ESBG

POSITIONS
PARLIAMENTARY WORKING LUNCH

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THE ESBG NETWORK

ESBG has 25 members in 21 countries that represent 887 savings and retail banking institutions. Of these, 15 members accounting for 610 institutions are in the euro area and 22 members accounting for 747 institutions are in the EU-28.

![ESBG members, 2014](image)

In 2013, ESBG members served 220 million customers through an extensive network of almost 60,000 outlets, 110,000 automated teller machines (ATMs), and had more than 820,000 employees. Approximately 170 million customers, 52,000 outlets and 83,000 ATMs were located in the euro area. ESBG members accounted for 35% of the outlets in their countries.

Overall performance

The financial and economic crises that started in 2008 and the subsequent sovereign debt crisis have affected the performance of the banking sector. In response, authorities and regulators have been changing the regulatory framework and the sector is undergoing a structural transformation. Obviously, ESBG members have not been an exception and have suffered some downturns. As figure 1 shows, growth stagnated since 2009 and in 2013 it decreased in most of the values. The fall in the number of loans (led mainly by inter-banking lending) partly contributed to a significant decrease in terms of assets. Deposits stagnated while non-bank deposits increased. This was probably caused by both the economic slowdown that resulted in lower demand for loans and by the adaptation of members to the new capital regulations.
Around 75% of ESBG member assets, loans and deposits are held by euro area members.

**Assets and loans**

Total assets held by ESBG members in 2013 totalled more than €6.8 trillion, a figure that had slightly decreased since 2009: assets held by ESBG members amounted to €7.1 trillion in both 2009 and 2010, €7.4 trillion in 2011, €7.3 trillion in 2012 and €6.8 trillion in 2013. In real terms, this means a 0.7% decrease in 2010, a 2.9% increase in 2011, a 2% decrease in 2012, and a 5.6% decrease in 2013 (figure 2). However, since 2007, the amount of assets held by ESBG members increased 10%, mainly due to the acquisition by Lloyd’s Banking Group of HBOS in 2009. Out of the €6.8 trillion in 2013 assets, €5.1 trillion are held by euro area members and €6.5 trillion by EU-28 members.

Figure 2 shows the yearly growth rates in real terms of assets and loans over the last seven years (excluding the effect of the acquisition of HBOS by Lloyd’s Banking Group in 2009). The decrease in total loans is mainly driven by the huge decrease in interbank lending since 2008, although in 2012 and 2013 non-bank loans decreased as well.

Through 2013, total loans awarded by ESBG members amounted to almost €4.4 trillion, which represents a decrease in real terms of 5.6% from 2012 (€4.7 trillion). This followed the decrease of 6.7% in 2011, which followed the small negative growth during 2010 (0.7% decrease) and the decline in 2009.

The amount of bank loans decreased 6.6% in 2013, 10.4% in 2012 and 33% since 2008. Given the large share of non-banking loans in the total amount of loans and also, in part, on the asset side of the balance sheet, assets, loans and non-banking loans follow roughly the same trend. While in 2007 and 2008 non-bank loans increased more than 5%, the effect of the crisis in 2009 made growth rates fall into negative figures, decreasing 1.3% (and so too did assets and total loans). However, in 2010, ESBG members reacted well to the environment and non-bank loans grew slightly (1.1%), which led to a stagnation of assets and total loans (-0.7%).
The adaptation to the new legislation, including the process of deleveraging in which banks must engage to comply with it, can be seen, for example, in 2011, when total assets grew by 3% while loans decreased by around 1%. In 2012, due to reduced demand for loans and stricter regulations and capital requirements, growth was again negative across the board, especially in the case of loans. This trend continued in 2013 when non-bank loans decreased by 4% and total assets by 5%.

ESBG members are savings and retail banks committed to the local economy and their business model is oriented towards the needs of the local population. Out of the €4.4 trillion of loans granted by ESBG members in 2013, 84% (€3.7 trillion) was awarded to non-financial corporations (figure 3). Out of these non-bank loans, 54% were for individuals (consumer loans, housing loans, etc.), 40% for companies (60% for SMEs and 40% for large corporations) and 6% for governments and public authorities. In the case of loans to companies, savings banks specialise in loans to SMEs. Figures show that although loans to SMEs were in smaller amounts, their combined total was still higher than that of loans to large corporations, which means that the number of loans to SMEs is much higher than the number of loans to large corporations.

Compared to the rest of the sector, it can be seen that the ratio of total loans as a percentage of total assets (figure 4) is higher for ESBG members than for the rest of the banking sector. Although the decrease in the number of loans seen above has made the ratio decrease since 2007
and the gap with the whole sector narrow, in 2013 the difference is 6 percentage points (pp). The higher ratio of ESBG members shows that members use greater share of their assets as loans than the rest of the sector, which supports the fact that savings and retail banks are committed to the real economy.

As figure 5 shows, the level of non-performing loans (NPLs) increased from 2006 to 2012. This resulted in an increase of the share of NPL in relation to total loans, from slightly more than 2% in 2006 to higher than 7% in 2013 for the whole euro area and EU-28 banking sector. ESBG members maintained their NPL levels lower than the EU-28 and euro area banking sectors, mainly after 2008 when NPL levels started to increase due to an economic situation in which more borrowers were not paying back, which explains as well some of the reduction in loans granted by ESBG members. Members are being more prudent with their clients. In comparison with the rest of the sector, even though ESBG members have a higher loans to assets ratio, their NPL ratio is still lower than the rest of the sector.

