Mr. Jörgen Holmquist
Director General DG MARKT
European Commission
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Prot. No. 151/GH
Brussels, 16 April 2010

Re: SME respond to the CRD IV consultation

Dear Mr. Holmquist,

with this letter I would like to answer on behalf of UEAPME, the European Association for Crafts and SMEs in Europe, to your consultation on new capital requirements for the banking sector. Although Europe's SMEs do not have the capacity to answer to the specific technical question, which were put forward in your consultation document, we want to present to you with some general comments on regarding the current discussion on regulatory capital for banks, which are of utmost importance for small and medium sized enterprises and their access to finance.

1. **Need for a serious impact assessment of any new capital requirement regulation on real economy**

   Many discussions we had during the last months with the banking sector have shown that at this moment even banks are not able to assess the impact of the proposals for new capital requirements made by the Basel Committee and by DG Market. It would be absolutely unacceptable if political decisions on a new capital requirement framework are made without a clear understanding of what such a regulation would mean for access to finance for enterprises and especially for SMEs in Europe.

   Therefore, UEAPME demands an encompassing and independent assessment of any new capital requirement regulation about the macro and micro economic impact of such a new regulation, including a specific assessment on consequences for SME finance in Europe. A European Quantitative Impact Study by CEBS is not sufficient and a final decision cannot be based on such a narrow assessment.

2. **Pro-cyclicality of financial market regulations was always a concern of SMEs and has materialised throughout the current crisis**

   Several years ago, when the Basel II regulation was discussed, SMEs had already raised their concerns about the pro-cyclical effects of the current capital requirement regulation of banks. The introduction of IFRS created additional effects in the same direction. Nowadays, there is a broad consensus that such pro-cyclical effects have materialised in both directions. When the bubble was building up, the increase of equity in the balance sheets of banks and the improved rating of companies increased the capacity of financial institutions to provide credit and loans at very high volume and at low prices, while during the last year, when equity and other forms of regulatory capital melted down and the ratings of enterprises got worse, the provision of financing to companies had to be reduced and the prices went up.

Therefore, UEAPME would support any regulatory change to dampen these pro-cyclicality effects in a new proposal from the Basel Committee, i.e. by forcing financial institutions to build-up reserves in "good" times (dynamic provisioning).

3. An increase in capital requirements is not justified for retail businesses, which have not caused the current crisis

The current crisis proved that the current regulations for regulatory capital (Basel II as transposed in the CRD) have not been sufficient to avoid the need to bailout financial institutions. Therefore, we believe that the discussion about an increase of regulatory capital in the balance sheets of financial institutions is justified, insofar as it necessary to avoid such a crisis again. At the same time, the amount of capital required must not create comparative disadvantages for the European economy and should not diminish the capacity of the financial system to provide financing to the real economy.

Therefore, UEAPME supports a reasonable increase as regards capital requirements, but this increase should be linked to financial services and products that created the current problems, like the trading book and sophisticated products, even if they have a good rating (during good times). However, UEAPME sees no justification to increase the capital requirements for normal retail or SME loans.

4. The introduction of a general leverage ratio provides wrong incentives and may increase risk-taking by financial institutions

A general leverage ratio does not take into account the risk involved and provides positive incentives to take more risks and disadvantages for businesses with lower risks but also lower profit margins (i.e. SME loans). An increase of capital requirements only for riskier activities, which makes normal retail business more attractive for banks and also avoid the need for a general leverage ratio, would be more adequate. If such a leverage ratio cannot be avoided, it has to be limited to investment banking activities.

Therefore, UEAPME calls for a review of the proposal for a general leverage ratio and, if such a ratio is not avoidable, for an exclusion of retail and SME loans.

5. **Decentralised banking systems of different banking business models contribute to stability in the market**

   Currently SMEs from all EU Member States complain about difficulties and restriction in access to finance, but there are significant differences among countries. SMEs from countries where a highly decentralised banking system still exists, including local and regional cooperative banks and saving banks, show significantly less problems with access to finance throughout the crisis compared to SMEs in countries where SME finance is dominated by commercial banks only.

   Therefore, UEAPME asks to respect the particularities of co-operatives and savings banks as regards their capital and not to exclude their specific types of capital from tier 1, which would otherwise create serious problems for access to finance for SMEs in many regions of Europe.

We would like to ask for your support in finding solutions capable of contributing to restabilising the financial market, in line with the needs of real economy enterprises and without endangering their access to finance in the future.

Yours sincerely,

Andrea Benassi
UEAPME Secretary General