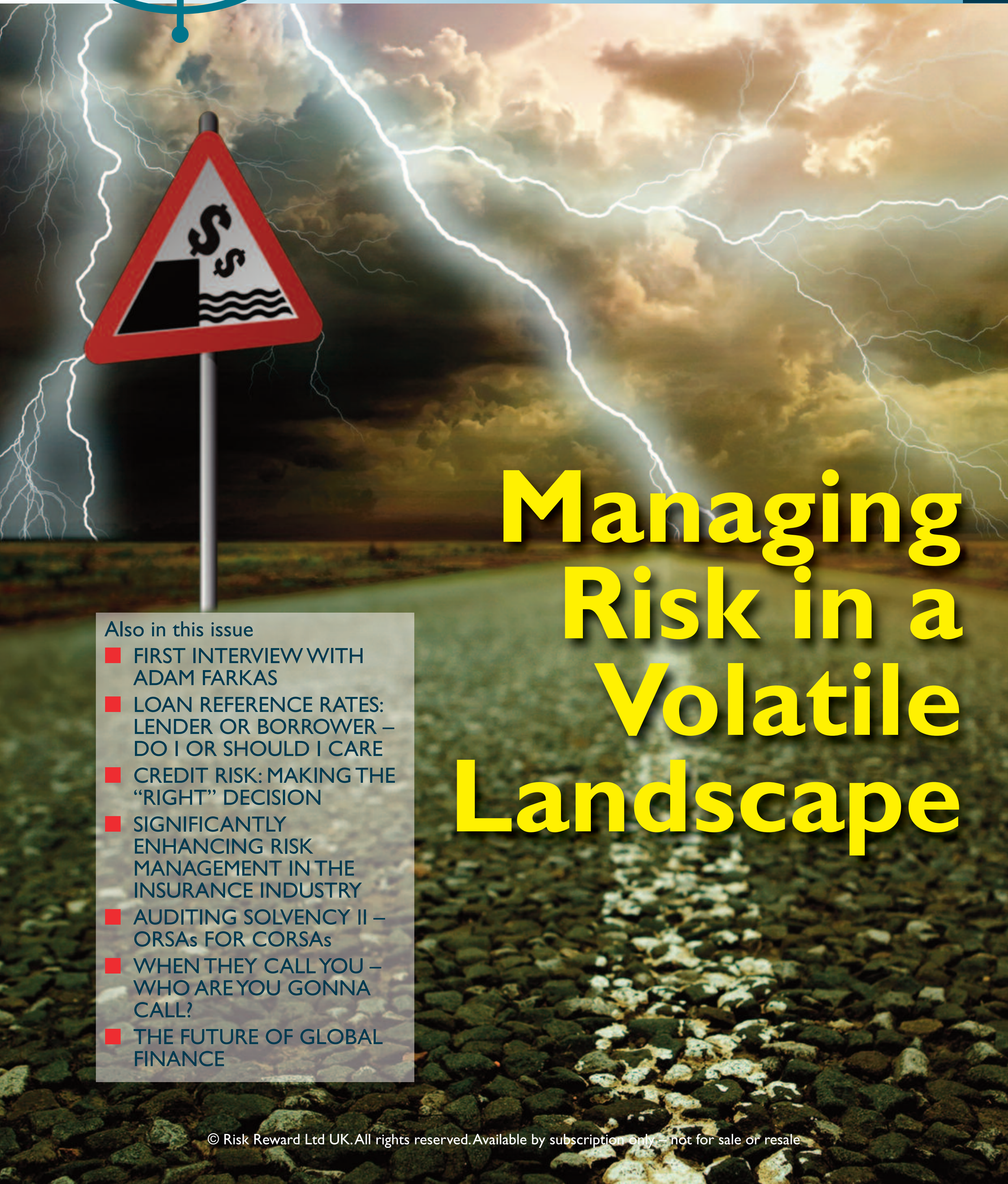

Managing Risk in a Volatile Landscape

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FIRST INTERVIEW WITH ADAM FARKAS, EXECUTIVE DIRECTOR, EUROPEAN BANKING AUTHORITY

Adam Farkas, First Executive Director, was interviewed in London by Dennis W Cox, CEO, Risk Reward Limited. *The European Commission drew up the final shortlist of candidates from which Adam Farkas was selected as Executive Director by the EBA Board of Supervisors on 2 March, 2011. The Executive Director is charged with the day-to-day management and operations of the Authority. He will remain in office for a five-year term and may be re-elected only once. Mr Farkas, who has recently served as Chairman of the Hungarian Financial Supervisory Authority and has extensive financial services experience, undertook his duties as Executive Director of the EBA in mid-April 2011. This is his first interview to industry.*

DWC: Shall I start with the question, generally, what do you consider to be the scope of the EBA?

AF: Three areas will be our main focus:

Rule making/regulatory policy
The EBA has clear powers set out in the Regulation establishing the Authority and they include, among others, the obligation to draft binding technical standards which will be then endorsed by the EU Commission and become directly applicable regulation across Europe. The primary aim of our regulatory efforts is to create a single rulebook and thereby a level playing field avoiding regulatory arbitrage. Regulatory arbitrage was a key problem of the former regulatory architecture.