**Figure 4: Total loans as % of total assets**

![Graph showing total loans as percentage of total assets for ESBG and EU-28 (ECB) from 2007 to 2013.](image)

**Figure 5: Non-performing loans**

![Graph showing non-performing loans as a percentage from 2006 to 2013 for ESBG, Euro area, EU-28.](image)

**Deposits**

In 2013, deposits held by ESBG members amounted to €4.2 trillion, which represents a very slight decrease from previous years: deposits totalled €4.3 trillion in 2012 and €4.35 trillion in 2011. In
2013, €0.8 trillion were deposits by other banks and €3.4 trillion by non-banks. Growth in real terms is shown in figure 6. Between 2011 and 2013 growth in total deposits has been negative, decreasing 0.3% in 2011, 2% in 2012 and 0.8% in 2013. As with loans, this negative growth was mainly due to the fall of the interbanking market, with deposits from other banks decreasing 7.8% in 2009, 9.7% in 2010, 3.2% in 2011 and 7.5% in 2012 and 2013. On the other hand, non-bank deposits stagnated, increasing by only 0.5% in 2011 and 2012 and by a 0.75% in 2013.

The main depositors at ESBG members are individuals (figure 7). They account for 58% of total deposits. More generally, deposits by banks account for 19% of total deposits and 81% of these are deposits by non-banking corporations. Of this 81% (€3.4 trillion), 81% are deposits by individuals, 14% by corporations and 3% by public authorities.

When comparing the amount of non-bank deposits to total assets, it can be observed that for the case of ESBG members the ratio has been steady since 2008, with a slight increase in 2013 due to the fact that, as seen above, the amount of assets decreased but also because non-bank deposits increased. For the entire EU-28 banking sector, the evolution is quite similar to that of ESBG members, at only 11pp higher.
Loans-to-deposits ratio

The ratio of loans-to-deposits increased gradually between 2006 and 2010 for ESBG members and decreased sharply since 2011, mainly due to the reduction of the number of loans. On the other hand, since 2008 the ratio decreased gradually for the whole EU-28 banking sector (figure 9). Since 2009 ESBG members maintained a higher ratio than the rest of the industry in the EU-28. The reduction of the ratio observed since 2011 is due to the new banking regulations (LCR liquidity ratio in Basel III), which are inducing banks to reduce their loans-to-deposits ratio to a figure close to 100%.
Market shares

ESBG members hold 16.5% of the total MFI\(^1\) assets in the euro area and approximately 15% of those in the EU-28. In the 21 countries where ESBG members operate, ESBG members hold 16% of total MFI assets.

In terms of loans, the ESBG presence is slightly greater: 19.5% of loans by MFIs in Europe (in countries where members were present), 20.3% of loans in the euro area, and 19% in the EU-28. But members are most relevant to non-banks (i.e. individuals, companies and governments), granting 23.5% of all credit institution loans in the euro area.

In terms of deposits and non-bank deposits, ESBG members’ market presence is similar. Members hold 19.7% of deposits in the countries where they are present. Members hold 20% of deposits in the euro area and 18.9% in the EU-28. In terms of non-bank deposits, market shares are much higher. Members hold 23.4% of total credit institution deposits in the euro area.

Maps 1 and 2 show the individual market share in terms of non-bank assets and deposits held individually by each ESBG member in its own country. Individual market shares range from approximately 70% to 4%. On average, ESBG members account for 17% of assets, 19.5% of total loans and deposits, and 23.5% of non-banking loans and non-banking deposits. These figures show the focus and the strong position that members have with retail customers.

Map 1: Market shares of non-bank loans awarded by individual ESBG members, 2013

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\(^1\) Monetary financial institutions form the money-issuing sector of the euro area. They include (i) the Eurosystem (ESCB), (ii) resident credit institutions (as defined in EU law), (iii) all other resident financial institutions whose business is to receive deposits and/or close substitutes for deposits from entities other than MFIs and, for their own account (at least in economic terms), to grant credit and/or invest in securities as well as electronic money institutions that are principally engaged in financial intermediation in the form of issuing electronic money, and (iv) money market funds, i.e. collective investment undertakings that invest in short-term and low-risk instruments.
In general, indicators show that after bottoming out in 2009, ESBG members recovered and put their return and efficiency ratios back on track, although they have not yet recovered their pre-crisis levels.

In terms of return-on-assets (RoA) (figure 10), ESBG members suffered a large decrease in 2008 and 2009, when it bottomed out. In the years after, it recovered slightly, reaching in 2012 the same level as 2008 but decreasing 0.25pp in 2013 to stay at 0.47%.

Figure 11 shows the evolution of the average return-on-equity (RoE). As with RoA, ESBG members’ RoE decreased due to the crisis between 2007 and 2009. It stagnated between 2009 and 2011 and increased in 2012 to reach 9%. In 2013 it decreased by 3pp to remain at 6.3%.
On the other hand, as figure 12 shows, the cost-to-income ratio remained stable over the period. Although the average for the whole EU-28 banking sector remains higher than that of ESBG members, the gap has been reduced. In 2013 the ESBG average was 61% while the whole sector had an average of 65.3%. ESBG members still have a lower ratio, which means that they are slightly more efficient.

**Figure 12: Cost-to-income ratio**

Leverage ratio

The evolution of the leverage ratio, or the ratio between assets and equity, has been almost identical since 2009 for ESBG members and the whole EU-28 banking sector. Comparing it with pre-crisis levels, the ratio decreased substantially, stagnating at around 20 between 2009 and 2011 and decreasing slightly in 2012 and 2013, when the ratio was 16.3 for ESBG members and 17.25 for the whole EU-28 banking sector. This decrease indicates that banks have switched their way of financing to more internal and less risky, by doing so with equity instead of other means. This is partly caused by the deleveraging process of the economy and by the new legislation in terms of capital requirements.

