

ANNUAL REPORT 2011 AND 2012



Finance Watch

Making finance serve society

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Finance Watch was created in June 2011. This first annual report covers the 18 month period from the founding AGM on 30 June 2011 to the end of 2012.



Finance Watch

Making finance serve society

Finance Watch is an independent, non-profit, public interest association dedicated to making finance work for the good of society. It focuses on improving European financial regulation.

Why Finance Watch?

The financial crisis showed that the world of finance cannot control itself, while politicians lack the tools to counter strong financial lobbies. A better balance between private and public interests is needed so that financial regulation can benefit the entire community.

Our mission is...

- to strengthen the voice of society in the reform of financial regulation,
- to conduct advocacy and present public interest arguments to financial policymakers and the public,
- to act as a counterweight to the private interest lobbying of the financial industry.

We are working for...

- a financial system that allocates capital to productive use in a transparent and sustainable manner without causing detriment to society at large.

Letter from the chair

Ieke van den Burg

Ieke is a Member of the Scientific Committee of the European Systemic Risk Board. She was a Member of the European Parliament (MEP) from 1999 to 2009 and served on the European Parliament's Committee on Economic and Monetary Affairs (ECON).



Finance Watch provides in-depth knowledge

without a private agenda, coupled with

a close connection to civil society and ordinary people.

When I was a Member of the European Parliament dealing with financial markets regulation there was very little expertise available to us from outside the financial sector. I saw financial lobbyists – an astonishing number – and they had impressive know-how but of course their input was always skewed by their private corporate interests. Distilling the overall general public interest from all that information was not an easy thing to do.

Now we have Finance Watch, which I am very proud and honoured to serve as chair and to have helped launch in the period after I stepped down as MEP.

Finance Watch provides exactly what we missed in that period of heavy deregulation before the financial crisis: in-depth knowledge and analysis without a private agenda, coupled with a close connection to civil society and the ordinary people who use and work in financial services.

Our association has a broad membership: it contains European and national level consumer organizations, trade unions, social housing groups, environmental and development groups, NGOs that fight corruption and tax evasion and others, all united in their determination to make finance serve society again.

Beside them is a select group of qualified individual members, including leading academics and former finance professionals, some of whom have had second thoughts about their former working practices!

The current 13-strong staff of Finance Watch also includes such former traders, bankers and lobbyists, with a huge academic and practical knowledge between them.

This combination of backgrounds and experience is what gives Finance Watch its strength and makes it different from any other NGO, think tank or campaigning platform.

In the Board of Directors, which was elected at Finance Watch's first AGM on 30 June 2011, we also represent these different backgrounds and we are fully conscious of the challenges that this special mission brings.

Reforming financial regulation in the public interest will take years and the stakes are high, as the crisis and recessions showed. Those with vested interests to defend will continue fighting and spending to protect their positions. The biggest challenge for Finance Watch is to stay at the table by achieving sustainable funding. I do appeal to all readers of this report to consider becoming a Friend and a sponsor of Finance Watch.

With my colleagues on the board, together with the Secretary General and his excellent team, I am proud to present this first Annual Report, covering the fascinating first one and a half years of Finance Watch's existence.

Warm wishes,
Ieke van den Burg
On behalf of the Board of Directors

Interview with . . .

Thierry Philipponnat

Secretary General

Thierry was appointed Secretary General of Finance Watch on 30 June 2011. He was previously an executive board member of Amnesty International in France and, before that, an investment banker for more than 20 years.

Why does the public need someone to speak for it on financial regulation?

Thierry Philipponnat > With finance, a member of the public can have a gut feeling that there is something big at stake, let's call it the general interest. But financial regulation is technical and to lobby on it you need to wake up in the morning and know this is your job. Finance Watch has the ability to analyse regulation from a public interest point of view and say things as they are; so if the emperor is naked, so to speak, it's our job to say so.

What is special about Finance Watch as an NGO?

T. P. > The first thing is that Finance Watch is a Members' association. This is really important: Members and staff work together, feeding each other's work. I can feel that there's something happening; people are convinced about what they're doing and seeing that chemistry taking place is a great pleasure. The second is that the team comes from the financial world. Between us we've done quite a few things - lending money, structuring products, derivatives trading, infrastructure, capital markets, communications and financial lobbying, to name a few - so we have the same level of expertise as the people on the other side.

Why does financial regulation matter?

T. P. > I really believe that a strong civil society is the key to making sure we take care of the future, of what happens beyond the next earnings cycle or election. If we want this world to be sustainable and to address the big issues then we have to get things right in financial regulation first. It's the first layer of the building.

What do you mean by "public interest"?

T. P. > You can write long theories about that but, in short, you know it when it's there. When you see something that benefits a very limited number of actors but which doesn't help the economy and even puts society at risk, then you know public interest is not being respected.

What has the reception been like for Finance Watch?

