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THE SUPERVISION OF MIXED FINANCIAL SERVICES GROUPS IN EUROPE

by Frank Dierick

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by Frank Dierick [1]

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EXECUTIVE SUMMARY

Financial services are often offered through group structures. To avoid regulated entities circumventing prudential rules using such structures and to address group specific risks, individual supervision has to be supplemented by group-wide supervision. For financial groups active in the same business area, the European regulatory framework for such supervision has already existed for some time. With the adoption of the Financial Conglomerates Directive in December 2002, a supplementary layer was created to also deal with the supervision of mixed financial services groups. Member States have to transpose the Directive into national law by August 2004.

Such groups, in particular those that combine banking and insurance, have become increasingly important in Europe over time. They often result from cross-sectoral mergers and acquisitions, which are typically domestic in nature. The majority of large banks and insurance companies in the European Union (EU) are now part of a wider banking and insurance (bancassurance) group. Although the groups can assume quite complex structures, a useful typology for analysing them starts with four basic models, each having its own strengths and weaknesses: the integrated model, the parent-subsidiary model, the holding company model and the horizontal group model.

Several factors explain the growing importance of structural cross-sectoral capital linkages, including the opportunity to realise efficiencies of scale and scope and diversification effects to reduce the volatility of cash flows (thus reducing the probability of financial distress and the need for external financing). Additionally, managers may want to realise their own objectives (e.g. increased status and remuneration), which do not necessarily coincide with the shareholders' best interests. Conglomeration also poses some clear risks: intra-group transactions create opportunities for regulatory arbitrage, moral hazard and the spreading of difficulties across group entities. Complex group structures may reduce transparency, and there are concerns about conflicts of interest and the abuse of economic power.

The EU rules which address some of these concerns have to a large extent been inspired by earlier work of the Joint Forum, to which the international organisations of banking, insurance and securities supervisors contribute. They are generally intended to introduce a supplementary layer of supervision on regulated group entities. Capital adequacy, and in particular the need to address the multiple use of the same capital by different group entities, is a major issue. Other areas of attention are intra-group transactions, large exposures and organisational requirements. The coordinating supervisor plays a crucial role in this supplementary supervision.

The regulatory and supervisory structures, at both the European and the national level, have to cope with the growing cross-sectoral linkages, in particular through conglomerates. Information and cooperation arrangements have been set-up, such as joint committees, memoranda of understanding and mutual board representation. Some countries have gone further by adopting a single, integrated financial supervisor.

By way of comparison, the treatment of financial conglomerates in the United States is discussed. Although the United States has traditionally had a strict separation between the different financial sectors, opportunities for conglomeration were enhanced through the adoption of the Gramm-Leach-Bliley Act. However, the US regulatory framework demonstrates some key differences to the European one in terms of, for example, organisational requirements, the role of credit institutions in the group, and the role of the lead-supervisor/coordinator. Finally, the paper concludes by highlighting some open issues related to supervision and financial stability.

INTRODUCTION

Financial companies are increasingly moving into each other's traditional core business areas and one way of doing so is through financial services groups. Some of these groups, called "financial conglomerates",[1] are active in several business areas such as banking and insurance. These groups pose certain risks which are not adequately addressed by the sectoral supervisory framework. In order to tackle this, the Financial Conglomerates Directive[2] was adopted at the European Union (EU) level. This paper investigates in more detail the various issues related to the emergence of such conglomerates.

Section 1 reviews the data on the development of cross-sectoral capital linkages, in particular between the banking and insurance sectors. Such linkages are a necessary, but not sufficient condition for the existence of a financial conglomerate. *Section 2* therefore examines the conditions required for a financial conglomerate to exist under the Financial Conglomerates Directive. A characteristic of such groups is that they are active in several business areas. *Section 3* thus identifies the key characteristics of the main business areas, which sheds some light on the motives for conglomeration and the risks involved, as discussed in more detail in *Section 4*. Conglomerates can adopt very complex corporate structures, which are often a combination of different basic models. *Section 5* reviews four such basic corporate models and identifies the related key concerns. This is followed by a discussion of the supervision of financial services groups. While *Section 6* presents a broad outline of such group supervision, *Section 7* addresses some major, specific supervisory issues. Financial conglomerates have to be dealt with through adequate supervisory structures, both at the national and the international level, and the different models adopted in practice are presented in *Section 8*. Other jurisdictions are also confronted with financial conglomerates and *Section 9* compares the situation in the EU with that in the United States. *Section 10* reviews some open policy issues and *Section 11* contains the paper's conclusions.

1 Annex 1 contains a glossary which explains the technical terms used in this paper.
2 Annex 2 provides an overview of all key directives referred to in this paper together with their full references.

1 THE DEVELOPMENT OF CROSS-SECTORAL CAPITAL LINKAGES

Because of demographic developments, deregulation, increasing competition and innovation, financial companies are increasingly moving into each other's areas. Banks[3] are now acting as insurance agents or brokers by selling insurance policies through their branch networks, insurance companies are selling insurance policies that have all the characteristics of investment products, and many commercial banks have moved into the securities business. In Europe the combination of banking and insurance has become increasingly popular. Apart from banks developing insurance activities ("bancassurance" or "bankinsurance" in the narrow sense), insurance companies also develop banking activities ("assurfinance") or holdings combine both ("allfinanz"). These cross-sectoral strategies can take different forms: distribution agreements, joint ventures, the establishment of own subsidiaries or mergers and acquisitions (M&A) involving already existing companies. This paper concentrates in particular on bancassurance groups as they are a common form of financial conglomerates in the EU.

1.1 CROSS-SECTORAL MERGERS AND ACQUISITIONS ACTIVITY

Total M&A activity in the banking and insurance sectors[4] involving EU undertakings reached around €950 billion in the period 1990-2003 (see Table 1). Around 60% of this activity concerned same-sector, same-country deals, pointing to the difficulties that continue to exist in establishing financial groups that cross existing geographical and sectoral boundaries. Given the fact that, in terms of total assets, the banking industry in the EU is significantly larger than the insurance sector, it is not surprising that the value of banking deals outweighed those in the insurance sector by a factor of more than two. Cross-border deals were almost evenly split-up between those involving EU parties on both sides and those involving a non-EU party on one side.

The value of cross-sectoral deals in the same period stood at around €130 billion, with insurers showing more activity than banks as acquirers. However, it should be noted that this finding is very much influenced by the takeover of Dresdner Bank by Allianz, a deal which alone totalled more than €22 billion. The value of purely domestic deals is in relative terms somewhat higher for inter-sectoral transactions than for intra-sectoral ones, but the difference is perhaps is not as great as one would expect given the additional layer of complexity that results from combining companies from different financial sectors in different countries. This may at least partly be explained by the fact that no minimum threshold was applied to the M&A data in terms of the stake acquired in the companies. Hence, the data cover purely financial shareholdings as well as long-term strategic investments made with the intention of developing business synergies. Obviously, in

3 In this paper the terms "bank" and "credit institution" are used interchangeably.

4 The M&A data discussed in this part were retrieved from SDC Platinum (Thomson Financial). The banking sector is defined in such a way that it covers credit institutions, commercial banks, bank holding companies, mortgage banks and mortgage brokers (SDC Platinum codes). The EU figures do not include the new Member States that joined on 1 May 2004.

Table 1 Value of M&As involving credit institutions and insurance undertakings in the EU (period 1990-2003)

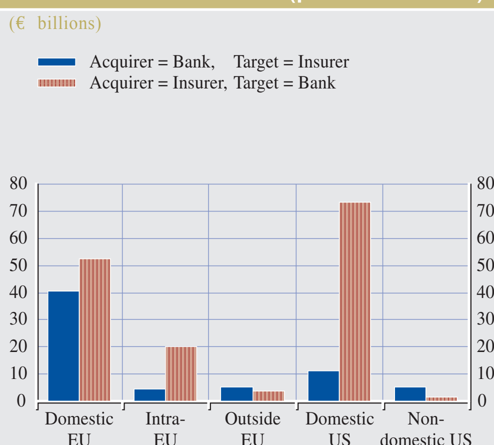
(€ billions)

	Target							
	Domestic		Intra - EU		Outside EU		Total	
Acquirer	Bank	Insurer	Bank	Insurer	Bank	Insurer	Bank	Insurer
Bank	446.3	40.7	75.1	4.3	60.0	5.1	581.4	50.1
Insurer	52.3	115.3	20.2	36.9	3.9	73.3	76.5	225.6

Source: Thomson Financial. Transactions also include asset deals. No minimum threshold in terms of acquired share was used.

Chart 1 Value of M&As involving credit institutions and insurance undertakings in the EU and in the United States (period 1990-2003)

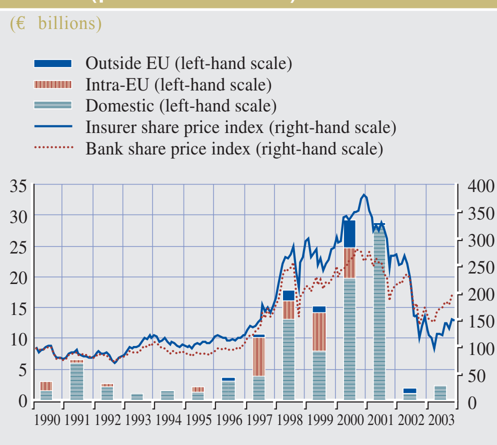
(€ billions)



Source: Thomson Financial. Transactions also include asset deals. No minimum threshold in terms of acquired share was used.

Chart 2 Value of M&As involving credit institutions and insurance undertakings in the EU (period 1990-2003)

(€ billions)



Source: Thomson Financial and Datastream. Transactions also include asset deals. No minimum threshold in terms of acquired share was used. Indices: 1990 = 100.

the first type of deal integration problems are much less of a concern.

Chart 1 compares the situation in the EU with that in the United States. In each case a distinction is made between domestic and cross-border deals, and for the EU this is further broken down into deals taking place entirely within the EU and those where the bidder or target is outside the EU. A similar analysis is not performed for Japan, where legal impediments continue to prohibit financial conglomeration.[5] Total cross-sectoral M&A activity in the United States in the period 1990-2003 was almost three quarters of the activity in the EU. Similar patterns as for the EU can be observed (i.e. the dominance of domestic deals and the active role of insurance companies as acquirers), but the patterns are much more pronounced in the case of the United States. Again, due care should be taken in drawing general conclusions from the figures since in the case of the United States the results are strongly influenced by the Travelers Group/ Citicorp mega deal worth USD 73 billion.

As is clear from Chart 2 and Table 2, most of the cross-sectoral M&A activity in the EU was concentrated in the late nineties and 2000/2001. Three quarters of the total deal value was in fact realised in the period 1998-2001, with 2000 and 2001 as clear peak years. This particular time pattern, which roughly coincides with a period of strongly booming financial markets, raises the question whether the "bancassurance" and "assurfinance" business models will be long-lasting or whether they are merely the result of particularly favourable but temporary market conditions. The fact that more recently some banks have had to inject capital into their ailing life insurance subsidiaries or that insurers have had to support their bank subsidiaries in countries such as Germany, Switzerland and the United Kingdom, may indeed cast some doubt on the success of certain strategies. One may also want to keep in mind the fact that for industrial and commercial conglomerates a trend towards "deconglomeration" was observed in the eighties and nineties, resulting in an increased focus on core businesses.

Another distinct pattern that emerges from the data is the importance of mega deals (see Table 3). About half of all domestic cross-sectoral M&A activity in the EU was accounted for by just three transactions, with the Allianz/

5 Van Cauter (2003).

Table 2 Value of M&As involving credit institutions and insurance undertakings in the EU (period 1990-2003)

(€ billions)

	Acquirer = Credit institution Target = Insurance undertaking			Acquirer = Insurance undertaking Target = Credit institution		
	Domestic	Intra-EU	Outside EU	Domestic	Intra-EU	Outside EU
1990	0.0	-	-	1.4	1.5	0.2
1991	0.4	0.4	-	5.6	0.0	0.0
1992	1.6	0.0	-	0.5	0.3	-
1993	0.6	-	0.0	0.5	0.1	0.0
1994	0.4	0.2	0.1	1.0	-	0.0
1995	1.2	-	-	0.1	0.8	0.1
1996	3.1	-	-	0.1	-	0.2
1997	2.8	-	0.1	1.1	6.4	0.0
1998	0.1	0.6	0.3	12.9	2.6	1.3
1999	6.1	0.0	0.7	1.8	6.2	0.5
2000	16.0	3.1	3.4	3.7	1.9	1.1
2001	5.7	-	0.0	22.7	0.1	0.3
2002	0.9	-	0.6	0.2	0.3	0.2
2003	1.6	-	-	0.7	-	-
1990-2003	**40.7**	**4.3**	**5.1**	**52.3**	**20.2**	**3.9**

Source: Thomson Financial. Transactions also include asset deals. No minimum threshold in terms of acquired share was used.
- = not available or no transactions; 0.0 = value lower than €0.04 billions.

Table 3 Most important M&A bank-insurance deals involving EU institutions (period 1990-2003)

(€ billions)

	Acquirer		Target		Year	Deal value
1	Allianz (I)	DE	Dresdner Bank (B)	DE	2001	22.3
2	Lloyds TSB Group (B)	UK	Scottish Widows Fund & Life (I)	UK	2000	12.0
3	Fortis (I)	BE	Générale de Banque (B)	BE	1998	10.5
4	Nationale Nederlanden (I)	NL	NMB Posbank Groep (B)	NL	1991	5.6
5	ING Groep (I)	NL	BBL (B)	BE	1997	4.1
6	Abbey National (B)	UK	Scottish Provident Institution (I)	UK	2001	2.9
7	Dexia Belgium (B)	BE	Financial Security Assurance (I)	US	2000	2.7
8	Irish Permanent (B)	IE	Irish Life (I)	IE	1999	2.7
9	ING Groep (I)	NL	BHF Bank (B)	DE	1999	2.3
10	Lloyds TSB Group (B)	UK	Lloyds Abbey Life (I)	UK	1996	2.1
11	Wuestenrot Beteiligung (B)	DE	Wuerttembergische Versicherung (I)	DE	1999	2.1
12	Skandinaviska Enskilda Banken (B)	SE	Trygg-Hansa (I)	SE	1997	2.0
13	Fortis NL (I)	NL	Banque Générale du Luxembourg (B)	LU	2000	1.8
14	Banco Santander Central Hispano (B)	ES	Cia de Seguros Mundial (I)	PT	2000	1.7
15	Halifax Group (B)	UK	Equitable Life Assurance Society (I)	UK	2001	1.7
16	Vakuutusosakeyhtio Sampo (I)	FI	Leonia Bank (B)	FI	2000	1.7
17	Fortis International (I)	NL	ASLK-CGER (B)	BE	1999	1.5
18	Royal Bank of Scotland Group (B)	UK	Churchill Insurance Co Ltd (I)	UK	2003	1.5
19	Caixa Geral de Depositos (B)	PT	Cia de Seguros Mundial (I)	PT	2000	1.4
20	Fortis (I)	BE	MeesPierson (B)	NL	1997	1.3
21	ING Groep (I)	NL	BHF Bank (B)	DE	1998	1.3
22	ING Groep (I)	NL	Crédit Commercial de France (B)	FR	1999	1.2
23	Unidanmark (B)	DK	Tryg-Baltica Forsikring (I)	DK	1999	1.2
24	Assicurazioni Generali (I)	IT	Banca della Svizzera Italiana (B)	CH	1998	1.1

Source: Thomson Financial. Only deals with a value of at least €1 billion are shown. No minimum threshold in terms of acquired share.
B = bank; I = insurance undertaking.

Dresdner Bank deal representing a particularly large share. Some groups, such as ING, Fortis and Lloyds TSB emerge as particularly active acquirers as they have been involved in several major deals.

1.2 MAJOR EUROPEAN BANCASSURANCE GROUPS

Annex 3 provides an overview of the top five banks in each of the 15 "old" EU Member States together with the name of the bancassurance group of which they are part. If the group has an insurance undertaking in the same country, this undertaking is also mentioned. There is a similar overview of the top five insurance undertakings. On the basis of this detailed information, the major European bancassurance groups indicated in Table 4 can be identified.

This list is not comprehensive as groups which do not include a top-five bank or insurance undertaking are not included. No minimum threshold for each business area was applied so the relative weight of the banking or the insurance part may vary widely. For example, Axa and Münich Re are groups with a strong insurance focus, but Barclays and Deutsche Bank are predominantly banking groups. Not all the groups may therefore qualify as a financial conglomerate under the Financial Conglomerates Directive, which imposes a minimum threshold for the cross-sectoral activities. In addition, the table does not provide details regarding the banking or insurance activities outside the EU.