**Figure 13: Leverage ratio**
Ready to comply with the new capital requirements

The Basel III framework, transposed via the Capital Requirements Directive, will establish new minimum capital requirements. Figure 14 shows members increased capital reserves by increasing the Tier 1 capital and capital adequacy ratios. The new rules set a core equity Tier 1 ratio of 4.5% plus additional Tier 1 of 1.5%. This can be complemented by up to 5% of additional buffers, which would render a Tier 1 maximum of 11%. Members’ average was above 11%: their 2013 average Tier 1 capital ratio was 15%, 1.1pp more than in 2012 and 1.85pp more than in 2011. Members also increased their capital adequacy ratio (the ratio of Tier 1 and Tier 2 capital to risk weighted assets) between 2009 and 2013, reaching almost 18%.

![Figure 14: Tier 1 capital and capital adequacy ratio, ESBG average](image)

Infrastructure and payments

As stated above, in 2013, ESBG members employed more than 820,000 people and operated through an extensive network of almost 60,000 outlets and 110,000 ATMs, which is equivalent to one ATM per 5,000 inhabitants on average in the countries with ESBG members and to one ATM per 2,000 ESBG member customers.

The number of points of sale (PoS) was 2.5 million in 2013, which is equal to one PoS owned by an ESBG member for every 220 inhabitants on average in the countries with ESBG members and one PoS per 90 ESBG customers.

The number of banking outlets has maintained its decreasing trend due to the increasing use of new technologies that make banking operations reachable through channels other than face to face. ESBG members own around 30% of the banking outlets in Europe. Following the general trend in Europe, in 2013 the number of ESBG members’ outlets decreased 5.8%, following decreases of 4.4% in 2012 and 3.7% in 2011. The number of ATMs fell by 3.6% in 2013.
This reduction in the number of outlets affected the number of employees. The number of people employed full-time by ESBG members was 820,000 in 2013, which represents a 2.5% decrease compared to 2012 and continues the negative growth trend since 2009. In 2012, ESBG members accounted for 28% of banking sector employees in Europe, while in the banking sector as a whole the trend was similar, decreasing 3.2% in 2013, continuing the decreasing trend since 2009.

On the other hand, the number of customers registered with Internet banking services increased 10% and almost doubled from 2008 to 2013. During the same period, the number of electronic and Internet banking transactions increased as well among ESBG members.

The change in customer behaviour toward increased use of Internet banking and the effect it has had on the number of outlets and employees can also be seen regarding payments. On one hand, the number of ATM withdrawals slowly decreased over the last five years (approximately 1.5% each year) and the number of over-the-counter withdrawals dropped. On the other hand, the number of non-cash money (including debit and credit card) transactions processed by ESBG members increased approximately 7% every year.
LIQUIDITY

Background

Liquidity Coverage Ratio (LCR): After receiving the two reports on liquidity prepared by the EBA, the European Commission is currently preparing the delegated act on the definition of liquid assets for the purpose of the LCR that should have been released, in principle, by 30 June 2014. So far, the EBA’s approach is quite strict with regards to the pool of liquid assets and also does not take into account the economic situation or deleveraging process in Europe. The European Commission is expected to take a more pragmatic approach in a number of issues in its delegated act.

Net Stable Funding Ratio (NSFR): The NSFR is included in the CRR only as a reporting requirement. By 31 December 2015, the EBA will report to the European Commission on the appropriateness of introducing the NSFR in Europe; in particular it will analyse the impact of the NSFR on the refinancing structures of different banking models in Europe. By 31 December 2016, the European Commission will submit a legislative proposal implementing the NSFR; this proposal will be based on the EBA report and on the further work which is currently ongoing at the Basel Committee on Banking Supervision - BCBS (for the record, the BCBS published in January 2014 its revision which seeks to reduce cliff effects on the measurement of funding stability, improves its alignment with the LCR and focuses more attention on short-term volatile funding sources).

State of play

LCR: The proposal of delegated act has circulated amongst the different Directorates General in inter-service consultation, and is still in the process of being adopted. An impact assessment of this proposal has been undertaken by the European Commission. The Commission’s approach seems to have been adapted in response to industry requests as well as to requests from Member States (in particular Denmark) and, most importantly, the ECB. Finally, covered bonds may be included as level 1 with a lower haircut (7%) than previously stated, and banks will be free to use the bonds for as much as 70% of their liquidity buffers, against the 40% of Level 1 under the Basel III rules. As stated above, the requirements for ABS (securitisation instruments) will also be eased. According to some sources the Commission’s plan retains the Basel Committee’s limit of 15% of its required liquidity buffer in Level 2A, while it expands the range of such debt that can be used. Under the latest Basel text, this is limited to residential mortgage-backed securities (RMBS). Collective investment undertakings (CIUs) will be included into the high quality liquid assets (HQLA) which claim to remove regulatory roadblocks from securitised markets. Another open issue is the use of minimum deposits held at central institutions as HQLA; the liquid level of these assets held by the institutions will depend on what type of assets the central institutions invest (otherwise they could be considered as Level 2B); therefore, for the time being, these deposits are not fully recognised as Level 1. The bank’s debt granted by sovereigns may eventually be considered as HQLA since it could be recognised as debt issued by promotional banks.
ESBG position

**LCR:** With regards to the LCR, ESBG has been very critical at the beginning of the process. In our opinion, the LCR has already had negative impacts on the economy and on the way banks do business as it has probably led to a reduction in lending due to the raise in requirements which oblige banks to buy a large amount of non-profitable liquid assets. However, ESBG is of the opinion that the European Commission is now heading in the right direction with regards to the liquidity standards. Furthermore, a more coordinated approach with other initiatives and policies at European level is prevailing - particularly due to the efforts of the ECB. This will be a positive step which may clear further obstacles away and leave the path free for credit growth and recovery in the European Union.