T. P. > It's been tremendous. We've received many expressions of public support in quite a few different countries. Regulators and policymakers have not only accepted us but have asked for us. Even the financial industry understands that we need an adult dialogue if we want to progress beyond bank-bashing and populism.

How can people support Finance Watch's work?

T. P. > You can sign up as a Friend and receive our free newsletter, or get more involved and become a Member: every person that joins us increases our weight in the debate. Donations are also crucial. Having lots of small donations is the best type of funding for an NGO like ours as it shows that people care about financial regulation and how it affects their lives.



If we want this world to be sustainable

and to address the big issues then we have

to get things right in financial regulation first.



HISTORY

MEPs BECAME CONCERNED THAT AN ASYMMETRY OF LOBBYING COULD LEAD TO UNDEMOCRATIC OUTCOMES

In the summer of 2010, some Members of the European Parliament (MEPs) noticed that they had become inundated with requests to meet representatives of the financial industry. At the same time, they were dealing with ever more technical financial legislation coming through Brussels in the aftermath of the financial crisis of 2007.

This group of 22 MEPs became concerned that an asymmetry of lobbying could lead to undemocratic outcomes as reform proposals were reshaped or weakened by the industry lobby on their way to becoming law. They

therefore launched a cross-party call for action in July 2010, which became known as the “Call for a finance watch”.

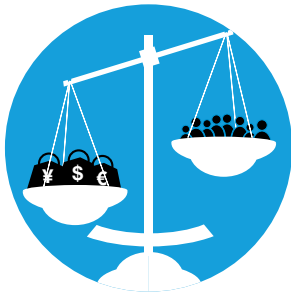
Their petition found strong support in Brussels and beyond. In the next five months it grew to nearly 200 signatures from national politicians and MEPs from a wide range of political parties and Member States in Europe.

In December 2010, some of the initial MEPs funded a six-month project to investigate whether a new, independent body could be created to improve the way civil society’s voice is represented

in the legislature on matters of financial reform. Over the course of more than 120 meetings with representatives of civil society and other organisations, a set of concrete proposals for Finance Watch was drawn up.

Finance Watch was registered on 28 April 2011 as an Association Internationale Sans But Lucratif (international non-profit association) under Belgian law and held its founding General Assembly in Brussels on 30 June 2011, where its Members adopted the statutes of the AISBL and elected the Board, which appointed the Secretary General.

SOCIAL MISSION AND PRINCIPLES



GOVERNANCE

TIMELINE

2010

June 2010

22 MEPs launch
"Call for a finance watch"

November 2010

the call gathers 189 signatures
– MEPs and national politicians

December 2010

start of project phase for
the creation of Finance Watch

2011

28 April 2011

Finance Watch registered
as AISBL

30 June 2011

founding
General Assembly, Brussels

August 2011

"virtual" General Assembly
approves budget
for 2011 and 2012

September 2011

first staff appointments,
offices taken
in Square de Meeûs

10 November 2011

General Assembly approves work
plan for 2012 and appoints CTI

2012

19-20 November 2012

General Assembly approves
auditor and work plan for 2013

2013

19 April 2013

General Assembly approves
financial report for 2011
and 2012 and strategic plan

OUR MISSION IS to strengthen the voice of society in the reform of financial regulation by conducting advocacy and presenting public interest arguments to lawmakers and the public as a counterweight to the private interest lobbying of the financial industry.

FINANCE WATCH WORKS ACCORDING TO THE FOLLOWING PRINCIPLES:

→ **The financial industry plays an important role** in allocating capital, coping with risk and providing financial services and this role has strong public interest implications.

→ **The essential role of the financial system** is to allocate capital to productive use in a transparent and sustainable manner.

→ **The purpose of finance is to serve** the real economy. The situation where the economy becomes subordinated to finance must be rejected because it is destructive of economic and social structures.

→ **Whilst profitability constitutes** both a legitimate objective and a necessary condition for the sustainability of financial institutions, the pursuit of profitability should not be conducted to the detriment of public interest.

→ **The transfer of credit risk** to society at large is not acceptable.

→ **The general objective of Finance Watch** is an economic organisation of society where the needs of the real economy to have access to capital and to financial services are fulfilled in a sustainable, equitable and transparent manner.

BOARD OF DIRECTORS

COMPOSITION

for 2011-2014



Ieke van den Burg (Dutch)
Member of the Scientific Committee of the European Systemic Risk Board, former Member of the European Parliament (chair)



Friends of the Earth Europe (FoEE), represented by **Paul de Clerck** (Dutch), coordinator of FoEE's Economic Justice Program.



European Consumers' Organisation (BEUC), represented by **Monique Goyens** (Belgian), BEUC Director General (vice chair).



Transparency International EU Office, represented by **Jacques Terray** (French), Vice-President of TI France and member of TI International Board of Directors.



European Trade Union Confederation (ETUC), represented by **Andreas Botsch** (German), ETUC Special Advisor (treasurer).



Philippe Loumeau (French), Independent consultant, former Chief Operating Officer of Montreal Exchange, former Board member of Boston Options Exchange.