Table 4 Major bancassurance groups in the EU

(As of end 2001, total consolidated assets in € billions)

1	Deutsche Bank	DE	917.7	27	Danske Bank	DK	209.0
2	Allianz	DE	911.9	28	UniCredito Italiano	IT	208.2
3	BNP Paribas	FR	825.3	29	Munich Re Group	DE	190.1
4	HSBC Holdings	UK	778.6	30	San Paolo IMI	IT	169.3
5	ING Group	NL	705.1	31	Standard Life Assurance Company	UK	130.4
6	ABN Amro Holding	NL	597.4	32	Svenska Handelsbanken	SE	124.8
7	The Royal Bank of Scotland Group	UK	590.0	33	Skandinaviska Enskilda Banken	SE	118.6
8	Barclays	UK	573.5	34	Gruppo Monte dei Paschi di Siena	IT	116.8
9	Crédit Agricole	FR	563.3	35	Foereningssparbanken - Swedbank	SE	99.2
10	Société Générale	FR	512.5	36	Caja de Ahorros y Pens. de Barcelona	ES	87.5
11	Fortis	BE	475.4	37	Allied Irish Banks	IE	86.3
12	AXA	FR	474.0	38	Caixa Geral de Depositos	PT	66.5
13	Santander Central Hispano	ES	355.9	39	Skandia Insurance Company	SE	64.1
14	Dexia	BE	351.3	40	Groupama	FR	60.1
15	Banca Intesa	IT	313.2	41	Eureko	NL	53.2
16	Lloyds TSB Group	UK	312.9	42	Wuestenrot & Wuertembergische	DE	53.1
17	Banco Bilbao Vizcaya Argentaria	ES	305.5	43	National Bank of Greece	GR	52.6
18	Abbey National	UK	303.3	44	BAWAG PSK Group	AT	47.9
19	Aviva	UK	300.9	45	Raiffeisen Zentralbank Oesterreich	AT	44.6
20	Groupe Caisse d'Epargne	FR	285.9	46	SNS Reaal Groep	NL	43.8
21	Aegon	NL	264.1	47	Espirito Santo Financial Group	LU	42.7
22	Almanij	BE	259.3	48	Alpha Bank	GR	30.7
23	Prudential	UK	255.8	49	Okobank Group	FI	30.0
24	Nordea	SE	241.5	50	Sampo	FI	29.4
25	Generali Assicurazioni	IT	222.9	51	Banco BPI	PT	24.8
26	Credit Mutuel - CIC	FR	218.8	52	Commercial Bank of Greece	GR	18.1

Source: Based on information from Bankscope and Isis. Assets are on a consolidated basis if available

2 DEFINITION OF FINANCIAL CONGLOMERATE

2.1 GENERIC DEFINITION

In the most general sense, a financial conglomerate is a group of entities whose primary business is financial and whose regulated entities engage to a significant extent in at least two of the activities of banking, insurance and securities.[6] According to this definition, bancassurance groups would qualify as financial conglomerate, but so would groups combining insurance and securities or banking and securities.

The definition used in the different countries for their supervision of financial conglomerates is sometimes more restrictive than the aforementioned general definition. For example, the regulations on financial holding companies in the United States require the presence of a bank, which is not a prerequisite under the Financial Conglomerates Directive. Also, bank-investment firm groups do not fall under the Directive since they are treated as "homogeneous" groups while in the United States, the financial holding regulations apply.

2.2 DEFINITION UNDER THE FINANCIAL CONGLOMERATES DIRECTIVE

Although the Directive does not refer to the concept of systemic groups, it is this type of group that the EU legislator had in mind when establishing the supervisory framework.[7] The following formal requirements have to be met for a group to qualify as a financial conglomerate under the Directive:

(i) the presence in the group of at least one regulated entity in the EU;
(ii) if the group is headed by a regulated entity, it must be the parent of, hold a participation in or be linked through a horizontal group with an entity in the financial sector;
(iii) if the group is not headed by a regulated entity, its activities should occur mainly in the financial sector;
(iv) the group should have at least one insurance or reinsurance undertaking and at least one entity from a different financial sector; and
(v) the group must have significant cross-sectoral activities.

A "group" is a set of undertakings, consisting foremost of a parent undertaking and its subsidiaries as defined under the Consolidated Accounts Directive. However, according to the prudential objective of the Financial Conglomerates Directive, the group concept is at the same time wider than the one used for pure accounting consolidation. First, the supervisory authorities can include in the group entities between which in their opinion a dominant influence exists, even if they do not formally meet the accountancy definition of parent-subsidiary. Second, the group also includes the participating interests[8] held by the parent and subsidiaries. And third, horizontal groups are equally covered.[9] Because of the wider definition, a group that qualifies as a financial conglomerate does not necessarily coincide with a group that is required to publish consolidated accounts under the Consolidated Accounts Directive. In addition, the entities that have been used to check whether the group meets the definition of a financial conglomerate, are not necessarily the same that will be subject to the supplementary supervision provided for in the Financial Conglomerates Directive.

The group should include at least one regulated entity in an EU Member State. A "regulated entity" is a credit institution, insurance undertaking or investment firm as defined under

6 Joint Forum (1999).
7 Van Cauter (2003).
8 The participating interest of a company in another undertaking is the right in capital, which, by creating a durable link with this undertaking, is intended to contribute to the company's activities. Additionally, the direct or indirect ownership of 20% of the voting rights or capital in an undertaking also qualifies as a participating interest. When the company exercises a significant influence in the undertaking (which is presumed to be the case when the company has at least 20% of the voting rights), the undertaking is considered to be an "associated undertaking" under the Consolidated Accounts Directive.
9 See Section 5.4 for more details on horizontal groups.

the respective EU directives for those sectors. The reason for this requirement is that the aim of the Financial Conglomerates Directive is to create a supplementary supervision of EU-regulated entities. If there are no such entities, there is no need for an additional layer of supervision. It is not required that the regulated entity is a credit institution.

If the group is not headed by a regulated entity, which is the case when it is headed by a non-regulated entity or does not have a parent company (a "horizontal group"), the group's activities should mainly occur in the financial sector. When a non-regulated entity heads a financial conglomerate, its parent is called a mixed financial holding company. A quantitative threshold, based in principle on balance sheet data,[10] is used to define what "mainly occur in the financial sector" means. The ratio of the balance sheet total of the financial sector entities in the group to the balance sheet total of the whole group has to be greater than 40%.

The financial sector entities envisaged are:

(i) credit institutions, financial institutions and ancillary banking undertakings (= banking sector);
(ii) insurance undertakings, reinsurance undertakings and insurance holding companies (= insurance sector);
(iii) investment firms and financial institutions (= investment services sector);
(iv) mixed financial holding companies; and
(v) asset management companies.[11]

These various types of entity are defined under the respective sectoral Directives. Some of them are regulated entities according to these Directives, while others, such as financial institutions, reinsurance undertakings and the various holding companies, are not.

The group should have at least one entity in the insurance sector and at least one entity in another financial sector, i.e. the banking or the investment services sector. It is not required that there is a regulated entity in each financial sector covered by the group. For example, a group consisting of a regulated investment firm and an unregulated reinsurance undertaking could, in principle, qualify as a financial conglomerate.

The last condition is that the group should have significant cross-sectoral activities. For this assessment, two sectors are considered: (i) the insurance sector and (ii) the banking/investment services sector taken together, and both have to be significant. Again, quantitative criteria are used to define what "significant" means. There is a relative criterion and an absolute criterion. The relative criterion refers to the importance of the sector in the group's total assets and solvency requirements, which has to be on average more than 10%.[12] The absolute criterion is that when the smallest sector, measured according to the above-mentioned relative criterion, has a balance sheet total of more than €6 billion, the cross-sectoral activities are also presumed to be significant. But if the group does not meet at the same time the minimum threshold of the relative criterion, the competent authorities may decide not to treat the group as a financial conglomerate.[13]

10 In exceptional cases, and by common agreement, the relevant competent authorities may replace or complement the criterion based on the balance sheet total by the income structure and/or off-balance sheet activities.
11 The specific case of asset management companies is discussed in more detail in Section 6.2.
12 Also here, the criterion based on the balance sheet total may be replaced by the income structure and/or off-balance sheet activities.
13 The Financial Conglomerates Directive gives two examples where this can be the case: (i) the smallest sector is 5% or lower of the group's balance sheet total and/or solvency requirements, and (ii) the market share for each sector in any Member State is 5% or lower.

3 MAIN CHARACTERISTICS OF A CONGLOMERATE'S BUSINESS AREAS[14]

Financial conglomerates combine banking, insurance and securities business in the same group. These three business areas differ in terms of risk characteristics and the way they are supervised (see Table 5), which complicates matters in getting an overall view of the conglomerate.

The main business of banks consists of collecting customer deposits in order to grant loans and invest in securities. Typically, banks interact with customers through a branch network. Their primary risks are credit risk and funding liquidity risk. The balance sheet of securities firms reflects their securities portfolios and financing arrangements. The asset side is dominated by the financial instruments portfolio and receivables from borrowed securities and repos; on the liabilities side, there are mainly the customer receivables and obligations related to the firm's own short positions. Securities firms are especially exposed to market risk and liquidity risk. Insurance companies underwrite risks for a premium. To cover potential claims, technical provisions are made and an investment portfolio is held to meet the liabilities. Insurers typically interact with customers through tied agents and independent brokers. Their main risks are underwriting risk (the risk that the technical provisions or premiums are too low) and investment risk (the risk that the investment portfolio does not generate a sufficiently high return).

The different core businesses correspond to different time horizons. Securities firms have the shortest horizon, reflected in the "mark to market" valuation of their balance sheet, while insurance companies often have the longest horizon. Premiums are received in the present, but claims may occur far into the future. One should, however, distinguish between life and non-life insurance. In the latter case, the time horizon is usually shorter as most of the claims are settled within a few years of the policy's inception, although "long-tailed" risks may

14 This section draws in particular on Joint Forum (2001b).

Table 5 Comparision of bank, insurance and securities business

Criterion	Bank	Insurance	Securities
Main assets	Customer loans, interbank assets, securities	Investment portfolio	Receivables secured by securities, financial instruments
Main liabilities	Customer deposits, interbank liabilities	Technical provisions	Payables to customers
Typical distribution channel	Branch	Agent, broker	Financial intermediary
Time horizon	Intermediate	Long (life), long or short (non-life)	Short
Main risks	Credit risk, funding liquidity risk	Underwriting risk, investment risk	Market risk, liquidity risk
Main risk transfer mechanisms	Securitization, credit derivatives, OTC derivatives	Reinsurance	OTC derivatives
Use of capital vs. provisions	Capital as well as provisions	More provisions (especially life)	More capital
Primary supervisory concerns	Systemic risk, protection depositors	Protection policyholders	Investor protection, systemic risk, fair / transparent / efficient markets
Main supervisory tools	Capital requirements, restrictions on permitted activities, sound policies and procedures	Capital requirements, adequacy technical provisions, investment rules, rules on reinsurance	Capital requirements, asset segregation, record keeping, operational controls

Source: Based on information in Joint Forum (2001b).

occur. The time horizon for banks is somewhere between the other two.

The different risks and time horizons are reflected in the institutions' risk management practices. The most sophisticated risk practices for a certain risk category are found in institutions that are most exposed to that risk. For example, internal ratings and credit risk portfolio models are especially found in banks and "value at risk" (VAR) models in securities firms. The risk transfer techniques also differ: banks and securities firms are large users of "over the counter" (OTC) derivatives, while the standard risk transfer technique used by insurance companies is reinsurance. Recently, the use of credit derivatives by banks to transfer credit risk to institutional investors, in particular insurance companies, has attracted the attention of authorities.

An important area of risk management is the role of capital and provisions. Both aim to absorb potential losses, but the degree to which they are relied on varies from sector to sector. Securities firms rely the most on capital and the least on provisions, while for life insurance companies the picture is reversed. The high importance of (technical) provisions for insurers follows from their core business, since they are created to cover future claims. In the case of securities firms, the regular "mark to market" valuation immediately reflects the likelihood of profits or losses in the firm's accounts, so there is less need to maintain loss provisions. Banks do not mark-to-market their loan portfolio, so loan loss reserves are kept as a buffer against expected credit losses. Minimum capital requirements are an important instrument in the supervisory tool kit. In Europe, banks and investment firms (securities firms) are subject to the same regime,[15] unlike in the United States.

The primary supervisory concerns vary somewhat for the three sectors. Systemic risk has traditionally been very high on the banking supervisors' priority list. The reasons are that banks are especially vulnerable to crises of confidence, the central role they play in the economy, and their high degree of interconnection through the interbank market and payment systems. By contrast, consumer or investor protection are of greater concern to insurance and securities supervisors, although it is recognised that the failure of a large securities or insurance firm might also have important spill-over effects.

The various risks and concerns are reflected in the tools used by supervisors. Investment and reinsurance rules are typically used by insurance supervisors, while correct record keeping and the segregation of customer assets from the firm's own assets are emphasised for securities firms. Bank supervisors typically expect banks to adopt sound policies and procedures[16] and restrict the activities they can engage in. All three categories of business are subject to minimum capital requirements, which underscores the importance of capital as the ultimate means to cover losses.

15 See the Capital Adequacy Directive.
16 A leading role in defining such sound practices is played by the Basel Committee on Banking Supervision.

4 MOTIVES FOR CONGLOMERATION AND THE RISKS INVOLVED

In a world with perfect capital markets and perfect competition and no information or agency problems, there would be no need for financial conglomerates since they would not create any added value. However, such a world is a theoretical abstraction and financial conglomerates do exist because of cost and revenue synergies, diversification benefits and agency problems. Their existence also creates certain risks, most of which are not unique to conglomerates, but come more to the fore in such organisations because of their sheer size and complexity.

4.1 MOTIVES FOR CONGLOMERATION

Cost and revenue synergies.[17] Cost synergies can be due to efficiencies of scale or scope. A company may be able to reduce its average cost by providing the same product on a larger scale or by providing multiple products. Some delivery methods exhibit important economies of scale, which may have increased over time due to technological advancements. The same may also be true for tools of financial engineering and risk management. Distribution channels and customer databases, on the other hand, are examples of areas where efficiencies of scope can be realised. If the organisation or group becomes too large, inefficiencies may arise because of coordination problems.

Efficiencies of scale or scope may also work on the revenue side. For example, multinational companies may only want to do business with financial companies of a minimum size. Scope efficiencies arise because of cross-selling opportunities resulting from consumption complementarity, the sharing of the reputation associated with a certain brand name, the possibility of developing a close customer relationship, and the preference of a customer to reveal private information to a single group. Revenue synergies are often mentioned as the main reason for the existence of bancassurance groups. Again, there is the risk that at a certain point the efficiencies turn into inefficiencies, for example when one moves away from the core business or when conflicts of interest arise.

Diversification. By diversifying, a company can reduce the volatility of its cash flows. This may in turn reduce the probability of financial distress, thus avoiding certain costs. In the scenario of a bankruptcy, there are direct (legal and administrative) as well as indirect costs (difficulty of running a company that is going through such a process). But even when the company is not entering bankruptcy, management may suffer because of increased conflicts of interest between bondholders and shareholders. Finally, diversification may also reduce the company's need for external finance. It has been argued that companies prefer internal finance because they want to avoid market discipline and the costs associated with issuing securities, or giving adverse signals to the market.

Diversification allows companies to tap new sources of revenue, which can complement a stagnating or shrinking core business. For example, by engaging in fee-business such as insurance broking, investment banking or fund management, banks may offset the prevailing disintermediation trend. Banks that have a strong market position may choose to expand in other, related markets in order to avoid intervention by competition authorities.

Agency reasons. By engaging in mergers and acquisitions, managers may want to achieve personal goals which do not necessarily coincide with the objective of maximising shareholder value. One such goal could be "empire building", if a manager's status and compensation are linked to the size of his company. Another goal could be to protect company-specific human capital by reducing the insolvency risk through diversification. Conglomeration also allows managers to complement their skills, thus making them more valuable to the organisation. Finally,

17 For a more extensive discussion, see Berger et al. (2000).

management may want to shelter itself from market discipline and corporate control mechanisms, which can be achieved through more stable cash-flows (i.e. diversification) and less external finance.