**NSFR:** With regards to the NSFR, ESBG still believes that it is an unnecessary ratio that - if finally applied - would most likely contribute further to the current lending shortage trends. More precisely, in its response submitted in April 2014, ESBG supports the BCBS policy goals of limiting banks’ overreliance on short-term wholesale funding, encouraging banks to better assess funding risk across all on- and off-balance sheet items, and promoting funding stability within the banking sector. Designing the net stable funding ratio as a simple and easy-to-implement tool as suggested by the BCBS goes in the right direction. Despite the fine-tuning of the proposal, in particular through an alignment with the LCR, some concerns remain, such as the potential imbalances that can lead to deleveraging in the short term, the treatment of covered bonds, reverse repos, derivatives, central counterparties and non-financial deposits.

**Key messages**

Although ESBG is optimistic based on the latest developments, some remaining issues deserve to be carefully considered. The Committed Liquidity Facilities (CLF) should not be explicitly priced, but rather be something left to the ECB to decide. The current formulation of restricted CLF with an overly costly price and recognised as Level 2B will not favour the use of these instruments, which can actually be a good instrument in the monetary policy to be used by the Central Bank. Moreover ESBG is concerned about the potential impact of the LCR on specific business models, such as for the decentralised institutions under Institutional Protection Schemes; the minimum deposits held by these institutions on the central institutions should be fully recognised as Level 1 HQLA.
BANKING STRUCTURE REFORM

Background

On 29 January 2014, the European Commission released its final proposal for a regulation on banking structure reform. The final text suggests a stronger model than it was first thought. As with the Liikanen Report, the proposal will solely apply to the 29 largest financial institutions in Europe according to the Commission’s plans. These banks will be banned from engaging in proprietary trading activities. Additionally, further separation of other trading activities, such as market-making activities, could apply when exceeding some metrics following a still unclear process in which competent authorities would have discretionary powers. The proposal includes a derogation clause that will make it compatible with the UK’s Vickers Report; this would not be the case for the German, French and Belgian new legislations.

State of play

Following the Greek Presidency’s plans, the Italian Presidency has already organised two meetings to discuss this file, which shows its willingness to advance the discussion first scheduled for the next European Parliament term. The meeting held on 17 July between Member States and the Commission in the European Council Working Group served to deal with open questions on the proposal, such as the geographic scope of the proposal, the metrics for separation of trading activities and the host/home supervisor concerns. The proposal still faces opposition from main Members States, such as Germany and France. The main concerns raised are the split of market-making activities, the competitive disadvantage for EU banks, and the level playing field in the EU. Furthermore, on 16 June the Council Legal Service released its opinion on the rule concluding that the derogation included in Article 21 of the European Commission’s draft text on Banking Structure Reform, which would particularly apply for the UK Vickers structural reform law, may be illegal, if a number of conditions are not met. The European Commission seems however to be committed to carry on with its plans on banking structure reform.

ESBG position

ESBG does not see the necessity of further structural reforms as the recently passed laws in the banking sector, such as CRD IV, BRRD, Banking Union, EMIR and MIFID are already addressing some of the aims that the banking structure reform proposals intend to address, in particular, the too-big-to-fail problem. Indeed, we miss an impact assessment that takes into account the potential cumulative impact of the mentioned reforms. Furthermore, we are seriously concerned by the negative effects for bank lending and for the economy that could come as a result of the application of this proposal since a future separation of market making activities, securitisation and derivatives trading executed on behalf of clients would significantly reduce liquidity in the markets, increase the cost of lending and subsequently lead to further concentration in the banking sector. This would in fact lead to the opposite effects to those sought by the Commission. ESBG is also of the opinion that the thresholds put forward by the European Commission proposal might be extremely low. In our opinion, these thresholds should not be predefined by the EBA or the legislator. Supervisory discretion should not be constrained and
risk-based thresholds should remain as indicators in the supervisory toolbox rather than triggers. We are also concerned by the lack of clarity of the proposal which may lead to a further increase in uncertainty in the markets. Moreover, we are especially concerned with how the separation could be applied to the savings banks’ business model, in particular, for entities that have an Institutional Protection Scheme (IPS) system. Lastly, we believe that the proposals or laws that already exist at national level are a good way forward and viable alternatives need to be thoroughly taken into consideration for legislative work. Most of them focus on addressing the risk arising from proprietary trading activities, without separating market-making activities.

**Key messages**

Instead of a structural mandatory separation, ESBG considers that it would be more valuable to focus on the implementation of the already existing regulatory proposals and on the strengthening of supervision and risk management. The diversity of European banking business models has proved to be an asset during the crisis, therefore it is key for the European economy to preserve the capacity of savings and retail banking to foster growth through financing households and SMEs.
FINANCIAL TRANSACTION TAX (FTT)

Background

- September 2011: the European Commission proposed an FTT to be implemented in all Member States.
- Autumn 2012: 11 Member States requested enhanced cooperation on the FTT.
- Spring 2014: The Greek Presidency viewed the FTT as a priority file and a basic agreement was reached in the ECOFIN Council on 6 May 2014 among 10 Member States.
- Autumn 2014: The Italian Presidency is expected to maintain momentum on this file as they are also part of the enhanced cooperation mechanism. They are expected to push for completion during its term.

State of play

The negotiations regarding the FTT are primarily done between the 11 Member States that form part of the enhanced cooperation mechanism. The negotiations are behind closed doors but indications are that the scope will be greatly reduced to protect pension funds, government bonds and repos amongst others. This is to no small extent due to the extensive lobbying efforts of the industry as a whole. Member States are divided into two camps. Italy, which is currently presiding in the European Council, is a member of the enhanced cooperation and thus pro-FTT.

ESBG position

ESBG members support the aim to curb short-term speculation and to encourage the prohibition of undesirable market behaviour. However, they do not support a Financial Transaction Tax at EU-level.