Oversight/supervision
While national regulators will continue to perform day-to-day supervision of individual institutions, the EBA will undertake regular Risk Assessments (part of which is the EU-wide stress test exercise) and develop methods and means, to ensure that there is a level playing field in the supervisory activities of national authorities. The objective is to create a more homogenous European culture of supervision. In terms of supervisory colleges, our target will be to improve consistency in the functioning of supervisory colleges across Europe. We will also have a role in dispute resolution in case of disagreement among national supervisors and we will be conducting peer group reviews. In our oversight activities, which will also see the involvement of the ESR B for macro-prudential assessments, the EBA may issue recommendations to national authorities if certain developments occur and we get the signal either from the ESRB or through our own risk assessments that there are risks in certain countries, institutions.

Consumer protection activities will be an increasing function of the EBA and we will also be looking at areas in cooperation with the European Securities and Markets Authorities (ESMA) and the European Insurance Occupational and Pension's Authority (EIOPA)

We will try to focus on a few areas. We will not have involvement in minor areas as we have limited capacity and resources for day-to-day consumer protection. While the EBA will be primarily focussed on macro regulation and guidance, there will also be opportunities for the EBA to make micro recommendations regarding specific institutions, groups of firms or industries. These would then be implemented by the relevant local regulatory body. In terms of supervisory colleges, we will target the improvement in the functioning of the colleges, consistently across Europe, developing cross-border groups and conducting peer group reviews. We will look for solutions to ensure that regulatory arbitrage does not exist and this may entail considering business areas which may migrate from the banking sector.

DWC: How will the EBA work with the EU Commission? What do you consider to be the challenges or opportunities?

AF: Specifically regarding the Commission, this is a key relationship for the EBA. A close relationship will be maintained with the key stakeholders including with directors within EU organisations and the EU Commission. Some areas that will be of concern to the EBA will require legislative changes. These will be implemented by the commission and the Council of Ministers. The EBA of course will be available to advise the relevant groups throughout this process.

DWC: Given the developing regulatory status of Basel III, What do you expect to be the key challenges?

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AF: The implementation of Basel 3 in the EU in the form of CRD 4 has not been finalised yet, and the EBA's opinion will have an impact on this. Once CRD 4 is approved, the EBA has the power to draft binding technical standards for its implementation. The standards when drafted by the EBA will then need to be endorsed by the EU Commission. The challenge is that the EBA expects that at least 40 standards will need to be drafted for implementing Basel 3 in the EU. We will also undertake impact assessments and carry out public consultations in the drafting process. There is a reasonable expectation that the deadlines within Basel 3 will be met within Europe. The EBA will do everything within its power to make contributions to ensure that organisations meet the Basel III deadlines. Basel 3 does introduce additional complexity to regulation in terms of capital and approaches. There are not specific challenges for the EBA although it is perhaps cumbersome and the level of complexity does need to be assessed. We do need to be fully prepared. Perhaps the key challenges are to complete the full picture. It is more complex than before but I am not surprised on the level of complexity, although it needs to be carefully assessed.

DWC: What will be the status of the guidelines issued by former bodies i.e. CEBS?

AF: Some of the guidelines will become binding regulatory standards but the EBA will continue to produce recommendations/ guidelines that will not in themselves be legally binding. The legislation based on the Basel requirements will result in technical standards from the former CEBS guidance notes becoming statutory requirements. The matters that will be left from the former guidance will then need to be revised and reissued. The former guidance many need to be varied in some cases.

DWC: Will guidance be issues on hybrid capital instruments, and what will be the impact on firms that have already issued such instruments?

AF: I will not comment on specific instruments. This is an issue which is exercising our attention, and yes the hybrid instruments will be in our standards. The definition of what is considered to be capital (tier 1, tier 2) is an issue, and what instruments can be considered in which category. Once the final version of CRD 4is released, the EBA is mandated with drafting binding technical standards which will provide a challenge for institutions and result in changes. It will not necessarily be certain that all existing hybrids will comply with this new guidance, so institutions may need to find a way to migrate to this new approach.

DWC: What will the EBA's role be regarding competition in the banking industry?

AF: The EBA will have a primary role in ensuring that unfair competition does not exist as a result of regulatory arbitrage. In terms of general competition within the European Banking Industry, this is outside the remit of the EBA which is not a competition authority. The EBA does not have a mandate to run competition procedures for itself. However, if consulted in matters relating to competition, the EBA will be responsive and participate in relevant competition procedures for example answering technical questions.

DWC: Do you think there will be a move of business from banking to non-banking firms? Will the EBA have/perceive any role in such areas?

AF: We are concerned about regulatory arbitrage. This is an area we will keep under review and, if necessary, we will make recommendations or take regulatory initiatives to deal with such matters.

DWC: What do you consider to be the role of liquidity management? Do you need other powers in this or other regards?

AF: Clearly it is not the EBA's role to provide liquidity, as the EBA does not have balance sheet capacity. However, if as a result of our risk assessment or stress testing exercising we identify liquidity issues with groups of firms, countries or parts of the industry than we will in the first instance communicate our concerns to the new European Systems Risk Board (ESRB). We will also receive signals from them in case coordinated action is required by macro-prudential Authorities.

DWC: How will the EBA communicate with its various stakeholders?

AF: Communication from the EBA will take place in a number of forms.

1. Regulation of the EBA requires the establishment of a banking stakeholder group. This is already in place with elected members consisting of the academia, consumer associations, as well as industry representatives). The first meeting of the BSG took place in May.

2. There will also be public consultation; this is where we can invite opinions on common standards, our main channels for this being via our web page.

3. Informal channels/dialogues will also be used as needed with industry representatives and individual institutions to enable us to exchange views and receive feedback.

DWC: Thank you, Mr Farkas, for your candor and frank responses and good luck in your new role and wishes for success to the EBA.

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