4.2 RISKS INVOLVED

Regulatory arbitrage. Since conglomerates are managed on a group-wide basis, transactions may be booked in certain entities or deals may be generated to exploit regulatory differences. Intra-group transactions can be set up to formally meet regulatory requirements, but at the same time circumvent the aims of those requirements. Examples which have attracted a lot of supervisory attention include "double or multiple gearing" and "excessive leveraging". Double gearing refers to the use of the same capital by two (or more) regulated entities in the group. Excessive leveraging can occur when debt is issued by a parent company and the proceeds are down-streamed in the form of equity to regulated entities of the group.

Contagion. Difficulties in one group entity may spill over to other ones. Such a situation can result directly from economic links between entities, such as capital holdings, loans, guarantees and cross-default provisions. Indirect contagion, on the other hand, results from the behaviour of third parties (e.g. customers, investors) to a group entity in response to problems of an affiliated entity. It can result from mere association (e.g. use of common branding and marketing).[18] Contagion is of particular concern when it affects regulated entities because of problems occurring in non-regulated entities. One may try to limit the contagion risk through the design of "firewalls"[19] but there is the possibility these may become ineffective, especially in times of stress. For example, market pressure may lead a parent company to support its ailing subsidiary although it may have no legal requirement to do so.

Moral hazard.[20] Moral hazard can work in several ways. First, a non-regulated entity may try to gain access to a bank's safety net (such as deposit insurance and lender of last resort facilities) by being associated with it in a conglomerate. Second, the conglomerate may become so large that it is perceived to be "too big to fail" by market participants. The expectation that the conglomerate will be bailed out by public authorities may stimulate risky behaviour. Third, moral hazard can also work within the group as group entities may expect help from other group entities in the event of financial distress and so behave in a more risky way.

Lack of transparency. Because of the group's size and complexity it may be difficult for markets and supervisors to obtain an accurate picture of its structure and risk profile. The legal and managerial structures of a group may vary (e.g. reporting according to business lines/ geographical areas, matrix structure). Due to the interaction between different group entities, the risk of the conglomerate is most likely to be different to the sum of the risks in the various entities on a stand-alone basis. Intra-group transactions can be used or abused to transfer assets from one entity to another and as a vehicle for cross-subsidisation. Another concern is that important risk positions may be built up which remain unnoticed because they are dispersed over many group entities. The group's complexity may also make a work-out or winding-down of an ailing conglomerate very difficult.

18 Freshfields Bruckhaus Deringer (2003).
19 "Firewalls" refers to restrictions placed between a bank and its affiliates to protect against liabilities/losses. More specifically, it also refers to statutory and regulatory limitations on financial transactions between banks and their affiliates. Such limitations are meant to prevent the spread of financial difficulties within a banking group. The restrictions should in particular prevent the group from shifting losses from its non-bank entities to its insured bank entities and potentially to the deposit insurance fund. See Walter (1996).
20 Moral hazard is the risk that the risk-taking behaviour of parties will increase because of the existence of certain arrangements or contracts.

Conflicts of interest. A conglomerate takes up a multiple of different roles in its customer-dealing which may potentially conflict. The sharing of customer information between group entities may violate privacy laws. However, conflicts of interest also exist in the same organisation so the key issue is whether there are any incentives and opportunities in the organisation to exploit such conflicts of interest. Professional investors may understand such situations and take them into account in their decisions. Competition and fear of reputation loss may also act as a restraint. Other possible measures to limit the risk are disclosure, voluntary codes of conduct and internal structures/procedures designed to ensure that the different business areas are managed sufficiently independently.

Abuse of economic power. Financial conglomerates can lead to greater market concentration, less competition and, ultimately, a less efficient financial system. They can drawn on revenue from many operations and are therefore in a better position to fight competitors. The lack of competition can in turn have a negative effect on innovation. The traditional separation between commercial banking and investment banking in the United States has been defended on the basis of the argument that this model would stimulate competition and innovation within business lines. The concentration of economic power as a result of dominating different financial sectors may ultimately lead to groups that are "too big to discipline" or "too large to fail".

5 CORPORATE STRUCTURES FOR PROVIDING FINANCIAL SERVICES IN A GROUP

Financial groups can provide financial services through various corporate structures and their choice will depend on practical as well as regulatory elements. It may, for example, not be legally possible to offer a range of financial services and products from a single balance sheet. Four basic models of corporate structure can be distinguished, each having certain benefits and risks: the integrated model, the parent-subsidiary model, the holding company model and the horizontal group model. The horizontal group is generally not discussed in the literature, but is mentioned here because the Financial Conglomerates Directive explicitly provides for it.

Although the four basic models are a convenient typology, reality is often much more complex and mixtures of the basic models in one and the same group frequently occur. For example, it seems to be rather common that, at least from a legal point of view, both a product and a geographical area dimension are present in group structures. Banking and insurance entities may not be neatly grouped into two clearly distinguishable parts of the group: in one country a parent bank may hold both insurance and banking subsidiaries, while in another country it is an insurance parent that owns the banking and insurance subsidiaries.

5.1 INTEGRATED MODEL

In the *integrated model*, the financial services are offered by one and the same entity. In the area of banking, this corresponds to the universal bank model where commercial and investment banking are combined in the same legal entity. This is the standard European model allowed under the Consolidated Banking Directive,[21] and it allows for a maximum realisation of the synergies and diversification benefits between activities. The degree to which use is made of this possibility can vary from country to country because the Consolidated Banking Directive only provides for a minimum level of harmonisation. Differences also occur between institutions as institutions may prefer, for a variety of reasons, to concentrate their securities business in a separate specialised subsidiary even if they are not legally required to do so.

The United States, by contrast, has under the Glass-Steagall Act traditionally had a very strict separation between commercial banking and investment banking and, although this separation has gradually been eroded over time, commercial banks are still prohibited from directly engaging in securities business. A variety of reasons have been put forward to justify this: to facilitate supervision, to avoid a situation where the safety net is extended beyond traditional banking activities leading to competitive distortions, to eliminate potential conflicts of interest and to insulate the banking business from the risks associated with other activities.[22]

5.2 PARENT-SUBSIDIARY MODEL

Insurance undertakings are subject to the specialisation principle in order to protect the interests of insured parties from the risks associated with other business activities. Combining insurance with banking, securities or any other commercial business in the same legal entity is therefore prohibited by law,[23] so alternative corporate models have to be used.

One such model is the *parent-subsidiary model*, which can come in different forms. Apart from the bank (parent)-securities firm (subsidiary) example mentioned earlier, other common structures are bank (parent)-insurance undertaking (subsidiary) and insurance undertaking (parent)-bank (subsidiary). The

21 The Consolidated Banking Directive, however, sets a number of (generous) limits on qualifying holdings outside the financial sector. Members States also have the option to exempt holdings in insurance and reinsurance undertakings from these quantitative limits.

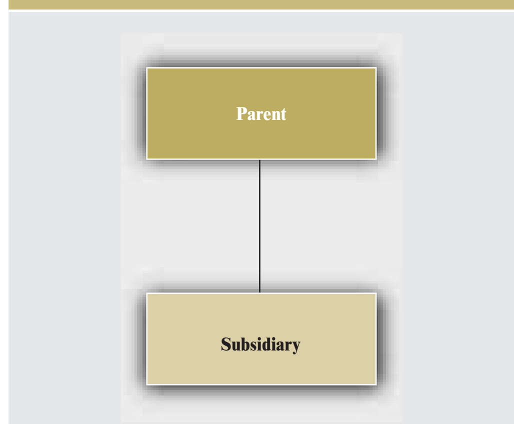
22 Santos (1998).

23 For the EU see Article 6(1)(b) of the Life Assurance Directive and Article 81(b) of the Non-Life Insurance Directive. Furthermore, life assurance and non-life insurance business can in principle not be performed by the same undertaking (see Article 18(1) of the Life Assurance Directive).

legal separation between parent and subsidiary also introduces operational separateness, so the synergies and diversification benefits of the integrated model cannot be fully realised. In addition, it requires the parent and the subsidiary to be separately capitalised and potentially introduces agency problems because of multiple management teams and different ownership structures. The advantage of such separation is that, at least from a legal point of view, the parent does not have to cover the liabilities of its subsidiary.

This last statement has to be qualified in several ways. First, the market may not perceive the parent and the subsidiary to be independent in spite of the fact that they are legally and operationally separate. This perception may be encouraged by practices such as the use of consolidated financial statements, integrated risk management systems and a single brand name. Second, in practice the parent may not be able to walk away from the subsidiary's liabilities because of the potential negative effects on, for example, the parent's reputation and on future market-funding opportunities. Third, the principle of separation is not absolute and might be modified by other legal principles. Parent companies have been declared liable for their subsidiaries' debts on the basis of representation, deficient capitalisation, de facto directorship, tortuous or negligent acts etc.

Chart 3 The parent-subsidiary model of the financial group



5.3 HOLDING COMPANY MODEL

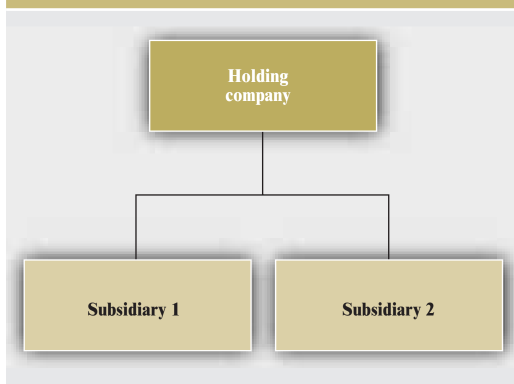
Under the *holding company model*, a top company without its own operational activities controls specialised subsidiaries. Common group functions can be centralised at the holding company level, such as risk management, capital raising and allocation, IT and group auditing.[24] In this way, the management structure may also better take into account the know-how of all business areas. It may also be easier in such a structure to isolate the different business streams of the group and evaluate each company on a stand-alone basis, not influenced by the activities of other group entities. On the other hand, by centralising functions, group entities may be rendered incapable of operating independently, which could complicate their later divestiture.

The main difference to the previous structure is that the various specialised firms do not have a direct capital relationship, but only an indirect relationship through the common holding company. In a parent-subsidiary structure with the bank as the parent, the profits of the subsidiary accrue directly to the bank. Moreover, its investment in the subsidiary is an asset accessible to the bank's creditors. In a holding company structure, by contrast, the bank does not have direct access to the profits or assets of the holding company's other subsidiaries, or vice versa.[25] However, as pointed out earlier, this formal separation may in practice not always be so absolute.

In a variant of the holding company model, the top company can head two other holding companies, one controlling the banking subsidiaries and one controlling the insurance subsidiaries. Such a two-legged approach has the advantage that both the banking and the insurance business are presented as equal partners, while the overall strategy is defined at the level of the ultimate holding company.

24 Oliver, Wyman & Company (2001).
25 Santos (1998).

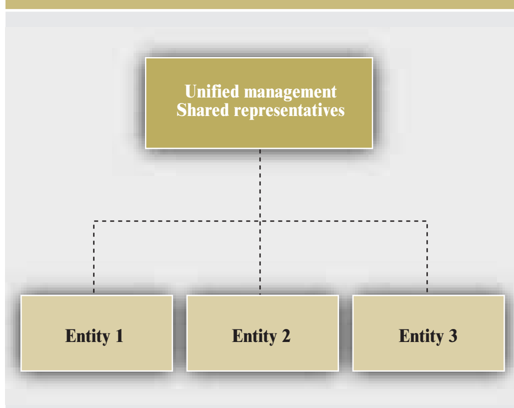
Chart 4 The holding company model of the financial group



5.4 HORIZONTAL GROUP MODEL

Finally, the Financial Conglomerates Directive provides explicitly for the case of *horizontal groups*. In a horizontal group, the entities are not linked to each other through direct or indirect capital links. Nevertheless, they can be considered to belong to the same group because pursuant to a contract or provisions in the memorandum/articles of association they are managed on a unified basis, or because the members of their corporate bodies are largely the same persons. Of course, these specific features make horizontal groups particularly difficult to identify.

Chart 5 The horizontal financial group



6 FRAMEWORK FOR THE SUPERVISION OF FINANCIAL SERVICES GROUPS

6.1 TYPES OF SUPERVISION

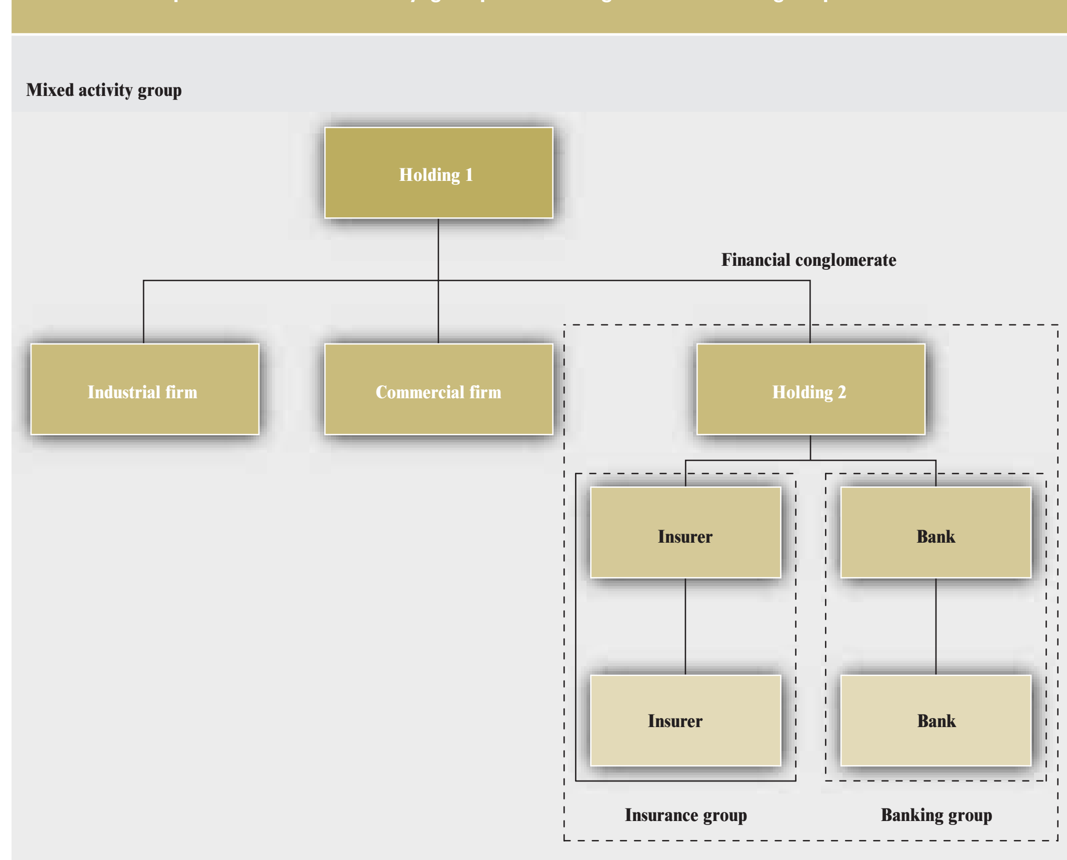
In the supervision of regulated entities three layers can be distinguished. At the *first layer*, the regulated entities are supervised on a stand-alone or solo basis.[26] For regulated entities in a group this is not sufficient since they are exposed to specific risks and may try to develop activities through group entities which they are barred from developing directly. The second and third layers of supervision therefore take a group-wide perspective. Groups that are predominantly active in the same financial services area, also called "homogenous financial groups", are dealt with at the *second layer*. Such supervision is the longest established and most developed for banking groups, while for insurance undertakings it is more recent and less comprehensive. Finally, the *third layer* corresponds to the supervision of financial conglomerates. These are mixed financial groups, or groups that are predominantly active in financial services but in different areas.

In addition, there are also mixed-activity groups, combining commercial or industrial activities with financial services. These groups are not subject to a specific harmonised regulation.[27] Indirectly, however, they may be

26 The legal basis for the stand-alone supervision of credit institutions in the EU is the Consolidated Banking Directive; for life insurance companies it is the Life Assurance Directive; for non-life insurance companies it is the Non-Life Insurance Directive; and for investment firms it is the Investment Services Directive.

27 The Consolidated Banking Directive only provides for an obligation for mixed-activity holding companies and their subsidiaries to supply information relevant for the purpose of supervising subsidiaries that are credit institutions. The Insurance Groups Directive contains a similar provision. Moreover, in the case of a mixed-activity insurance holding company, the competent authorities also have to exercise general supervision over intra-group transactions. These specific requirements are in addition to the more general requirement that significant shareholders should not pose a threat to the sound and prudent management of a bank or insurance undertaking.