The impact on financial activities essential to the functioning of financial markets and to the real economy could be extremely negative. We believe that the following activities will be impacted negatively by the proposed tax:

- the issuance and secondary markets for sovereign bonds;
- the use of derivatives contract for hedging purposes;
- the use of repurchase agreements to provide secured liquidity to the market;
- market-making activities; and
- the use of intra-group transactions for liquidity management and efficient capital allocation within a group.

Key messages

ESBG’s main concern with the current FTT proposal is that, in efficient fixed income markets, such as the markets for government and covered bonds, which are characterised by low spreads
between bid and offer prices\textsuperscript{2}, the tax will be far higher than what can be earned on market making, especially on instruments with short remaining time to maturity. The consequence of the tax will be that market-making will almost cease and the current liquid markets are likely to be transformed into buy and hold markets. As a result market liquidity will disappear or be significantly reduced.

\textsuperscript{2} The spread between bid and offer prices is currently around 0.02\% on German or French government bonds with 1 year remaining maturity. Adding at least 0.2\% FTT will hence mean a significant additional cost for doing a transaction.
MIFID

Background

The Markets in Financial Instruments Directive Review was the occasion to tighten the rules protecting the retail investors when seeking advice from an advisor. In particular, it introduces the concept of independent and non-independent advice, depending in particular on the remuneration model. There was an underlying question of the legitimacy of the inducement model where advisors are remunerated by the manufacturers of the investment products throughout the discussions within the European Parliament and the Council. Ultimately, the presumption that with inducements comes conflicts of interest has led to a ban on inducements in the case of portfolio management, but the current continental model of remunerating financial advice through inducements was ultimately conserved. The legislators acknowledged that the possible conflict of interest it creates can be managed while still allowing for high-quality advice and because of the enormous drawbacks that would result from a full banning as it is witnessed in the United-Kingdom.

State of play

Following the adoption of the final version of the MiFID by the European Parliament on 15 April 2014, the European Commission issued a call for technical advice to ESMA and in particular on investor protection issues. In this call, the European Commission tasked ESMA to define the inducements that can qualify as enhancing the quality of the advice, the only ones allowed under MiFID II. In late-May 2014, ESMA presented its proposals and opened a two-month consultation period for stakeholders.

ESBG position

ESBG considers that the outcome of the legislative process on MiFID II is clear: the legislators decided to give credit institutions a choice on their remuneration model. They can keep their continental model where the infrastructure is financed by inducements, or decide to provide independent advice and remunerate the advisor with client fees. However, ESBG is concerned that level II may threaten this decision as it may inappropriately restrict the number of inducements that respect the criteria of “quality enhancing” in such a way that it would jeopardise the whole inducement model and would prevent institutions from providing the service that they used to provide to their clients. In other words, credit institutions should have a real choice when considering whether to provide independent or non-independent advice, and not between a direct ban model and an indirect ban model. It should be explicitly clear that, besides the access to a wider product range or the provision of advice on an ongoing basis, the access to - and support of – a wide distribution net should be recognised as a relevant quality enhancement criterion in itself.

Key messages

It is paramount that the fact legislators decided to preserve the existing continental model where investment advice infrastructures are financed by inducements received from third-parties is
acknowledged. A ban on inducements would have a direct detrimental effect for the retail investor, as it could have been witnessed in the UK following the implementation of the Retail Distribution Review fully banning inducements: most retail banks no longer offer basic investment advice; instead, they offer private banking services accessible to a small share of the population. Level II of MiFID should not create a situation where it would go against the spirit of MiFID II by overly-restricting the continental model of remuneration until it struggles to exist.
BENCHMARKS

Background

A proposal from the European Commission to regulate the benchmark industry was published in September 2013 and is currently going through the European legislative procedure. Under this proposal, administrators of benchmarks would be regulated and supervised by national competent authorities under the coordination of the European Securities and Markets Authority (ESMA). For critical benchmarks, colleges of national supervisors would be formed. Furthermore, all those who calculate benchmarks or contribute information used in their calculation would be required to tighten up their governance and scrutiny procedures, particularly to prevent conflicts of interest. Also, the data for the calculation of benchmarks, as well as information on what each benchmark measures and its intended purposes, would have to be made publicly available. The proposal goes further and requires banks to assess the suitability of the benchmarks they use before entering into any financial contracts (such as a mortgages) with a customer and to warn customers if the benchmark is unsuitable.

State of play

The benchmark dossier is currently stuck at the European Parliament as it has been given up by MEPs before the European Parliament’s renewal because of a strong divergence in views between the different political groups. In particular, they were unable to agree a compromise on how to deal with smaller indices that do not pose a systemic threat to the financial system and on whether or not ESMA should be in charge of the supervision of benchmarks instead of national authorities. At Council level, the Working Party on Financial Services in the format of attachés and experts continues the examination of the Commission’s proposal during the summer and will continue during the second half of 2014 with the aim of a possible general approach.

Key messages

ESBG welcomes the initiative of the European Commission, as it supports the creation of a common public framework with the aim of strengthening the quality and grounds of trust in indices widely used as benchmarks.

ESBG has, however, some comments on the content and, in particular, the scope, which should correspond to the scope outlined in the International Organization of Securities Commissions (IOSCO) Principles for Financial Benchmarks. ESBG is also worried about the criteria for mandatory participation by contributors to critical benchmarks: forcing submitters to contribute to a benchmark is, in our view, a discriminatory practice and not compatible with benchmarks provided by private institutions on a voluntary basis. ESBG is also concerned that a badly designed regulation may chase away contributors, as they are already in a difficult situation: they receive no benefits from contributing to the production of a benchmark, as the prestige is no longer present and they will have to face suspicions from public supervisors in addition to reputational risks in performing an activity that is on a voluntary basis. The major benchmark providers have already lost a large percentage of their contributors; it is therefore essential that a quality Regulation be adopted as soon as possible.
REVISION OF PAYMENT SERVICES DIRECTIVE (‘PSD2’)

Background

Amendments to the Commission’s proposal to revise the Payment Services Directive (aka: PSD2) adopted on 3 April 2014 under the ordinary legislative procedure by the European Parliament in a first reading are now being reviewed by the Council Working Group under the Italian Presidency.

Key areas

State of play

The Presidency compromise dated 23rd July 2014 includes a number of positive developments, notably: clarification that third party payment providers do not hold funds in connection with the provision of goods and/or services (Art. 4.11), clarification of the definition of authentication “procedures” – i.e. not limited to any single, technology-based procedure, a self-contained description of conditions for payment service providers to access payment systems (Art. 29), clarification that Art. 58 is about “Payment initiation and use of payment account information by TPPs” (and not any longer about “Access to payment accounts”), and clarification that “the third party payment service provider shall not request from the user to provide his re-usable credentials for any purpose”. Furthermore it is stressed that third party payment service providers have to unambiguously identify themselves towards payers, and that consent to execute a payment transaction has to be given by the payer (it may be given by a third party payment service provider who is instructed to initiate the payment transaction – it is inferred by Art. 57.1 and Art. 58.1 that the TPP is instructed by the payer, but such inference should be made explicit).

ESBG position

Areas in which this Presidency compromise retains an approach which holds the potential to jeopardize account holder security are:

- That “Re-usable personalized security credentials shall not be shared” is a much valued advance compared to the Commission’s initial text. Yet the inference still is that users may provide to third parties, including third party payment service providers, their non-re-usable credentials. ESBG stresses anew that the payer should neither be allowed nor enticed to share with any third party the credentials provided by his account servicing payment service provider – not even when issued with a one-time password.

- A fundamental concern remains the distribution of liability and responsibility, and redress, between the account servicing payment service provider and the third party payment service provider. The Presidency’s proposal still places the onus to redress any unauthorized or wrongly executed transaction on the account servicing payment service provider – even though the latter may have no knowledge of the involvement of a third party payment service provider. The recurring, unresolved issue is that account servicing payment service providers are indiscriminately designated as the first point of call for a user problem, even though they might not be the cause of the problem, nor even be aware that a third party has been mandated.
ESBG proposes that 3 scenarios providing for full transparency to users, a fair distribution of responsibility and liability between providers, and an incentive for the latter to perform be incorporated into the PSD2 dispositions:

i. When the payer chooses a non-authorised (i.e. non-regulated, non-supervised) third party payment service provider, the payer must claim redress from either the said third party payment service provider and/or the payee for any loss whether directly or indirectly related to the non-execution or wrongful execution of the intended transaction.

ii. When the payer chooses an authorised third party payment service provider who has not entered into a contractual relationship with the account servicing payment service provider, the latter is only liable towards the payer for non-execution or wrongful execution of an intended transaction for those steps of the transaction which demonstrably are under its own control.

iii. When the payer chooses an authorised third party payment service provider with whom the account servicing payment service provider has a contractual relationship (aka: “sponsors”), the latter will be the first port of call for the payer in case of any issue, and can be liable towards the payer for non-execution or wrongful execution of an intended transaction – provided that both the payer and the third party payment service provider complied with the procedures established and communicated by the account servicing payment service provider.

Furthermore, Art. 87a.1.b proposes that EBA develops “common and secure open standards of communication for the purpose of authentication, notification and information between account servicing payment service providers and third party payment service providers, to be issued two years from the date of entry into force of the Directive, and be updated on a regular basis as appropriate”. The Commission’s view that “the standards to be defined should be universal and not technology driven and should apply to all actors concerned” should become part of the PSD2. Furthermore the potential time and content hiatus between the obligation for credit institutions to implement the ECB SecurePay Recommendations for Internet payments and the obligation for payment service providers to transpose the EBA dispositions must be addressed.

- Under any scenario providers must remain at liberty to recover their costs (as well as a rate of return). Where costs cannot be recovered from payers (due to existing legislative constraints) then providers may not be prevented from recovering them from other parties in the chain.

**Key message**

European legislators should be wary of creating a “European exception” with respect to third party payment service providers. The latter have not been an issue for legislators anywhere in the world, enshrining them into European legislation will potentially both threaten the security and trust in payment systems, and increase the cost of the system. Should they though be recognised, then it may not be that they (or any other third party) has access to personalized security credentials (even one time ones) of account holders.
CARD INTERCHANGE REGULATION PROPOSAL

Background

This proposal aims at capping interchange fees that may be charged by card issuers to acquirers of debit and credit card transactions, and to standardize a number of the business rules set by card schemes.

State of play

The European Parliament adopted on 3 April 2014 in a first reading a series of amendments to the Commission’s proposal. In essence, these amendments on one side drastically lower the permissible ceiling for debit card interchange (to a maximum of 7 cents for any transaction above EUR 35,00) and change the scope by bringing in commercial cards. Furthermore the Parliament proposes that (in order for processing entities to ensure that their system is technically interoperable with the systems of other processing entities) the European Banking Authority (EBA) develops “draft regulatory standards establishing requirements to be complied with by payment systems, payment schemes and processing entities”.