Chart 6 Example of a mixed activity group combining different sub-groups



affected by the rules that apply to their regulated entities/sub-groups. For example, supervisors may want to "ring-fence" the credit institution or the banking sub-group in a mixed-activity group by requiring that bank management operates independently from the rest of the group or by placing limits on intra-group exposures. It has been argued that in such groups additional firewalls could be erected in response to the contagion risk. This can be achieved, for example, by requiring that non-financial subsidiaries are separately capitalised, restricting inter-company funding and cross-company guarantees, limiting common membership of corporate bodies and encouraging the presence of independent non-executive directors, and adopting clear policies on the use of common brand and business names.[28] Finally, it should be noted that different types of sub-group can co-exist in one and the same group, each being subject to a specific regulation (see Chart 6).

The basis for the supervision of financial groups in the EU are directives with the common characteristic that they introduce minimum levels of harmonisation, thus leaving Member States the option to impose stricter rules. In all cases, the entry point for the supplementary group supervision is an individually regulated EU entity, which is either a credit institution, investment firm or insurance undertaking. Moreover, the supervision is of a supplementary nature, meaning that regulated entities continue to be supervised on an individual or solo basis, while non-regulated entities are not. Annex 4 compares the various sectoral group regulations and the conglomerates regulation with regard to a number of key characteristics.

6.2 THE SUPERVISION OF MIXED FINANCIAL SERVICES GROUPS

Some financial services groups fall outside the supplementary supervision regime that the Directives have established for homogenous financial services groups. This is, for example, the case for groups where a credit institution/investment firm controls an insurance undertaking (or vice versa) or where a holding company controls a credit institution/investment firm as well as an insurance undertaking. The recently adopted Financial Conglomerates Directive is the basis for the supervision of such heterogeneous or mixed financial services groups. Member States have to transpose the Directive into national law by August 2004 and its provisions will apply for the first time from 1 January 2005 onwards.

The Directive's rules have to a large extent been influenced by previous work undertaken by the Joint Forum. The Joint Forum is an international group of technical experts working under the umbrella of the Basel Committee on Banking Supervision (BCBS), the International Organization of Securities Commissions (IOSCO) and the International Association of Insurance Supervisors (IAIS). It was established in 1996 to take forward the work of a predecessor group, the Tripartite Group, in examining supervisory issues relating to financial conglomerates.[29] The Joint Forum has published a number of influential papers with supervisory principles on issues such as capital adequacy; the fit and proper requirements for shareholders, directors and managers; supervisory information sharing; and the role of the coordinator in supervising conglomerates.[30] The Joint Forum's principles have to a large extent been mirrored in the Financial Conglomerates Directive.

28 Oliver, Wyman & Company (2001). See also Freshfields Bruckhaus Deringer (2003) with recommendations on firewalls as a follow-up to this report.
29 For a more extensive discussion of the Joint Forum's mandate and work, see Joint Forum (2002).
30 Joint Forum (1999).

The supplementary supervision of financial conglomerates only covers regulated entities. The Directive obliges Member States to also include asset management companies[31] in the scope of this supplementary supervision, but equally in the supervision of homogenous financial services groups, a requirement which did not exist before the Directive was adopted. Member States also have to decide to which financial sector (banking, investment services, insurance) asset management companies belong. It should be noted that the entities used to check for the existence of a financial conglomerate (see Section 2.2) do not necessarily coincide with those that are included in the supplementary supervision.

In terms of applicable supervisory regime, the Directive distinguishes between two types of financial conglomerate: those that are headed by an entity with its heads office in the EU, and those with their head office in a third country. The latter case is discussed more in detail in Section 7.5.

31 An asset management company is any company whose regular business is the management of undertakings for collective investment in transferable securities (UCITS).

7 SPECIFIC REGULATORY AND SUPERVISORY ISSUES

7.1 CAPITAL ADEQUACY[32]

Regulated entities are subject to capital requirements both on an individual and on a group-wide basis. The general framework for the capital requirements of banks and investment firms in the EU is very similar. The requirements are determined on the basis of the institutions' "risk weighted assets", i.e. the sum of on-balance sheet and off-balance sheet items weighted by a coefficient to reflect their relative risk. The capital requirements for insurance undertakings are based on criteria that are related to the insurer's overall business volume as a risk proxy. This includes premiums and claims for non-life insurers and mathematical provisions and capital at risk for life insurers ("fixed ratio" approach). The solvency rules for banks, investment firms and insurance companies have the drawback that they are not sufficiently sensitive to the company-specific risk profile. Regulatory reforms are now underway to address this, and regulations may ultimately evolve in the same direction.[33]

The eligible capital elements to cover the capital requirements are generally very much the same for the three financial sectors. Paid-up capital, reserves and subordinated debt, for example, can in all cases be taken into account. But there remain peculiarities to each sector which are important in the context of a conglomerate's capital requirements (the issue of "cross sector" capital is discussed below). For example, future profits and subscribed but non-paid-up capital can under certain conditions be used by insurance undertakings to meet their capital requirements, which is not allowed for credit institutions.

The conglomerate as a whole is also subject to solvency requirements. The purpose of this is to avoid cross-sectoral double (or multiple) counting of the same capital by several group entities. Such a situation, termed "double (or multiple) gearing", can occur when one group entity uses (part of its) capital to acquire capital of another group entity. In these circumstances, the capital generated outside the group (the correct measure of the group's real solvency) is less than the sum of the capital in the different group entities. The common concept underlying all approaches to measuring group-wide capital adequacy consists therefore of comparing the aggregate of the different sectoral requirements (or their proxies) with the sum of the group-wide capital, adjusted to eliminate double counting.[34] To achieve this objective, the Financial Conglomerates Directive lists three calculation methods, which can be used alone or in combination.[35] These methods are already used in sectoral regulations to address similar concerns about "double gearing".

The *accounting consolidation method* is the only method that uses the consolidated accounts of the conglomerate. However, whereas Directives have laid down minimum harmonised rules on how the consolidated accounts of banking and insurance groups have to be prepared,[36] such rules are still missing for conglomerates. Then, on the basis of the consolidated accounts, if available, the consolidated own funds of the group are calculated. Since intra-group transactions are cancelled out in the consolidation process, the concerns about double gearing are dealt with. These consolidated own funds have then to cover the sum of the solvency requirements for each different financial sector represented in the group.

Under the *deduction and aggregation method*, the sum of the own funds of each regulated and non-regulated entity in the group is calculated, if needed with a correction for double gearing. Then the solvency requirements for each regulated and non-regulated entity in the group, and the book value of the participations in other

32 In this paper, the terms "capital" and "own funds" are used interchangeably unless it is clear form the text that capital only refers to a sub-category of own funds.
33 The "Basel II" project for banks and "Solvency II" project for insurance undertakings.
34 Joint Forum (2001b).
35 For more details on the technical calculations, see Article 6 and Annex I of the Financial Conglomerates Directive.
36 See the Insurance Accounts Directive and the Banking Accounts Directive.

group entities, are added together. The first figure (available own funds) has to be at least as high as the second (requirements). Including the book value of participations in the solvency requirements acknowledges the fact that the participating entity may not be able to use excess capital in the related entity to cover a group-wide capital deficit.

Finally, the starting point of the *book value/requirement deduction method* are the own funds of the group's parent (again possibly corrected for double gearing). Then whichever is greater out of the book value of the parent undertaking's participation in other group entities and the solvency requirements of those entities is added to the solvency requirement of the parent. The own funds of the parent have to be at least as high as this sum. Using whichever is the greater out of the book value and the solvency requirement acknowledges the fact that the parent may lose more on a participation than the amount at which it is valued in its books.

For all three methods, only the group's financial sector entities are included in the calculation. For non-regulated entities, a notional capital requirement is calculated.[37] Capital requirements at the conglomerate level can only be met through "cross sector" capital, i.e. own funds which are eligible under each of the sectoral rules. The underlying idea is that one cannot cover a capital deficit in one entity with the surplus capital of another entity if this surplus capital is not recognised under the first entity's sectoral rules. Authorities should also take into account the extent to which capital is transferable and available across the different group entities. In addition to the quantitative requirements, adequate capital adequacy policies need to be in place at the level of the conglomerate.

Common to the three methods is that the solvency requirements of the different group entities are summed up. In doing so, no account is taken of the possible risk reduction achieved through the diversification of the conglomerate's activities. Although the industry has defended the position that one should take such diversification effects into account, there are good arguments not to do so. First, this would result in an effective pooling of capital in each of the conglomerate's businesses and using it to underwrite the entire conglomerate. This could increase moral hazard and systemic risk, and decrease market discipline.[38] Second, it has been argued that diversification effects are the greatest within a single risk factor, decrease at the business level and are the smallest across business lines. Dependent on the business mix, the incremental diversification benefits at the latter level would only be about 5 to 10% of the capital requirements.[39]

7.2 INTRA-GROUP TRANSACTIONS AND LARGE EXPOSURES

Intra-group transactions and large exposures have to be monitored for the level or volume of risk, possible contagion, conflicts of interest, and the risk of circumventing sectoral rules. To that end there is the requirement for the group's regulated entities or mixed financial holding company to report on a regular basis, and at least annually, any significant risk concentration at the level of the conglomerate as well as all significant intra-group transactions of regulated entities in the group. The Financial Conglomerates Directive remains vague on the concrete reporting modalities, such as the types of risk to be reported or the thresholds that apply. An important role is given to the coordinator to define these modalities further.

37 This is the capital requirement that such an entity would have to comply with according to the relevant sectoral rules if it were a regulated entity of that particular financial sector.
38 Morrison (2002).
39 See Kuritzkes et al. (2002) and Oliver, Wyman & Company (2001). Bikker and van Lelyveld (2002), however, find substantial diversification effects that are possibly higher than the quoted 5 to 10%.

The reason for this lack of prescription is probably the absence of an established industry or supervisory standard for aggregating risks.[40]

Intra-group transactions are defined as transactions where the regulated entities rely on other group entities (or natural/legal persons closely linked to them) for the fulfilment of an obligation. This broad definition covers, for example, loans, guarantees, derivatives and service agreements. The point of reference is always the involvement of a regulated entity that relies on the performance under the transaction. Transactions where this entity has to deliver instead of receive would therefore not be covered. It is left to the authorities to define what "significant" means. In the absence of any other agreement, a minimum threshold of no lower than 5% of the conglomerate's capital requirements applies.

The sectoral requirements show some marked differences to the Financial Conglomerates Directive. The combined banking and securities groups are subject to quantitatively large exposures limits, but there are no harmonised European rules on intra-group transactions. For insurance groups, on the other hand, no rules on large exposures apply, but intra-group transactions have to be supervised. The objective of this latter supervision is more limited than in the case of conglomerates, since authorities are only required to take action when the solvency position of the insurance company is threatened.

7.3 ORGANISATIONAL REQUIREMENTS

The Financial Conglomerates Directive introduces a number of organisational rules for financial conglomerates, which relate in particular to risk management processes and internal control mechanisms, as well as to some "fit and proper" requirements.

The conglomerate's risk management processes must include policies with respect to risks assumed, capital adequacy and the integration of risk monitoring systems. This is the first time in EU rules on group supervision that integrated risk management systems have been required. The internal control mechanisms have to include adequate mechanisms to identify and measure the material risks incurred and appropriately relate the own funds to these risks. Reporting and accounting procedures have to be in place to capture intra-group transactions and risk concentrations. Finally, the necessary mechanisms must be in place to produce the information relevant for the supplementary supervision.

The regulated entities' shareholders and the members of the management bodies are subject to sectoral suitability ("fit and proper") requirements. In this way, the requirements indirectly also apply to the conglomerate. Since conglomerates are often managed on a top-down basis, the management would escape the "fit and proper" requirements if the conglomerate were headed by a non-regulated entity. For this reason, the Directive also requires that the persons who effectively direct this entity's business are of a sufficiently good repute and have sufficient experience to perform their duties.

7.4 THE COORDINATOR AND COOPERATION/ INFORMATION EXCHANGE BETWEEN AUTHORITIES

The coordinator is the competent authority responsible for exercising supplementary supervision at the level of conglomerates. More specifically, the coordinator has the following tasks (without prejudice to the tasks of the sectoral supervisors):

40 "Economic capital" seems to be developing as a common measure for risk, irrespective of where the risk is incurred. Economic capital defines the need for capital for all risk factors in probabilistic terms at a common point (solvency standard) in a loss (or value) distribution. However, many issues in this modelling approach remain unresolved: data quality, model validation possibilities, accounting for the diversification effects across different business areas, modelling of operational risk, etc. See Oliver, Wyman & Company (2001), Bikker and van Lelyveld (2002).

(i) to propose certain technical decisions related to the identification of a financial conglomerate, to inform the group that it has been identified as such and of the identity of its coordinator and to also inform other relevant authorities of this identification outcome;
(ii) to coordinate the gathering and dissemination of information regarding the conglomerate to the other relevant authorities, in particular on capital adequacy, risk-concentration and intra-group transactions;
(iii) to take technical decisions, sometimes after consultation with the other relevant authorities, regarding reporting on capital adequacy, risk concentration and intra-group transactions;
(iv) to perform a supervisory overview and assessment of the conglomerate's financial situation, as well as its risk management and internal control mechanisms;
(v) to plan and coordinate supervisory actions in cooperation with the relevant authorities; and
(vi) to take enforcement measures with respect to the mixed financial holding company.

The law of the coordinator's Member State will determine the rules that apply to the supplementary supervision. The Financial Conglomerates Directive lists a number of criteria regarding the appointment of the single coordinator from among the competent authorities that supervise the conglomerate's regulated entities on an individual basis. For example, if the group is headed by a regulated entity, the coordinator will be the authority that has authorised this entity. If the group is not headed by a regulated entity, various elements come into play, such as the number, location and balance sheet totals of the group's regulated entities, and the number and location of holding companies within the group, etc. The relevant authorities may also overrule the criteria listed in the Directive if they are of the opinion that this is appropriate.

The coordinator and the sectoral authorities have to cooperate closely, providing each other with essential information (at their own initiative) or relevant information (upon request) for the exercise of their tasks. This is particularly the case for areas such as the conglomerate's group structure, strategic policies, financial situation, major shareholders and management, organisation, risk management and internal control systems, information collection and verification procedures, adverse developments, major sanctions and exceptional measures taken. The Directive provides for procedures to be followed by the authorities to obtain information or to verify information related to entities in another country.

7.5 PARENT UNDERTAKINGS OUTSIDE THE EU

For groups with their centre of control outside the EU, it is necessary to verify whether such groups are subject to supplementary supervision equivalent to that provided for under the Financial Conglomerates Directive. This has to be done by the authority that would be the coordinator if the group were based in the EU. In the absence of such equivalent supervision, Member States may apply to the regulated entities by analogy the provisions concerning the supplementary supervision. Alternatively, other methods may be applied to ensure the supplementary supervision, such as requiring the establishment of a mixed financial holding company with its head office in the EU and then applying the supervision to this (sub)group. The potential extra-territorial impact of the "equivalence" issue and its effect on competition has raised some concerns outside the EU, in particular in the United States.[41]

41 See for example Pitt (2002).

8 REGULATORY AND SUPERVISORY STRUCTURES DEALING WITH FINANCIAL CONGLOMERATES

8.1 AT THE EUROPEAN LEVEL

8.1.1 FORUMS FOR INFORMATION EXCHANGE AND COOPERATION

European financial markets and financial institutions have become more integrated and inter-linked, especially since the introduction of the euro. Prudential supervision, however, is still the prerogative of national authorities and is based on the principle of "home country control". In order to remove potential obstacles to further financial integration, several institutional arrangements have been set up to promote the exchange of information and cooperation between national authorities. Table 6 provides an overview of these committees for the different financial sectors before the implementation of the "Lamfalussy framework". The Mixed Technical Group (MTG), which is active in the area of financial conglomerates, was created by the European Commission following the Joint Forum's recommendations. It consists of experts from regulatory and supervisory authorities for banking, insurance and securities, the European Commission (chair) and the European Central Bank (ECB). The MTG reports to its sectoral parent committees.