ESBG position

ESBG notes that the business rules section of the Regulation proposal borrows substantially from the banking payment industry’s 2006 SEPA Cards Framework (“SCF”), market transposition of which proved impossible through self-regulation. ESBG supports this part of the regulatory initiative, as adoption of such business rules will foster transparency, consumer-decision making capabilities, and competition (unless there is an attrition of providers). However ESBG has to express deep concerns over the following dispositions:

- There is no justification for bringing commercial cards in scope of the proposed Regulation. As the definition evidences, “commercial cards” result from a contract between professional counterparties who are deemed to understand their dealings, hence the consumer protection dimension that motivates most of the proposed Regulation’s dispositions does not apply. Furthermore commercial cards are used first and foremost for the ancillary services they enable, such as accounting and budgeting, VAT management, etc… Finally regulation of 4-party commercial cards would hand a de facto monopoly to a 3-party provider exempted from the Regulation.

- Whilst ESBG again values confirmation that interchanges for card-based transactions are permissible, stressing again that no Court in the EU or elsewhere ever found that card interchange fees restrict competition by object, ESBG must point out that the new, proposed lower cap of “the lower amount of 7 eurocents or 0,2% of the value of the transaction” does not rest on any market assessment and will trigger effects contrary to those pursued by the Regulation proposal. ESBG proposes to revert to the Commission’s original proposal (“…payment service providers shall not offer or request […] a per transaction interchange fee or other agreed remuneration with an equivalent object or effect of more than 0,2% of the value of the transaction”).
- The Parliament’s position also penalizes providers who’d wish to displace cash for transactions of less than 35 EUR (which would yield an interchange of less – often much less – than 7 eurocents). The Parliament’s cap either forces cross-subsidization of such transactions by higher value transactions (in effect only inviting the traditional incumbents into this critical market segment) and/or a stand-off in innovation and the use of cash. ESBG proposes that individual debit and credit card transactions of a value up to 35 EUR can be subject to an interchange fee of up to 7 eurocents per transaction.

- The Parliament proposes that the interchange caps apply within 1 year, obviously an average between the 2 months and 2 years initially proposed by the Commission. Because of the overwhelming proportion of national transactions, ESBG stresses again that a 2 year and even more so a 1 year timeline to transpose is too short to enable payment service providers to depreciate investments in infrastructure which have just been made, or which will have to be made to comply with the Regulation. A 4 year timeframe would allow for such depreciation.

- Regarding work to be done by the EBA, whilst ESBG assuredly supports the formulation and adoption of common standards and emphasizes that the card industry already rests on a significant body of standards, be they ISO or open industry standards, implementation specifications up to now had been developed to meet the needs of most European users, i.e. within national borders. Any harmonisation initiative would have to contend with 3 challenges: a) build on the existing body of standards, b) refrain from creating incompatibilities with international i.e. global standards, and c) allow for an implementation timeline which acknowledges the length and diversity of the card transaction chain (recognising that e.g. the retail sector generally depreciates terminals – 7 million of them over the EU - over a longer period than the 4 years referred to above, e.g. for issuer the potential obligation to re-issue some 500 million cards).

**Key message**

Whilst the business rules section of the Regulation proposal can be supported (taking into account though the remark made with respect to the work to be entrusted to the EBA), the interchange cap for debit card transactions must remain as proposed by the Commission. Furthermore commercial cards should not be imported into the scope of the Regulation.
DATA PROTECTION REGULATION PROPOSAL

Background

The purpose of the January 2012 General Data Protection Regulation proposal is to review and adjust the existing centrepiece of EU legislation on data protection, i.e. Directive 95/46/EC in order to acknowledge rapid technological developments and contribute to building trust in the online environment.

State of play

The 12 March 2014 European Parliament legislative Resolution brought some improvements to the January 2012 General Data Protection Regulation proposal, yet significant concerns remain, which if unaddressed will prevent the revised legislation to meet the expectations and requirements defined below.

ESBG position

ESBG welcomes the review underway of the EU legal framework on data protection. This review matters for 2 reasons:

• First, customers in particular consumers deserve certainty as to how the data they submit is processed, and their rights when they feel there is an issue.
• Second, suppliers of goods and services need certainty as to how they may exploit the vast amounts of data they can have access to.

Balancing customer expectations and supplier requirements is one of the challenges of the review process. Another is to acknowledge that in an increasingly digital world on one side borders tend to become blurred, on the other it is imperative not to place European companies at a competitive disadvantage compared to non-European market participants. Finally the review must acknowledge that financial service providers (including credit and payment institutions) are compelled by legislation and supervision to hold customer data: the outcome of this review cannot be that compliance with these obligations becomes more onerous.

ESBG urges the Council of the EU to take into account the following considerations:

• Requirements of national banking and financial supervision authorities on financial institutions to process data for fraud prevention must be covered by the legislative text.
• The lawfulness of processing data from public registers, lists, documents or records must be acknowledged – as would be processing within a “group”.
• The usefulness of profiling to both comply with legislation, mitigate risk and improve products and services must be acknowledged.
• The requirement for explicit consent of the data subject is not realistic, it should be replaced by “unambiguous”.
• The right to be forgotten should be adjusted to the duties to be carried out by financial institutions.
• The right to data portability should apply to data processing by electronic means within social networks or online databases. Due to the sensitivity of the data entrusted to and held by financial institutions portability should not apply to them.

• For breach notification a distinction should be made between unrelated, individual events, and events which would point to a more systemic issue – the latter having of course to be notified.

• The requirement to appoint a data protection officer should be implemented on a risk-based, proportionate basis.

• For international data transfers public interest or legitimate interest by regulated institutions as defined in third countries should also be recognised.

• Setting penalties must remain the competence of national supervisors. The size of the penalties should be comparable to infringement of similar nature, and not aligned – as proposed – with fines for anti-competitive behaviour – which are based on a completely different reasoning and body of law.