An important step in streamlining the European regulatory and supervisory arrangements was taken by adopting the recommendations of the "Lamfalussy Committee".[42] The Committee proposed a four-level top-down approach to regulating securities markets, the "Lamfalussy framework". This was to be complemented by more consultation and transparency among the different institutions involved. The new framework provides for the involvement of so-called regulatory ("level 2") and supervisory ("level 3") committees. The ECOFIN Council recommended in December 2002 to extend the arrangement to all other financial sectors, resulting in the committee architecture shown in Table 7. In the area of financial conglomerates, a European Financial Conglomerates Committee was provided for as a "level 2" committee. In November 2003 the European Commission adopted a series of measures to implement the

42 Committee of Wise Men (2001).

Table 6 Institutional arrangements for regulation and supervision (pre-Lamfalussy)

Banking	Securities and UCITS	Insurance and occupational pensions	Financial conglomerates
– Banking Advisory Committee (BAC)	– High Level Securities Supervisors Committee	– Insurance Committee (IC)	– Mixed Technical Group (MTG)
– Groupe de Contact	– Forum of European Securities Commissions (FESCO)	– Conference of Insurance Supervisors (CIS)	
– The ESCB's Banking Supervision Committee (BSC)	– Securities Contact Committee – UCITS Contact Committee		

Table 7 Institutional arrangements for regulation and supervision (post-Lamfalussy)

	Banking	Securities and UCITS	Insurance and occupational pensions	Financial conglomerates
Level 2 committee	European Banking Committee (EBC)	European Securities Committee (ESC)	European Insurance and Occupational Pensions Committee (EIOPC)	European Financial Conglomerates Committee (EFCC)
Level 3 committee	Committee of European Banking Supervisors (CEBS)	Committee of European Securities Regulators (CESR)	Committee of European Insurance and Occupational Pensions Supervisors (CEIOPS)	

Table 8 Key characteristics of the new regulatory and supervisory committees

	Level 2 committee	Level 3 committee
Nature work	Political, regulatory	Technical, supervisory
Chair	European Commission	National supervisor
Members	Ministry representatives	– National supervisors – Only banking: ECB + non-supervisory national central banks (non-voting)
Tasks	– Regulation (through "comitology") – Advice to the Commission	– Information exchange – Supervisory convergence – Supervisory best practices – Advice to the Commission

ECOFIN Council's recommendations. Table 8 compares the new committees on the basis of some key elements. No decision has been taken yet on the role of the MTG in the new set-up, so it continues to exist for the time being.

8.1.2 THE EUROPEAN FINANCIAL CONGLOMERATES COMMITTEE

The Financial Conglomerates Directive established a "level 2" regulatory committee, the European Financial Conglomerates Committee (EFCC), specifically for financial conglomerates. A "level 3" supervisory committee was not envisaged from the outset, nor established by the European Commission in its November 2003 decisions. The rationale for this position is that financial conglomerates are not considered to be a fourth, separate financial sector and that their supervision is supplementary to existing sectoral supervision.

The EFCC, chaired by the European Commission, is composed of one high-level Minister representative and one technical expert per country. The Chairperson of the "level 3" committee (if such committee were set-up) and the ECB have an observer role. Neither national central banks, nor supervisors are members of this committee. The Directive gives a threefold role to the EFCC: (i) assisting the European Commission in its legislative work, (ii) giving guidance to Member States on certain technical issues, and (iii) receiving information to be provided by the Member States or the Commission.

The EFCC gives opinions to the European Commission on technical changes that the latter wants to introduce in the Directive. These opinions have to be provided in accordance with the general "comitology" procedures.[43] When the Commission wants to change the Directive, it has to hold a public consultation before submitting the draft changes to the EFCC. The opportunity for the EFCC to give guidance to Member States relates to the "equivalence" of the supplementary supervision arrangements in third countries for financial conglomerates.[44] The EFCC is also obliged to keep such guidance under review. Finally, the Directive stipulates that the Member States and/or the Commission have in certain cases an information duty to the EFCC, in particular regarding:

– the supervisory principles applied to intra-group transactions and risk concentration at the conglomerate level;
– the definitions and requirements regarding such intra-group transactions and risk concentration;
– the implementation of the Directive with regard to asset management companies;
– the capital adequacy methods applied to assess solvency; and
– the reporting frequencies for capital adequacy requirements and risk concentration in national legislation.

43 Article 5 of the Council Decision of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission (1999/468/EC).

44 Such guidance has already been given on the supervisory regime in the United States and Switzerland, see European Financial Conglomerates Committee (2004).

With regard to the four latter points, by August 2007 the Commission must submit a report to the EFCC on the Member States' practices, possibly also with a proposal for further harmonisation.

8.2 AT THE NATIONAL LEVEL

8.2.1 THE INTEGRATED FINANCIAL SUPERVISOR

The growing role of financial conglomerates is an important element in the debate about the reform of supervisory structures. More specifically, the debate relates to the issue of an integrated financial supervisor, separate from the central bank, with responsibility for all markets and intermediaries. Other arguments that are put forward for such a supervisory set-up are economies of scale and scope, increased efficiency for the supervised entities, and the lower risk of regulatory arbitrage. But a single regulator also poses certain risks: conflicting supervisory objectives may be difficult to reconcile, there is more scope for moral hazard and collusive behaviour between the supervisor and the supervised entities ("regulatory capture"), and the decision-making process in the authority may be slowed down because of organisational diseconomies.[45]

The first integrated financial supervisors in Europe emerged in the Scandinavian countries. An important impetus for the further evolution towards such a model took place in 1997 with the creation of the Financial Services Authority (FSA) in the United Kingdom. The UK example was emulated in 2002 by Germany and Austria with the creation of the Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) and the Finanzmarktaufsicht. In 2003 this was followed by the establishment of the Irish Financial Services Regulatory Authority (IFSRA). More recently, Belgium integrated its sectoral supervisors into the Banking, Finance and Insurance Commission (2004) and work is now underway in the Netherlands to integrate the prudential supervision on the banking and insurance sectors into the central bank. As a result, in eight out of the fifteen "old" EU Member States there is now (or will soon be) a single supervisory authority. The mandate and regulatory responsibilities of these integrated authorities, however, vary widely. The same goes for the way they supervise conglomerates.

Table 9 Supervision of banking, insurance and securities in the EU

Country	Banking	Insurance	Securities
AT	FSA	FSA	FSA
BE	FSA	FSA	FSA
DE	FSA/CB	FSA	FSA
DK	FSA	FSA	FSA
ES	CB	I	S
FI	B/CB	I	S
FR	B/CB	I	S
GR	CB	I	S
IE	FSA/CB	FSA/CB	FSA/CB
IT [1)]	CB	I	S
LU	BS	I	BS
NL [2)]	CB	CB	CB
PT	CB	I	S
SE	FSA	FSA	FSA
UK	FSA	FSA	FSA

Source: updated from K. Lannoo (2002).
Note: CB = central bank. B = specialised banking supervisor. BS = specialised banking and securities supervisor. S = specialised securities supervisor. FSA = single financial supervisory authority.
1) CB supervises banks and investment firms on financial stability and prudential grounds. S supervises these institutions on conduct of business grounds.
2) Envisaged structure to be adopted in the course of 2004. CB will supervise banks, investment firms and insurance companies on prudential grounds. Supervision on conduct of business grounds will for all firms be conducted by a separate authority.

In all the EU Member States that do not have an integrated financial supervisor, insurance supervision is allocated to a separate, specialised authority. Supervision of investment firms and securities markets, by contrast, is sometimes combined with banking supervision. The adoption of the universal banking model in the EU and the legal requirement to perform insurance activities in a distinct legal entity are factors that explain this particular arrangement.

Another notable feature is that very often the central bank is in one way or another involved in banking supervision. This is of course due to

45 For a more extensive discussion on integrated financial supervisors, see, for example, Briault (1999), OECD (2002) and Taylor and Fleming (1999).

the pivotal role of banks in the financial system, in particular with regard to the implementation of monetary policy and ensuring the proper functioning of payment systems. In the past, this involvement has rarely extended to the prudential supervision of insurance companies. A clear illustration of this point is Article 105(6) of the Treaty establishing the European Community. This article provides for a simplified procedure to confer upon the ECB specific tasks concerning policies relating to the prudential supervision of credit institutions and other financial institutions, but at the same time explicitly excludes insurance undertakings.

However, the Netherlands is now the first EU Member State in which the central bank will become directly responsible for the supervision of insurance companies, thus taking over the responsibilities of the separate insurance supervisor. This break with a long supervisory tradition is due to the major role that financial conglomerates play in the Netherlands, thereby changing the nature of the financial system and systemic risk. To the extent that such changes reach a material degree, the direct involvement of the central bank in insurance supervision might indeed be warranted.

8.2.2 ALTERNATIVE COORDINATION MECHANISMS

In order to meet the challenges of supervising financial conglomerates and the blurring of traditional boundaries between financial products, countries that have not moved towards an integrated supervisor are using alternative solutions. Such solutions include (i) the conclusion of memoranda of understanding (MoUs)[46] based on the principles of information-sharing and cooperation, (ii) mutual board representation, (iii) the introduction of formal consultation procedures, and (iv) the establishment of specific cross-sectoral committees. Often the central bank, even when it is not directly responsible for banking supervision, is involved in such arrangements, in particular where the area of financial stability is concerned.

For example, in France a committee comprising supervisory authorities from the different sectors of the financial industry (the "collège des autorités de contrôle des entreprises du secteur financier") was established. The purpose of this committee is to facilitate the exchange of information among supervisory authorities of financial conglomerates and to raise issues of common interest pertaining to the coordination of control of such conglomerates. Similarly, before the aforementioned reform in the Netherlands, the Council of Financial Supervisors was the main organisational set-up for cooperation between the three sectoral supervisory authorities (banking, insurance and pension funds, securities). The Council was also responsible for the coordination of policy and regulations in non-sector-specific areas of financial supervision. Committees and working groups were set-up to deal with specific topics, such as the supervision of financial conglomerates. Moreover, the cooperation between the central bank or banking supervisor and the insurance supervisor was formalised through a covenant and mutual representation at the levels of the management committee and the supervisory board.[47]

Some EU countries, such as Finland, the Netherlands and Spain,[48] developed their own legal framework for the supervision of financial conglomerates well before the Financial Conglomerates Directive. In the Netherlands, the supervision of such groups is under review and a proposal is being discussed that will give the supervisory authorities more direct powers to supervise the top holding company of a conglomerate;[49] this review will now be combined with the implementation of the Financial Conglomerates Directive. EU Member States have to adjust their legal framework by August 2004 to comply with the Directive, so countries which do not yet have a

46 A memorandum of understanding is a non-legally binding formal agreement between authorities which sets out their respective tasks and responsibilities.
47 De Nederlandsche Bank (2003).
48 Vargas (1998).
49 De Nederlandsche Bank (2002).

specific regime for the supervision of such groups will have one soon. In addition to existing general legal frameworks, specific memoranda of understanding have been concluded on a cross-sector, and sometimes cross-border, basis to deal with the supervision of specific financial groups. This has been the case, for example, for the Sampo-Leonia Group, the Nordic Baltic Holding Group and Fortis.[50] Also outside the EU, countries such as Australia, Canada, Switzerland and the United States have adopted regulation or adapted their supervisory practices with the aim of supervising financial conglomerates.[51]

50 For an example of an MoU covering the supervision such groups, see the case of the Nordic Baltic Holding Group. An unofficial translation of this MoU is available on the website of the Financial Supervision Authority of Finland.

51 Van Cauter (2003).

9 THE SUPERVISION OF FINANCIAL CONGLOMERATES IN THE UNITED STATES

9.1 THE GLASS-STEAGALL ACT AND BANK HOLDING ACT

The United States has traditionally been characterised by a strict separation between traditional banking ("commercial banking"), securities activities ("investment banking") and insurance. The legal basis for this separation was the Glass-Steagall Act (1933) and the Bank Holding Company Act (1956). Under the Glass-Steagall Act, banks were prohibited from directly or indirectly engaging in the underwriting of or dealing in securities. The Act was introduced in the wake of the Great Depression. The banking crisis that accompanied it had led to the belief that the securities activities of banks were an important cause of their collapse, as well as to accusations that banks had exploited conflicts of interest.[52] Under the Bank Holding Company Act banks were also prohibited from affiliating with insurance underwriters and non-financial firms. The Act was adopted in response to concerns that financial conglomerates could amass too much power and that banks could become exposed to losses from insurance underwriting.

Sections 16, 20, 21 and 32 are the relevant provisions of the Glass-Steagall Act. Sections 16 and 21 refer to the direct operations of banks and Sections 20 and 32 to bank affiliations. Section 16 bars national banks[53] from investing in shares, limits them to buying and selling securities as an agent, and prohibits them from underwriting and dealing in securities. Section 20 prohibits Federal Reserve member banks from affiliating with a company principally engaged in the underwriting of or dealing in securities. Section 21 makes it unlawful for securities firms to accept deposits. Section 32 further prohibits a Federal Reserve member bank from having director, officer or employee interlocks with a company principally engaged in the underwriting of or dealing in securities. Certain securities, called "bank eligible securities" (e.g. US government bonds), are exempted from the Act.[54]

Over time, the prohibitions gradually became eroded because of decisions by regulators and courts. A landmark decision was that taken by the Federal Reserve Board in 1987 to allow securities subsidiaries of bank holding companies to underwrite and deal in certain bank ineligible securities in so far as revenue generated through these activities did not exceed certain revenue thresholds and "firewalls" were respected. Since these subsidiaries were allowed by the Federal Reserve under its power to define what "principally engage in securities business" meant, they were commonly known as "Section 20 subsidiaries".[55] As time went by, the power of the securities subsidiaries was further expanded. In the area of insurance, there was also an erosion when the Office of the Comptroller of the Currency (OCC) allowed insurance to be sold by national banks anywhere in towns with fewer than 5,000 residents. Insurance underwriting, on the other hand, continued to be prohibited.

9.2 THE GRAMM-LEACH-BLILEY ACT

9.2.1 EXPANDED POWERS FOR BANK HOLDING COMPANIES AND BANKS

Deregulation reached a high-point in 1999 with the adoption of the Gramm-Leach-Bliley Act ("GLB"),[56] which, among other things, repealed Sections 20 and 32 of the Glass-Steagall Act which prohibited affiliations between banks and securities firms. Banks and securities firms

52 Later research has shown that these concerns were based more on anecdotal evidence than on generalised facts or practices. Santos (1997), Zaretsky (2000).

53 National banks are chartered, supervised and regulated by the Office of the Comptroller of the Currency (OCC), a sub-agency of the US Treasury. State-chartered banks which are members of the Federal Reserve System are supervised and regulated by the Federal Reserve Board. State-chartered banks which are not members of the Federal Reserve System are supervised and regulated by the Federal Deposit Insurance Corporation (FDIC).

54 Kwan (1997).

55 For more information about these subsidiaries, see Santos (1997) and Kwan (1997).

56 For an overview of the Act, see Federal Reserve Bank of Philadelphia (2000), Peabody & Arnold (1999) and US Senate Committee on Banking, Housing and Urban Affairs.

Table 10 US financial holding companies whose country of origin is in the EU

Name group	Country of origin
Abbey National PLC	UK
ABN Amro Holding, N.V.	NL
Banque Federale de Banques Populaires	FR
Barclays PLC	UK
BNP Paribas	FR
Caja de Ahorros de Vigo, Ourense e Pontevedra	ES
Caja de Ahorros y Monte de Piedad de Madrid	ES
CERA Stichting	BE
Den Danske Bank	DK
Deutsche Bank AG	DE
Dexia S.A.	BE
Dresdner Bank AG	DE
Fortis	BE
HBOS PLC	UK
HSBC Holdings PLC	UK
Rabobank Group – Rabobank Nederland	NL
Santander Central Hispano	ES
Societe Generale	FR
Unicredito Italiano S.P.A.	IT

Source: The Federal Reserve Board. The list includes only the top-tier holding company in each organisation. Situation as of January 2003.

continued to be prohibited from directly engaging in each other's business. GLB created a new category of bank holding company[57] called a "financial holding company",[58] which had to be registered with the Federal Reserve Board. This has to be accompanied with (self-)certification that all the depository subsidiaries are well capitalised and managed. The same process has to be followed by foreign bank holding companies whose US banking presence is solely through subsidiary banks. For foreign banks operating in the United States through branches or agencies, the certification process requires them to meet the same risk-based capital standard as US financial holding companies, but a lower leverage standard.[59] At the end of January 2003, the Board had recognised 641 top-tier financial holding companies, of which 19 were located in the EU.

Financial holding companies are allowed to engage in an expanded range of activities, including in particular:

(i) *Financially related activities.* This covers securities underwriting and dealing, insurance agency and underwriting activities, and merchant banking. Merchant banking activities can only be performed through a securities or insurance affiliate.

(ii) *Other financial activities.* If they are deemed by the Federal Reserve Board (after consultation with the US Treasury) to be financial in nature or incidental to financial activities.

(iii) *Complementary activities.* If the Federal Reserve Board determines that they are complementary to a financial activity and do not pose a substantial risk to the safety or soundness of depository institutions or the financial system.

In principle, financial holding companies continue to be barred from commercial, non-financial activities. But they can engage in activities with commercial characteristics, such as the aforementioned complementary activities and merchant banking. Moreover, a limited amount of commercial activity by non-banking companies that become financial holding companies is allowed. Merchant banking, which is broadly defined to include investments in non-financial companies, is not allowed through a depository institution or its subsidiaries.

GLB expanded the activities permitted to banks. Through financial subsidiaries, national banks can engage in financial activities permitted to financial holding companies and which the banks are not allowed to perform directly, such as securities business. They continue to be excluded from underwriting insurance, real estate development, merchant banking and the above-mentioned complementary activities. If the activities are pursued through a bank

57 A "bank holding company" is a company that controls, directly or indirectly (through another bank holding company), a bank.

58 GLB also allows the creation of "investment banking holding companies" under the supervision of the SEC. Such a company owns or controls one or more registered brokers or dealers, but does not control any commercial bank or thrift. Investment bank holding companies are not discussed further in the text.

59 Meyer (2000). For the procedures to follow, see Board of Governors of the Federal Reserve System (2000a and 2001).

subsidiary, they are subject to more safety and soundness restrictions than is the case for subsidiaries of financial holding companies. Similar rules apply to state banks that are members of the Federal Reserve System.

In practice, almost all of the new activities undertaken by the financial holding companies have been in insurance sales and merchant banking. The previous "Section 20 subsidiaries" have been converted into traditional securities subsidiaries. Smaller holding companies have used their new powers to acquire insurance brokerage entities. They also see their status as financial holding company as a relatively low-cost option for future expansion. However, a dramatic transformation of the financial services industry has not occurred. GLB brought the rules more in line with market practice rather than creating opportunities for entry into new markets. Bank holding companies which wanted to be active in the securities business were already doing so before GLB and, although banks have been engaged in selling insurance in the past, it is not clear that they are also interested in underwriting insurance.[60]

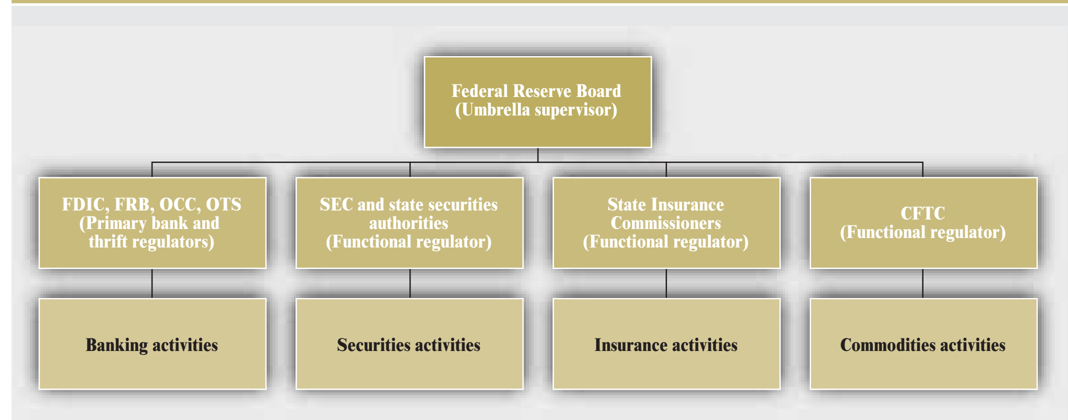
9.2.2 SUPERVISORY STRUCTURE

GLB has made the Federal Reserve Board the "umbrella supervisor" of financial holding companies. In this capacity, the Board focuses on the holding company's financial strength and stability, its consolidated risk-management process and its overall capital adequacy, with the specific goal of assuring the safety and soundness of the affiliated depository institutions.[61] Areas that are particularly important are intra-group exposures and risk concentrations. Under the new framework, formal "firewalls" have become less common, but are at the same time more critical. In that respect, Sections 23A and B of the Federal Reserve Act have become key provisions as they limit the credit flows from banks to their affiliates and require that such transactions be collateralised and made at market prices.[62] GLB also authorises the banking regulators to adopt prudential standards and restrictions on relationships or transactions between depository institutions and their subsidiaries and affiliates. Non-bank subsidiaries of financial holding companies which are engaged in securities, insurance or commodities activities continue to be supervised by their "functional regulator".

In its supervision of financial holding companies, the Federal Reserve Board relies on

60 Olson (2002a) and Santomero (2001).
61 Ferguson (2000). For a more detailed discussion on the framework of financial holding company supervision, see Board of Governors of the Federal Reserve System (2000b).
62 Meyer (2000) and Moskow (2000). Some have expressed doubts about the effectiveness of these rules, see Wilmarth (2001).

Chart 7 Supervisory structure for US Financial Holding Companies



information exchange and cooperation with the primary bank, thrift and functional regulators, and foreign supervisors. The Board relies substantially on reports already filed with/ prepared by these authorities, as well as on publicly available information. Finally, its supervisory approach is risk-focused and is coupled with market discipline.[63]

The supervisory powers of the Federal Reserve Board over entities that are supervised by their functional regulators are limited. The Board has to rely largely on information already gathered by the functional regulator and cannot impose capital requirements on functionally regulated subsidiaries. Moreover, it may not require such subsidiaries to provide funds or assets to an affiliated depository institution except in very limited circumstances. If the functional regulator does not provide the requested information in a timely manner, the Board may in certain circumstances seek it directly from the subsidiary. This will be the case when the information is necessary to assess a material risk to the financial holding company or any of its affiliated depository institutions. Other circumstances are when the information is needed to assess compliance with laws enforced by the Board, or to assess the compliance of the holding company's systems for monitoring and controlling risks that may pose a threat to an affiliated depository institution.[64] Under similar conditions, the Board may also directly examine functionally regulated subsidiaries.

9.2.3 COMPARISON BETWEEN THE US AND EU SITUATION

A striking feature of the supervisory framework of financial conglomerates in the United States is that it is very bank-orientated, which is less the case in the EU. This feature is particularly manifest in the central role of the Federal Reserve Board as the "umbrella supervisor" and in its powers and ultimate objective to safeguard the depository institutions in the group. In fact, the presence of a bank in the group is a precondition for falling under the rules of a financial holding company, which is by definition a special type of bank holding company. Because of this bank-focus, there is a risk that securities and insurance subsidiaries may be subject to a "quasi-bank" regulatory structure that effectively requires them to satisfy both a functional and a modified form of bank supervisory requirements.[65] On the other hand, because of the systemic concerns conglomerates may create, the close involvement of the central bank in the supervision of such institutions is clearly an advantage.[66]

In the EU framework, it is at least theoretically possible (although less likely in practice) to have a group without a credit institution that qualifies as a financial conglomerate. Here, the presence of an insurance or reinsurance undertaking in the group is the essential element for such qualification. In general, it also seems that there can be a much larger non-financial component in an EU financial conglomerate than in a US one. Moreover, the EU rules on the appointment of the coordinator do not guarantee that this will function will be assumed by a banking supervisor, whether or not it is a central bank.

Another difference is that the US regulation poses more organisational restrictions. At the level of shareholders of the financial holding company, non-financial commercial companies continue to be barred from owning banks. Financial holding companies that were previously not banking holding companies are nevertheless permitted to retain limited commercial activities at the level of the parent company, but only under strict restrictions. Another example is the prohibition against banks engaging directly or indirectly in insurance underwriting or merchant banking, or

63 Board of Governors of the Federal Reserve System (2000b). The Board's approach is based on the procedures and practices it developed as part of the "Large Complex Banking Organizations" program in the mid-1990s, see Half et al. (2002).
64 Ferguson (2000).
65 Half et al. (2002).
66 This argument was also advanced by the European Central Bank (2001a) in the debate on the role of central banks in prudential supervision.

directly in securities business. Such restrictions have the advantage of providing additional safeguards against possible spill-over effects on depository institutions in the event of financial difficulties. But they also imply costs for the group and may only provide protection that is more apparent than real.[67] In the EU framework, there are no special requirements regarding the shareholders of the financial conglomerate apart from the indirect requirements through the specific sectoral rules. In addition, banks can own insurance companies (and vice versa) and directly or indirectly build up substantial activities in securities business and merchant banking.

67 These arguments have been advanced by Santos (1997) in the context of the debate on where banks should locate their securities business.

10 OPEN ISSUES

With the adoption of the Financial Conglomerates Directive, the EU now has a very important additional regulatory element in place for the supervision of financial services groups. The increasing importance of mixed financial groups, in particular bancassurance groups, and the often systemic relevance of such groups underscore the need for an appropriate micro-prudential framework. However, the Directive does not offer an answer to all concerns related to conglomerates. In particular, the following areas might require further attention from authorities.

SCOPE OF THE DIRECTIVE

The Financial Conglomerates Directive defines quite strictly which groups fall under its regime of supplementary supervision. However, there might also be mixed financial groups that do not meet the strict definition of a financial conglomerate, for example because their financial or cross-sectoral activity does not reach the minimum thresholds provided for in the Directive. In such cases, it is up to national authorities to decide whether a supervisory regime for mixed financial groups that fall outside the scope of the Directive is needed. In any case, the framework introduced by the Directive will be a useful reference point for defining such a national regime.

Similarly, mixed-activity groups that combine commercial or industrial activities with financial services also fall outside the scope of the Directive and are not subject to harmonised rules. Nevertheless, there might also be supervisory concerns related to banks embedded in such groups which national authorities might want to address by, for example, introducing limits on intra-group exposures and large exposures or building in safeguards to ensure the independence of the bank's management.

TRANSPARENCY

The Financial Conglomerates Directive is quite detailed on the criteria for a group to qualify as financial conglomerate. For those who only have access to public information, it is very difficult to check whether a particular group indeed falls under the supplementary supervision. With a general trend towards increased transparency and a growing role for market discipline, it is unfortunate that authorities are not obliged (although they retain the freedom to do so) to publish a list of groups that fall under the scope of the Directive together with their regulated entities. In the United States, by contrast, the Federal Reserve Board, in its role as umbrella supervisor, publishes a list of financial holding companies that fall under its supervision, as well as financial information on those companies.

Another cause of insufficient transparency is the absence of common rules regarding the financial statements of financial conglomerates. Whereas directives have laid down reporting rules for homogenous banking groups and insurance groups, there are at present no such commonly agreed rules for conglomerates. It would be worthwhile to investigate more closely the existing reporting and disclosure practices of such groups, which are most likely to differ widely. The lack of minimum harmonisation hampers comparability across groups and the effective working of market discipline. It may also result in a higher funding cost as investors will demand a premium for the ensuing uncertainty related to the financial reporting.

The situation might improve with the forthcoming adoption of international accounting standards IAS/IFRS by EU companies, which would introduce accounting rules that are applicable to both the banking and insurance sectors. However, these sectors have also expressed serious reservations about some of the standards as they are currently drafted, and the tricky problem of aggregating insurance data and banking data remains.

SUPERVISORY COOPERATION

The Financial Conglomerates Directive addresses the main areas that were identified by the Joint Forum as relevant for the supervision of financial conglomerates. The most developed area is that of the capital adequacy requirements, and in particular the methods for addressing concerns of "double gearing". For other areas, such as large exposures and intra-group transactions, the Directive is much less prescriptive, and supervisors retain a large degree of freedom to define the concrete elements. This might be the right way to proceed due to factors such as the need to accommodate the peculiarities of individual groups or the lack of clear market standards, but this flexibility also opens the door to an uneven playing field.

In addition, it seems that so far authorities have only concluded memoranda of understanding, which detail the modalities of their cooperation, for a few conglomerates. No systematic study has been made of the content of such MoUs to identify what they have in common and what is potentially missing. For example, it is unclear to what extent these MoUs sufficiently address crisis management issues.

Finally, the mandates, approaches and concrete experiences of supervisors in dealing with mixed financial groups vary widely across countries. For example, several EU Member States have now adopted the model of an integrated supervisor, but for some (such as the Scandinavian countries) this is already a long-established model, while for others (such as Belgium, Germany and the Netherlands) the experience is much shorter.

The above leads to the conclusion that there would be merit in increasing the efforts to enhance supervisory cooperation with the aim of pursuing supervisory convergence in the area of financial conglomerates. In this respect, it has to be noted that no "level 3" or supervisory committee has been established under the Lamfalussy framework for such groups. The three sectoral "level 3" committees should therefore provide enough space in their work schedules to deal with supervisory issues related to financial conglomerates. More generally, a specific forum to discuss cross-sectoral issues, such as financial conglomerates, hybrid financial products, risk transfer instruments and open distribution models, in a more structured way might be desirable.

THE ROLE OF THE COORDINATOR

The coordinator should play an important role in the supplementary supervision of conglomerates. The coordinator acts as an interface with the conglomerate in receiving information and passing it on to the other supervisors; conducts a supervisory assessment of the conglomerate's financial situation, risks management and internal control mechanisms; and sometimes takes technical decisions.

The law of the Member State in which the coordinator is located will determine the rules of his supplementary supervision. Minimum rules have been laid down in the Financial Conglomerates Directive, but, as pointed out earlier, these minimum rules are very general, thus leaving room for ample national discretion. In view of this, it should be pointed out that the coordinator does not necessarily have to be based in the same country in which the group has its economic centre of gravity. For example, if a conglomerate is headed by a holding company that is based in the same Member State as that of a regulated entity, the latter's supervisory authority will also have responsibility for the supplementary supervision of the group. This rule would apply regardless of the importance of the local entity within the group, although the relevant authorities can waive this rule by mutual agreement.

The risk therefore exists that group structures will be set-up in order to minimise the perceived regulatory burden related to the supplementary

supervision. This risk may increase when it is easier to shift the corporate seat across borders, as is the case, for example, under the European Company Statute[68] and the planned Directive on cross-border transfers of registered offices.[69] Authorities should be aware of the possibility of such "regulatory arbitrage", which is an additional argument for supervisory cooperation and convergence.

It should be stressed that the supervision of conglomerates is only a supplementary layer of supervision. Any decisions taken by the coordinator therefore leave the responsibilities of the different national supervisors in the area of the supervision of individual regulated entities intact. Although the coordinator cannot instruct an individual national authority to take any specific measure with respect to a regulated entity in the latter's jurisdiction, the supervisors of the individual entities nevertheless have a collective responsibility for ensuring that the conglomerate meets the requirements of the supplementary supervision, and they also have a legal obligation to cooperate to achieve this end result. In that respect, it is important that supervisors do no take a narrow national view and that any national obstacles that would prevent a national supervisor from complying with the above obligations are effectively removed when the Directive is transposed into national law.

It has been argued that the concept of coordinator should be introduced for other financial groups, in particular in the context of the review of capital requirements for banks and investment firms ("Basel II" and "CAD3" projects).[70] This call has been inspired by the industry's desire to reduce the administrative burden of groups having to deal with a multitude of different authorities and (reporting) rules in Europe. The coordinator would have clearly defined tasks and powers in a wide range of areas, including at least the necessary powers to, for example, coordinate prudential reporting and validate internal models used for capital requirements purposes.

FINANCIAL STABILITY ISSUES

Due to their size, presence in financial markets, and the structural linkages they introduce between different financial sectors, financial conglomerates are particularly relevant for financial stability, not only at the national but also at the international level. For example, it has been argued that as individual conglomerates become more diversified across business lines, the financial sector as a whole becomes less diversified as the largest institutions are more similar in their risk exposures. As a result, a single large shock could adversely affect several major groups at the same time, potentially leading to macro-economic problems.[71]

At present, there is no systematic and regular monitoring of such groups at the European level, which would be the starting point for assessing their relevance for financial stability. Supervisors are currently in the process of collecting information to identify groups that would qualify as financial conglomerates under the Financial Conglomerates Directive, but this information is restricted to the supervisors concerned and therefore serves exclusively micro-prudential purposes. No systematic and regular pooling of information on individual groups in a multilateral forum is planned, although such pooling would be useful for micro-prudential purposes (e.g. to perform peer analyses) as well as for financial stability monitoring.[72]

An important tool to limit systemic risk is the existence of ex ante arrangements to deal with crisis situations resulting from financial conglomerates. Since crisis situations are likely to require the intervention of central banks through emergency liquidity assistance, it is important that central banks are also involved in such arrangements.

68 The European Company is governed by the Council Regulation (EC) No. 2157/2001 of 8 October 2001.
69 European Commission (2004).
70 European Commission (2003).
71 Bank for International Settlements (2003).
72 Padoa-Schioppa (2004).

Crisis situations are typically characterised by communication and coordination problems and conflicts of interest. Such difficulties increase exponentially with the number of authorities involved especially when they are from different countries and have different mandates,[73] as is the case when financial conglomerates are involved. Although these problems can never be completely eliminated, their negative impact can be minimised by analysing in advance possible crisis situations and conflicts of interest that may arise. Moreover, ex ante structures to deal with crises have to be in place and tested.