Key message

This legislation will be substantial in shaping the future of the digital economy in the EU. Therefore it is essential that consumer protection and supplier enabling matters are well balanced, in addition the specific obligations already imposed on the financial sector must be recognised in order not to increase friction and societal costs.
LONG-TERM FINANCING

Background

The debate on Long-Term Financing (LTF) has started at global level within the different international institutions (in particular OECD, IMF, FSB) under the impetus of the G20. During the first G20 Finance Ministers’ and Central Bank Governors’ meeting during Russia’s Presidency, held on 15-16 February 2013 in Moscow, the G20 cited long-term financing as crucial for innovation financing, research, and future infrastructure. As a result, the main objective of fostering and increasing the capacity of banking institutions to channel savings to long-term investment projects was established by the G20 members.

The debate took a European perspective with the publication of a consultation paper by the European Commission: “Green Paper on the Long-Term Financing of the European Economy” followed by a Communication on 27 March 2014 with an underlying idea that bank lending will durably shrink and that this change should be assisted rather than fought.

State of play

The Italian Presidency has indicated that the Long-Term Financing dossier will be one of their priorities during their 6 months leading the European Council. It will base its actions on the Communication released by the European Commission and will select and push forward some of the foreseen initiatives at short and long-term. In particular, it will discuss with the European Commission on ways to increase the lending to the real economy and will have a specific and trans-sectoral focus on the question of the securitisation of SME lending. It will furthermore closely follow the activities of the ECB in that respect.

ESBG position

ESBG does not agree with the approach which consists of encouraging one model against another – capital market funding vs. bank funding – to address the issue of the decrease in bank lending. This is not acceptable as it is not in the interest of the economy. The role of banks is to provide long-term financing and to protect the depositors. The other intermediaries’ (such as asset managers) role is not to protect depositors but to provide returns. If the banks are not taking the risk for the transformation of deposits into long-term investments, then the saver is directly taking the risks. The banks’ role is to assess the risks, while institutional investors are not able to do so currently.

With regards to the access to finance for SMEs, these companies are not a good target for capital markets as 90% of SMEs have less than 5 employees. These SMEs are best served by the banks as they have the contact with local communities and the deposits that can be transformed into adequate lending. However, ESBG welcomes the Commission’s intention to support high quality securitisation products. Exploring a preferential treatment for these products emerges as an important work stream in the short term and the industry stands ready to work with the authorities on it.
ESBG is currently developing concrete proposals in the area of LTF which will be shared with the legislators as soon as they are available.

**Key messages**

ESBG is convinced that the envisaged structural change is not in the interest of the European economy which is not adapted to capital market-based financing models. Thus, we recommend rethinking the long-term financing approach in order to create a banking regulation framework which enables banks to fulfil these tasks where they have the most expertise: lending to the real economy.
ANTI-MONEY LAUNDERING

Background

In June 2007, the Financial Action Task Force (FATF) adopted the Guidance on the Risk Based Approach (RBA), which includes guidance for public authorities and financial institutions, to combat money laundering and terrorism financing. This was the culmination of extensive consultation between private and public sector members of an Electronic Advisory Group established by the FATF. After on-going international consultations the FATF adopted the RBA Guidance for the money services business in June 2009. The purpose of the Guidance is to: i) support the development of a common understanding of what the RBA approach involves; ii) outline the high-level principles involved in applying the RBA approach; iii) indicate good public and private sector practice in the design and implementation of an effective RBA approach.

On 5 February 2013, the European Commission published a proposal for a Fourth Anti-Money Laundering Directive (4th AMLD), which fully takes into account the FATF Recommendations from 2012 and goes even further in a number of fields. It also takes into account specificities related to the political and legal nature of the European Union and its single market.

State of play

In March 2014, the FATF organised a meeting of the Private Sector Consultative Forum to discuss the implementation of the anti-money laundering and counter-terrorist financing (AML/CFT) measures set out in the FATF Recommendations from 2012. The FATF sought feedback on revised guidance for applying the RBA to the banking sector. These discussions were key to developing a common understanding of the RBA, such as how it applies to both private sector stakeholders and at national level.

On 18 June 2014, the Permanent Representatives Committee (COREPER) agreed on the Council’s General Approach on the 4th AMLD, which had been completed by the Greek Presidency some days before. Furthermore, Member States agreed on the draft regulation on the transfer of funds which is supposed to replace the current regulation 1781/2006. In addition, COREPER gave a mandate to the Italian EU Council Presidency to enter trialogue negotiations with the EU Parliament and the European Commission. Negotiations are expected to start in autumn 2014.

ESBG position

Regarding the 4th AMLD, ESBG welcomes the fact that the proposal introduces registers with information on beneficial ownership on companies, which will support the promotion of greater transparency concerning information on corporate ownership structures and beneficial owners. Furthermore, ESBG welcomes the introduction of a register listing the names of Politically Exposed Persons (PEPs) as it would represent a substantive tool for financial institutions to discharge their customer due diligence obligations independently of any lists bought from commercial providers.
Nonetheless, ESBG is of the opinion that further clarifications with regard to processing AML/CFT and a clear and consistent legislative framework for the obliged entities is necessary in order to tackle possible inconsistencies between EU data protection legislation and requirements of the 4th AMLD. Moreover, ESBG believes that a list of third-countries which are deemed equivalent in their AML legislations is of great importance in order to avoid confusion because of individual evaluations of these third countries. Finally, ESBG is of the opinion that clarification is needed with regard to the obligations of real estate agents. Thereafter, customer due diligence measures should only be applied by those who are involved in the financial transaction associated with the acquisition of a property.

**Key messages**

ESBG believes that the 4th AMLD faces the challenge of convergence between the FATF and the BCBS guidance note on the RBA. Individual country’s national laws could lead to an overlap of the two so that banks would implement one method over the other. Therefore, ESBG calls for ensuring that the BCBS’s guidance note supports the implementation of the FATF standards at national level without modifying those standards.
## ESBG Members' Key Figures, End of 2013

### Data at the End of 2013 Accounting Year

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