It is unclear to what extent present national and European structures are geared towards dealing with potential problems emanating from financial conglomerates. The earlier suggestion to perform a systematic review of existing MoUs would clarify the extent to which they also provide for crisis situations. At the EU level, an MoU has been concluded on high-level principles of cooperation between banking supervisors and central banks in crisis management situations[74] but insurance supervisors are not party to the MoU so its application to financial conglomerates is limited.

Finally, the Financial Conglomerates Directive creates the opportunity, but not a legal obligation, for the competent authorities to exchange information with central banks, the European System of Central Banks (ESCB) and the ECB, as such information may be needed for the performance of their respective tasks. Central banks should indeed have the means to assess the possible systemic implications of the behaviour of such conglomerates for financial markets as well as for payment and settlement systems. In this context, it is worth mentioning the recommendation of the "Brouwer I" report that the cooperation between supervisors and central banks should be strengthened to ensure that if the emergence of financial problems at a major group could have contagion effects in other EU Member States this will is reported to the relevant authorities.[75]

73 On this, see for example Holthausen and Rønde (2004).
74 European Central Bank (2003).
75 Economic and Financial Committee (2000).

11 CONCLUSION

Due to structural factors such as deregulation and the development of financial markets, the linkages between financial sectors in the EU, in particular the banking and insurance sectors, have increased over time. These linkages now have a multitude of different forms: distribution agreements, credit exposures, credit and operational risk transfers, shareholdings, etc. This paper focussed on a particular form of institutionalised relationship between financial sectors, the financial conglomerate, which is often created via shareholder links between banks and insurance firms. The combination of different financial services in one and the same group offers some clear revenue synergies through the exploitation of a common customer base and common distribution networks, which explains why this particular business model has become increasingly popular in the EU. In recent years, in the wake of the poor performance of financial markets, some groups have had to provide financial support to their cross-sector subsidiaries or have even disposed of them. Nevertheless, the business model exhibits strengths that are likely to underpin its continued long-term attractiveness.

However, such mixed financial services groups also create certain risks to which the groups and public authorities have to respond appropriately. These risks relate in particular to the transmission of problems from one group entity to another one via intra-group exposures. Insufficient capital at the group level resulting from excessive leveraging and multiple gearing may result in financially vulnerable groups. At the macro-level, concerns relate in particular to the impact of such complex groups on financial markets, on payment and settlement systems and, more generally, on financial stability. An adequate supervisory framework therefore needs to be in place to address these risks. With the adoption of the Financial Conglomerates Directive, this micro-prudential framework is now to a large extent in place in the EU. However, there are still a number of open issues, some of which this paper has identified, which will have to be addressed in the implementation of the Directive. One specific area for further work could be the regular collection of information on and monitoring of such groups for financial stability purposes. Given the systemic relevance of many of these groups, it is also important that central banks are involved in this process.

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ANNEX I

GLOSSARY

Ancillary banking services undertaking (EU): An undertaking whose principal activity consists in (i) owning or managing property, (ii) managing data-processing services, or (iii) any other similar activity which is ancillary to the principal activity of one or more *credit institutions*.[76]

Asset management company (EU): Any company whose regular business is the management of *undertakings for collective investment in transferable securities* (UCITS). These UCITS can be in the form of unit trusts/ common funds and/or of investment companies.[77]

Bank holding company (US): A company that controls a bank, either directly or indirectly (through another bank holding company).[78]

Competent authority (EU): National authority empowered to supervise *credit institutions*, and/or *insurance undertakings*, and/or *investment firms* on an individual or group-wide basis.[79]

Coordinator (EU): *Competent authority* responsible for exercising supplementary supervision on the *regulated entities* in a *financial conglomerate*.[80]

Credit institution (EU): An undertaking whose business is to receive deposits or other repayable funds from the public and to grant credits for its own account.[81]

Double gearing (multiple gearing): The dual (or multiple) use of the same capital within a group of (supervised) undertakings as a cover for the supervisory capital requirements of different undertakings within that group.

Excessive gearing (leveraging): Excessive debt level of the group compared to its activities. Includes situations of *double gearing* and the downstreaming of debt by the parent as equity to the subsidiary.

Financial conglomerate (EU): A group that meets the following conditions: (i) it has at least one *regulated entity* in the EU, (ii) if it is headed by a *regulated entity*, it must be the parent of, hold a participation in or be linked through a *horizontal group* with a entity in the *financial sector*, (iii) if the group is not headed by a *regulated entity*, its activities should occur mainly in the *financial sector*, (iv) it has at least one entity in the insurance sector and at least one entity in the banking or investment services sector, and (v) it has significant cross-sectoral activities.[82]

Financial conglomerate (Joint Forum): A conglomerate whose primary business is financial and whose regulated entities engage to a significant extent in at least two of the activities of banking, insurance and securities.

Financial holding company (EU): A *financial institution* which is not a *mixed financial holding company*. Its subsidiary undertakings are exclusively or mainly *credit institutions/ investment firms* or *financial institutions* and at least one of the subsidiaries is a *credit institution/investment firm*.[83]

Financial holding company (US): A *bank holding company* that is allowed to engage in expanded financial activities. These are: (i) financially related activities (including insurance agency and underwriting activities, securities underwriting and dealing, and merchant banking), (ii) other financial activities (if allowed to do so by the Federal Reserve Board, after consultation with the Treasury), and (iii) complementary activities (if allowed to do so by the Federal Reserve Board).[84]

76 Art. 1(23) Consolidated Banking Directive.
77 Art. 2(5) Financial Conglomerates Directive.
78 Sec. 2(a) Bank Holding Company Act.
79 Art. 2(16) Financial Conglomerates Directive.
80 Art. 10(1) Financial Conglomerates Directive.
81 Art. 1(1) Consolidated Banking Directive.
82 Art. 2(14) Financial Conglomerates Directive.
83 Art. 1(21) Consolidated Banking Directive. Art. 7(3) Capital Adequacy Directive.
84 Sec. 2(p) Bank Holding Company Act.

Financial institution (EU): An undertaking, other than a *credit institution*, whose principal activity consists of (i) acquiring holdings or (ii) carrying out one or more of the activities that are subject to mutual recognition under the Consolidated Banking Directive, with the exception of acceptance of deposits and other repayable funds. This includes activities that are also permitted to an *investment firm*, but does not include insurance activities.[85]

Financial sector (EU): A sector composed of one or more of the following entities: (i) a *credit institution*, *financial institution* or an *ancillary banking undertaking* (= banking sector), (ii) an *insurance or reinsurance undertaking* or an *insurance holding company* (= insurance sector), (iii) an *investment firm* or *financial institution* (= investment services sector), (iv) a *mixed financial holding company*.[86]

Firewalls (Tripartite Group): Method of addressing contagion risk caused by intra-group exposures whereby regulated entities within a conglomerate are prevented from helping other entities in the same group if the provision of such help resulted in the provider being in breach of its capital requirements.

Horizontal group (EU): Also called consortium. The entities in such group are not connected through direct or indirect (via a common holding company) capital links. But they can be considered to belong to the same group because pursuant to a contract or to provisions in the memorandum/articles of association they are managed on a unified basis, or because their corporate bodies consist for the majority of the same persons.[87]

Insurance holding company (EU): A parent undertaking, other than a *mixed financial holding company*, whose main business is to acquire and hold participations in subsidiary undertakings. The subsidiary undertakings are exclusively or mainly *insurance or reinsurance undertakings* and at least one has to be an *insurance undertaking*.[88]

Insurance undertaking (EU): An insurance undertaking within the meaning of the Life Assurance Directive or the Non-Life Insurance Directive.

Investment firm (EU): Any legal person whose regular occupation or business consists of the provision of investment services for third parties on a professional basis. The investment services covered are, among others, the reception, transmission and execution of orders, underwriting and portfolio management. The instruments these services relate to are transferable securities, *UCITS*, money market instruments and derivatives.[89]

Mixed-activity holding company (EU): A parent undertaking, other than (i) a *financial holding company*, (ii) a *credit institution/ investment firm*, or (iii) a *mixed financial holding company*. Its subsidiary undertakings must include at least one *credit institution/ investment firm*.[90]

Mixed-activity insurance holding company (EU): A parent undertaking, other than (i) an *insurance or reinsurance undertaking*, (ii) an *insurance holding company* (iii) or a *mixed financial holding company*. Its subsidiary undertakings must include at least one *insurance undertaking*.[91]

Mixed financial holding company (EU): A parent undertaking, other than a *regulated entity*, which heads a *financial conglomerate*.[92]

Regulated entity (EU): A regulated entity is (i) a *credit institution*, (ii) an *insurance undertaking*, or (iii) an *investment firm*.[93]

85 Art. 1(5) Consolidated Banking Directive.
86 Art. 2(8) Financial Conglomerates Directive.
87 Art. 12 Consolidated Accounts Directive.
88 Art. 1(i) Insurance Groups Directive.
89 Art. 1(2) Investment Services Directive.
90 Art. 1(22) Consolidated Banking Directive. Art. 7(3) Capital Adequacy Directive.
91 Art. 1(j) Insurance Groups Directive.
92 Art. 2(15) Financial Conglomerates Directive.
93 Art. 2(4) Financial Conglomerates Directive.

Reinsurance: Insurance placed by an underwriter in another company to cut down the amount of the risk assumed under the original insurance.

Reinsurance undertaking (EU): An undertaking, other than an *insurance undertaking*, whose main business consists in accepting risks ceded by an *insurance undertaking* or other reinsurance undertakings.[94]

Technical provisions: The amounts set aside on the balance sheet that are estimated to be appropriate to meet liabilities arising out of insurance contracts.

Technical risk: Synonym for *underwriting risk.*

Undertakings for collective investment in transferable securities or UCITS (EU): Undertakings whose sole object is the collective investment in transferable securities of capital raised from the public and which operate on the principle of risk-spreading. They can be constituted according to the law of contract (as common funds) or trust law (as unit trusts) or under statute (as investment companies).[95]

Underwriting: The process by which an insurance company determines whether or not and on what basis it will accept an application for insurance.

Underwriting risk: Risk that the actuarial or statistical calculations used in estimating *technical provisions* and setting premiums are wrong. Also called *technical risk.*

94 Art. 1(c) Insurance Groups Directive.
95 Art. 1(2) UCITS Directive.

ANNEX 2

Key directives

Number	Full name	Abbreviated name
2002/87/EC	Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate and amending Council Directives 73/239/EEC, 79/267/EEC, 92/49/EEC, 92/96/EEC, 93/6/EEC and 93/22/EEC, and Directives 98/78/EC and 2000/12/EC of the European Parliament and of the Council	Financial Conglomerates Directive
2002/83/EC	Directive 2002/83/EC of the European Parliament and of the Council of 5 November 2002 concerning life assurance	Life Assurance Directive
2000/12/EC	Directive 2000/12/EC of the European Parliament and of the Council of 20 March 2000 relating to the taking up and pursuit of the business of credit institutions	Consolidated Banking Directive
98/78/EC	Directive 98/78/EC of the European Parliament and of the Council of 27 October 1998 on the supplementary supervision of insurance undertakings in an insurance group	Insurance Groups Directive
95/26/EEC	European Parliament and Council Directive 95/26/EC of 29 June 1995 amending Directives 77/780/EEC and 89/646/EEC in the field of credit institutions, Directives 73/239/EEC and 92/49/EEC in the field of non-life insurance, Directives 79/267/EEC and 92/96/EEC in the field of life assurance, Directive 93/22/EEC in the field of investment firms and Directive 85/611/EEC in the field of undertakings for collective investment in transferable securities (UCITS), with a view of reinforcing prudential supervision	Post-BCCI Directive
93/22/EEC	Council Directive 93/22/EEC of 10 May 1993 on the investment services in the securities field	Investment Services Directive
93/6/EEC	Council Directive 93/6/EEC of 15 March 1993 on the capital adequacy of investment firms and credit institutions	Capital Adequacy Directive
92/30/EEC	Council Directive 92/30/EEC of 6 April 1992 on the supervision of credit institutions on a consolidated basis	Second Directive on the Consolidated Supervision of Credit Institutions
91/674/EEC	Council Directive 91/674/EEC of 19 December 1991 on the annual accounts and consolidated accounts of insurance undertakings	Insurance Accounts Directive
86/635/EEC	Council Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions	Banking Accounts Directive
85/611/EEC	Council Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations and administrative provisions relating to undertakings for collective investments in transferable securities (UCITS)	UCITS Directive
83/350/EEC	Council Directive 83/350/EEC of 13 June on the supervision of credit institutions on a consolidated basis	First Directive on the Consolidated Supervision of Credit Institutions
83/349/EEC	Seventh Council Directive of 13 June 1983 based on the Article 54 (3) (g) of the Treaty on consolidated accounts	Consolidated Accounts Directive
78/660/EEC	Fourth Council Directive 78/660/EEC of 25 July 1978 based on the Article 54 (3) (g) of the Treaty on the annual accounts of certain types of companies	Annual Accounts Directive
73/239/EEC	First Council Directive 73/239/EEC of 24 July 1973 on the coordination of laws, regulations and administrative provisions relating to the taking-up and pursuit of the business of direct insurance other than life assurance	Non-Life Insurance Directive

ANNEX 3

Top 5 banks and insurers in each of the EU countries and their bancassurance groups

Banks

		Name of bank	Total assets (€ millions)	Name of bancassurance group	Total assets (€ millions)	Name of most important related insurance company	Total assets (€ millions)
AT	1	Bank Austria Creditanstalt AG	159,596	Munich Re Group	190,059	Victoria Volksbank Versicherungsa.g	761,9
AT	2	Erste Bank der Oesterr. S. AG	86,033	X	X	X	X
AT	3	BAWAG PSK Group	47,941	BAWAG PSK Group	47,941	BAWAG Versicherungs AG	486
AT	4	Raiffeisen Zentralbank Oesterr. AG	44,583	Raiffeisen Zentralbank Oester. AG	44,583	Uniqa Versicherungen AG	12,452
AT	5	Oesterreichische Postsparkasse AG	11,982	BAWAG PSK Group	47,941	BAWAG Versicherungs AG	486
BE	1	Fortis Bank	378,000	Fortis	475,411	Fortis	NA
BE	2	Dexia Bank Belgique	222,000	Dexia	351,250	DVV De Volksverz. – Les AP	5,556
BE	3	KBC Bank NV	216,000	Almanij	259,302	KBC Insurance NV	NA
BE	4	Bank Brussel Lambert – BBL	160,653	ING Group	705,119	BBL Life	1,450
BE	5	Axa Bank Belgium	14,089	AXA	474,000	Axa Belgium SA	15,259
DE	1	Deutsche Bank AG	917,669	Deutsche Bank AG	917,669	X	X
DE	2	Bayerische Hypo- und Vereinsbank AG	715,860	Munich Re Group	190,059	ERGO Versicherungsgr. AG	101,439
DE	3	Dresdner Bank AG	506,345	Allianz	942,925	Allianz Lebensversicherung	95,793
DE	4	Commerzbank AG	500,980	X	X	X	X
DE	5	WestLB AG	423,218	X	X	X	X
DK	1	Danske Bank A/S	184,155	Danske Bank A/S	208,961	Danica Liv & Pension Livsfors.a.s.	22,554
DK	2	Realkredit Danmark A/S	71,690	Danske Bank A/S	208,961	Danica Liv & Pension Livsfors.a.s.	22,554
DK	3	Nykredit A/S	69,386	X	X	X	X
DK	4	Nordea Bank Danmark Group A/S	66,986	Nordea AB	241,549	Tryg Forsikring Livsforsikringss.	2,432
DK	5	BRF Kredit A/S	19,370	X	X	X	X
ES	1	Santander Central Hispano	355,903	Santander Central Hispano	355,903	Aseguradora Banesto Com. de Segur.	1,922
ES	2	Banco Bilbao Vizcaya Argentaria	305,470	Banco Bilbao Vizcaya Argentaria	305,470	BBVA Seguros SA de Seguros. y Reas.	8,543
ES	3	Caja de Ahorros y Pens. de Barc.	87,504	Caja de Ahorros y Pens. de Barc.	87,504	Caixa de Barcelona Seg. de Vida	*2,362*
ES	4	Caja de Ahorros y Monte de P. de M.	66,559	X	X	X	X
ES	5	Banco Español de Crédito SA, Banesto	44,689	Santander Central Hispano	355,903	Aseguradora Banesto Com. de Segur.	1,922
FI	1	Nordea Bank Finland Plc	215,851	Nordea AB	241,549	Nordea Life Assurance Finland	6,037
FI	2	Sampo Bank Plc	20,812	Sampo Plc	29,399	Varma Sampo Mutual Pension Insuran.	16,826
FI	3	OKO Bank	12,649	Okobank Group	30,030	Aurum Life Insurance	1,635
FI	4	Aktiva Savings Bank Plc	3,331	X	X	X	X
FI	5	Alandsbanken Abp	1,813	X	X	X	X
FR	1	BNP Paribas	825,288	BNP Paribas	825,288	Natio Vie	32,980
FR	2	Credit Agricole CA	563,288	Credit Agricole	563,288	Predica	83,930
FR	3	Societe Generale	512,499	Societe Generale	512,499	Sogecap	34,383
FR	4	Groupe Caisse d'Epargne	285,896	Groupe Caisse d'Epargne	285,896	Ecureuil Vie	51,500
FR	5	Credit Mutuel Centre Est Europe	218,800	Credit Mutuel – CIC	218,801	Groupe des Assurances du Cr.Mutuel	20,531
GR	1	National Bank of Greece SA	52,648	National Bank of Greece SA	52,648	The Ethniki Hellenic Insurance Co	1,251
GR	2	Alpha Bank AE	29,904	Alpha Bank AE	30,684	Alpha Insurance Company AE	290
GR	3	EFG Eurobank Ergasias SA	19,617	X	X	X	X
GR	4	Commercial Bank of Greece	18,143	Commercial Bank of Greece	18,143	Phoenix General Insurance Co. SA	366
GR	5	Agricultural Bank of Greece	16,243	X	X	X	X

Top 5 banks and insurers in each of the EU countries and their bancassurance groups (cont')

Banks

		Name of bank	Total assets (€ millions)	Name of bancassurance group	Total assets (€ millions)	Name of most important related insurance company	Total assets (€ millions)
IE	1	Allied Irish Banks Plc	86,327	Allied Irish Banks Plc	86,327	ARK Life Assurance Company	1,045
IE	2	Bank of Ireland	81,643	X	X	X	X
IE	3	DePfa-Bank Europe Plc	44,962	X	X	X	X
IE	4	Rabobank Ireland Plc	18,682	X	X	X	X
IE	5	Anglo Irish Bank Corporation	15,720	X	X	X	X
IT	1	Banca Intesa Spa	313,220	Banca Intesa Spa	313,220	Compagnia di Ass. i Riass. Sulla Vita	6,368
IT	2	UniCredito Italiano Spa	208,172	UniCredito Italiano Spa	208,172	Creditras Vita Spa	4,394
IT	3	San Paolo IMI	169,347	San Paolo IMI	169,347	San Paolo Vita Spa	10,181
IT	4	Capitalia Spa	131,415	X	X	X	X
IT	5	Banca Monte dei Paschi di Siena Spa	116,768	Gruppo Monte dei Paschi di Siena	116,768	Montepaschi Vita Spa	6,244
LU	1	Deutsche Bank Luxembourg SA	48,885	Deutsche Bank AG	917,669	X	X
LU	2	Dexia Banque Intern. a Luxembourg	44,708	Dexia	351,250	X	X
LU	3	HVB Banque Luxembourg SA	40,650	Munich Re Group	190,059	X	X
LU	4	Banque Generale du Luxembourg SA	38,996	Munich Re Group	190,059	X	X
LU	5	BNP Paribas Luxembourg	37,009	BNP Paribas	825,288	X	X
NL	1	ABN Amro Holding NV	597,363	ABN Amro Holding NV	597,363	ABN Amro Levensverzekering	2,966
NL	2	ING Bank NV	443,356	ING Group	705,119	Nationale Nederl. Levenverz.M	55,949
NL	3	Rabobank Nederland	363,619	X	X	X	X
NL	4	Fortis Bank Nederland (Holding) NV	80,002	Fortis	475,411	AMEV St. Rotterdam Verz. Groep	4,405
NL	5	SNS Bank NV	32,416	SNS – Reaal Groep NV	43,761	SNS – Reaal Groep NV	43,761
PT	1	Caixa Geral de Depositos	66,462	Caixa Geral de Depositos	66,462	Companhia de Seg. Fidelidade	3,781
PT	2	Banco Comercial Portugues SA	62,952	X	X	X	X
PT	3	Banco Espirito Santo SA	38,523	Espirito Santo Financial Group	42,748	Companhia de Seg. Tranquilidade Vida	4,282
PT	4	Banco Totta & Acores	27,366	Santander Central Hispano	355,903	X	X
PT	5	Banco BPI SA	24,791	Banco BPI SA	24,791	BPI Vida – Comp. de Seguros de Vida	NA
SE	1	Svenska Handelsbanken	124,841	Svenska Handelsbanken	124,841	SPP Livforsakring AB	10,257
SE	2	Skandinaviska Enskilda Banken AB	118,650	Skandinaviska Enskilda Banken AB	118,650	SEB Trygg Liv	6,836
SE	3	Foereningssparbanken – Swedbank	99,196	Foereningssparbanken – Swedbank	99,196	X	X
SE	4	Nordea Bank Sweden AB	66,384	Nordea AB	241,549	Nordea Life Assurance Sweden I, II	NA
SE	5	Stadshypotek AB	38,815	Svenska Handelsbanken	124,841	SPP Livforsakring AB	10,257
UK	1	Barclays Bank Plc	573,477	Barclays Plc	573,476	Barclays Life Assurance Company Ltd	11,151
UK	2	Royal Bank of Scotland PLC	338,825	Royal Bank of Scotland Group	590,034	Royal Scottish Assurance Plc	3,405
UK	3	HSBC Bank Plc	327,353	HSBC Holdings Plc	778,591	HSBC Life (UK) Ltd	5,100
UK	4	Lloyds TSB Bank Plc	315,769	Lloyds TSB Group Plc	312,889	Lloyds TSB General Insurance Limited	1,500
UK	5	Abbey National Plc	303,313	Abbey National Plc	303,313	Abbey Life Assurance Company Ltd	19,132

Source: Based on information from Bankscope and Isis. Assets are on a consolidated basis where available.

Top 5 banks and insurers in each of the EU countries and their bancassurance groups

Insurance companies

		Name of insurance company	Total assets (€ millions)	Name of bancassurance group	Total assets (€ millions)	Name of most important related bank	Total assets (€ millions)
AT	1	Uniqa Versicherungen AG	12,452	Raiffeisen Zentralbank Oester. AG	44,583	Raiffeisen Zentralbank Oester. AG	44,583
AT	2	Wiener Stadt. Allgemeine Vers.	10,652	X	X	X	X
AT	3	Generali Versicherung AG	5,305	Generali Group	222,936	X	X
AT	4	Uniqa Personenversicherung	5,049	Raiffeisen Zentralbank Oester. AG	44,583	Raiffeisen Zentralbank Oester. AG	44,583
AT	5	Raiffeisen Versicherung AG	4,942	Raiffeisen Zentralbank Oester. AG	44,583	Raiffeisen Zentralbank Oester. AG	44,583
BE	1	Fortis	NA	Fortis	475,411	Fortis Bank	378,000
BE	2	KBC Insurance NV	NA	ALMANIJ	259,302	KBC Bank NV	216,000
BE	3	AXA Belgium SA	15,259	AXA	474,000	Axa Bank Belgium	14,089
BE	4	SMAP Societe Mutuelle des A.P	9,886	X	X	X	X
BE	5	SMAP Pensions	6,267	X	X	X	X
DE	1	ERGO Versicherungsgr. AG	101,439	Munich Re Group	190,059	Bayerische Hypo-und Vereinsbank AG	715,860
DE	2	Allianz Lebensversicherung	95,793	Allianz	942,925	Dresdner Bank AG	506,345
DE	3	AMB Generali Holdings AG	78,587	Generali Group	222,936	Deutsche Bausparkasse Badenia	5,043
DE	4	Wuestenrot & Wuertembergis.	53,141	Wuestenrot & Wuertembergisse AG	52,943	Wuestenrot Bausparkasse AG	4,312
DE	5	Gerling Konzern Vers. Beteil. AG	40,323	X	X	X	X
DK	1	Danica Liv&Pension Livsfors.	22,554	Danske Bank	208,961	Danske Bank	208,961
DK	2	PFA Pension Forsikringsa.s.	20,734	X	X	X	X
DK	3	Codan A/S	11,882	X	X	X	X
DK	4	Kommunernes Pensionsfors.	8,872	X	X	X	X
DK	5	Magistrenes Pensionskasse	5,171	X	X	X	X
ES	1	Caifor SA	8,916	Fortis	475,411	X	X
ES	2	Vida-Caixa SA de Seg. y Reaseg	8,807	Fortis	475,411	X	X
ES	3	BBVA Seguros SA de Seg. y Rea	8,543	Banco Bilbao Vizcaya Argentaria	305,470	Banco Bilbao Vizcaya Argentaria	305,470
ES	4	Mapfre Vida SA Seguros y Rea.	8,415	X	X	X	X
ES	5	Allianz Comp. de Seguros y Rea.	4,921	Allianz	942,925	X	X
FI	1	Varma Sampo Mutual Pension In.	16,826	Sampo Plc	29,399	Sampo Bank Plc	20,812
FI	2	Ilmarinen Mutual Pension Ins.	13,786	X	X	X	X
FI	3	Nordea Life Assurance Finland	6,073	Nordea AB	241,549	Nordea Bank Finland Plc	215,851
FI	4	Suomi Mutual Life Assurance Co	5,892	X	X	X	X
FI	5	Tapiola Mutual Pension Ins. Co	4,610	X	X	X	X
FR	1	CNP Assurances	142,055	X	X	X	X
FR	2	Predica	83,930	Credit Agricole	563,288	Credit Agricole	563,288
FR	3	Groupama	60,056	Groupama	60,056	Banque Finama	2,312
FR	4	Ecureuil Vie	51,450	Groupe Caisse d'Epargne	285,896	Groupe Caisse d'Epargne	285,896
FR	5	CGU France	47,594	Aviva Plc	300,851	X	X
GR	1	The Ethniki Hellenic Insurance Co	1,250	National Bank of Greece SA	52,648	National Bank of Greece SA	52,648
GR	2	Phoenix General Insurance Co.	366	Commercial Bank of Greece	18,143	Commercial Bank of Greece	18,143
GR	3	X	X	X	X	X	X
GR	4	X	X	X	X	X	X
GR	5	X	X	X	X	X	X
IE	1	Hibernian Life and Pensions Ltd	5,230	Aviva Plc	300,851	X	X
IE	2	Hannover Reinsurance (Ireland)	3,274	X	X	X	X
IE	3	Eagle Star Life Assurance Co	2,510	X	X	X	X
IE	4	Scottish Mutual International Plc	1,792	Abbey National Plc	303,313	Abbey National Plc	303,313
IE	5	Allianz Irish Life Holdings Plc	1,508	Allianz	942,925	Dresdner Bank (Ireland) Plc	1,887

Top 5 banks and insurers in each of the EU countries and their bancassurance groups (cont')

Insurance companies

		Name of insurance company	Total assets (€ millions)	Name of bancassurance group	Total assets (€ millions)	Name of most important related bank	Total assets (€ millions)
IT	1	Riunione Adriatica di Sicurta Spa	43,146	Allianz	942,925	X	X
IT	2	Alleanza Assicurazioni Spa	22,638	Generali Group	222,936	Banca Generali Spa – Generbanca	895
IT	3	INA Vita Spa	19,549	Generali Group	222,936	Banca Generali Spa – Generbanca	895
IT	4	Toro Assicurazioni Spa	18,387	X	X	X	X
IT	5	Compagnia Assicuratrice Unipol	16,341	Compagnia Assicuratrice Unipol	16,341	Unipol Banca Spa	1,588
LU	1	Lombard International Assurance	2,888	X	X	X	X
LU	2	PanEuro Life SA	2,648	X	X	X	X
LU	3	Foyer Compagnie Lux. SA	1,751	X	X	X	X
LU	4	Scottish Equitable Intern. SA	1,739	Aegon NV	264,061	X	X
LU	5	Vitis Life Luxembourg SA	1,130	ALMANIJ	259,302	Kredietbank S.A. Luxembourgeoise	30,695
NL	1	Aegon NV	264,061	Aegon NV	264,061	Aegon Bank NV	5,872
NL	2	Nationale Nederl. Levenverz.M	55,949	ING Group	705,119	ING Bank N.V.	443,356
NL	3	SNS – Reaal Groep NV	43,761	SNS – Reaal Groep NV	43,761	SNS Bank NV	32,416
NL	4	Achmea Holding NV	39,876	Eureko B.V.	53,204	Achmea Bank Holding NV	15,710
NL	5	Delta Lloyd NV	34,239	Aviva Plc	300,851	Delta Lloyd Bankengroep NV	4,577
PT	1	Seguros e Pensoes Gere SGPS	8,283	Eureko B.V.	53,204	X	X
PT	2	Companhia de Seg. Tranquilidade	4,282	Espirito Santo Financial Group	42,748	Banco Espirito Santo SA	38,523
PT	3	Companhia de Seg. Fidelidade	3,781	Caixa Geral de Depositos	66,462	Caixa Geral de Depositos	66,462
PT	4	Mundial Confianca Comp. de Seg.	2,790	Caixa Geral de Depositos	66,462	Caixa Geral de Depositos	66,462
PT	5	X	X	X	X	X	X
SE	1	Skandia Insurance Co. Ltd	64,121	Skandia Insurance Co. Ltd	64,121	Skandiabanken	3,515
SE	2	Alecta Pensionsforsakring Oms.	36,962	X	X	X	X
SE	3	Arbetsmarkn. Pensionsfoers.a.b.	22,841	X	X	X	X
SE	4	Gamla Livfoers.a.b. Seb Trygg Liv	18,127	Skandinaviska Enskilda Banken AB	118,650	Skandinaviska Enskilda Banken AB	118,650
SE	5	Folksam Mutual Life Insurance	6,570	X	X	X	X
UK	1	Legal and General Group Plc	176,569	X	X	X	X
UK	2	Prudential Assurance Co. Ltd	136,222	Prudential Plc	255,846	Prudential Banking Plc	12,742
UK	3	Standard Life Assurance Co.	130,387	Standard Life Assurance Co.	130,387	Standard Life Bank Ltd.	8,049
UK	4	CGU International Insurance Plc	128,252	Aviva Plc	300,851	X	X
UK	5	Royal & Sun Alliance Insurance Plc	100,982	X	X	X	X

Source: Based on information from Bankscope and Isis. Assets are on a consolidated basis where available.

ANNEX 4

Comparison of the supervision of financial groups

Element of comparison	Banking groups	Insurance groups	Investment firm groups	Financial conglomerates
Legal basis	Consolidated Banking Directive	Insurance Groups Directive	Capital Adequacy Directive	Financial Conglomerates Directive
Scope of harmonisation and nature of standards	Minimum harmonisation/standards	Minimum harmonisation/standards	Minimum harmonisation/standards	Minimum harmonisation/standards
Entry point for supervision	Credit institution	Insurance undertaking	Investment firm	Regulated entity
Nature of supervision	Consolidated supervision	"Solo plus" supervision [3]	Consolidated supervision	"Solo plus" supervision [3]
Areas of supervision	– Solvency [1] – Own funds to cover market risk [1] – Large exposures [1] – Non-financial qualifying holdings [1] – Internal control systems for information production	– Solvency [1] – Intra-group transactions [2] – Internal control systems for information production	– Solvency [1] – Own funds to cover market risk [1] – Large exposures [1] – Non-financial qualifying holdings [1] – Internal control systems for information production	– Solvency [1] – Intra-group transactions [2] – Risk-concentration – Risk management processes – Internal control systems for information production
Types of entity included in supplementary supervision	– Credit institutions – Financial institutions – Ancillary banking services undertakings	– Insurance undertakings – Other undertakings (financial or non-financial)	– Investment firms – Financial institutions	Regulated entities
Entities within scope of supervision	– Entities within scope of consolidation (parent and subsidiaries)	– Related entities of insurance undertaking – Participating entities in insurance undertaking – Related entities of participating entities in insurance undertaking	– Entities within scope of consolidation (parent and subsidiaries)	– Entities heading a financial conglomerate – Entities, the parent of which is an EU mixed financial holding company – Entities linked with another financial sector entity through a horizontal group

1) Quantitative requirements.
2) It may be assumed that both positions and transactions (i.e. changes in positions) are covered. See Helsinki Protocol for Insurance Groups.
3) In contrast to consolidated supervision, "solo plus" supervision uses the group entities' individual financial statements as a starting point and corrects them for the group effect.

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