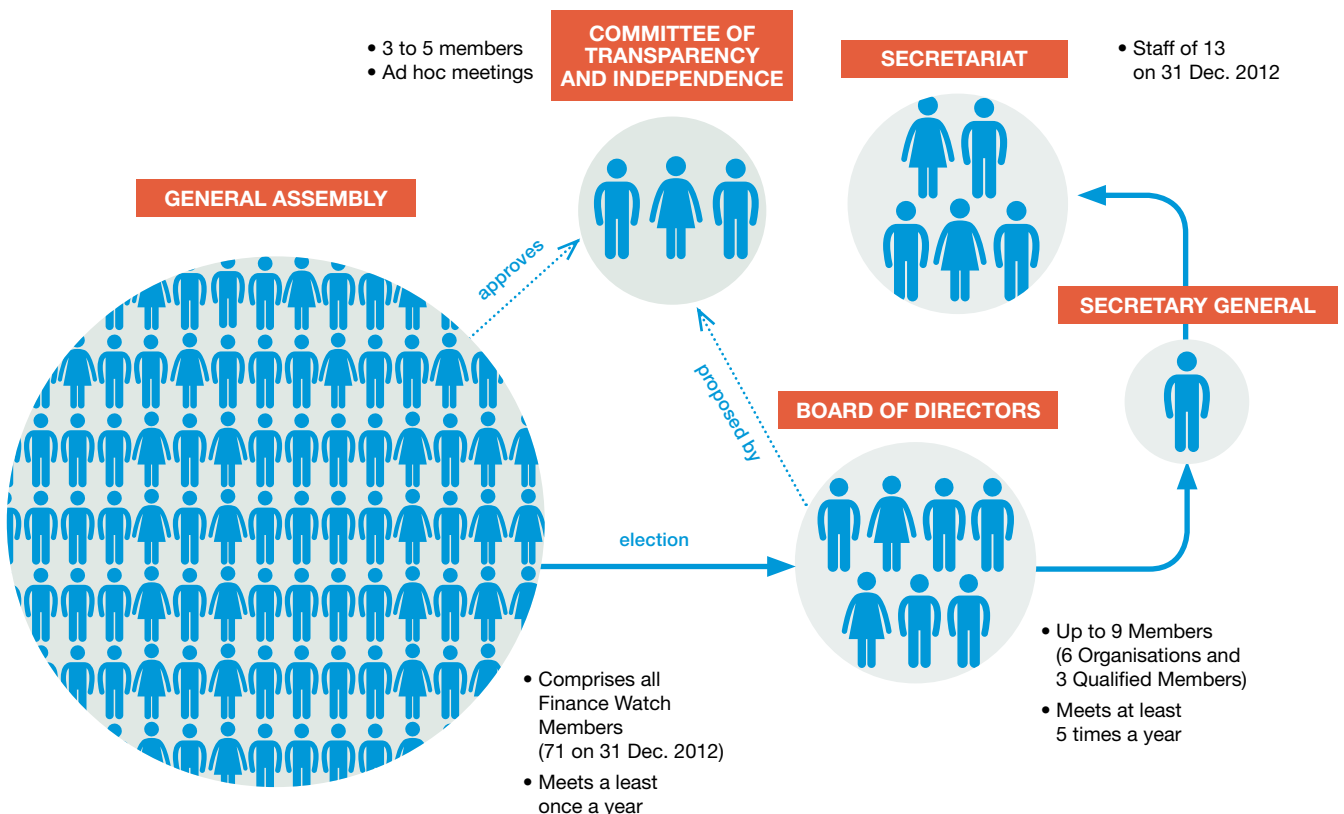


UNI Europa, represented by **Oliver Roethig** (German), UNI Europa Regional Secretary.



Wolfgang Köhler (German), freelance journalist and author, former business and financial editor of "Die Zeit" and former financial editor of "Wirtschaftswoche".

The Board is currently composed of eight members, following the resignation from the Board of EuroInvestors Managing Director Guillaume Prache. The Board is organising the nomination of a new Board member in 2013.



GOVERNANCE

GENERAL ASSEMBLY

The General Assembly is Finance Watch's highest governance body and comprises its Members. It meets at least once a year to debate and approve Finance Watch's key action priorities, to approve the budget and accounts, elect Board directors and approve members of the Committee of Transparency and Independence, among other things.

BOARD OF DIRECTORS

The Board of Directors comprises up to nine members elected by and from the General Assembly including up to six representatives of Member Organisations and up to three Qualified Members. Directors sit for three years, renewable once. The current Board was elected at the inaugural General Meeting in Brussels on 30 June 2011 and will serve until 2014. Board members are not paid for their services.

The Secretary General attends Board meetings in order to coordinate decisions with the secretariat, but may not vote on Board decisions. The Head of Operations of Finance Watch acts as secretary to the Board. Between 30 June 2011 and 31 December 2012, the Board met 14 times, including a two-day retreat in July 2012 to assess the work done so far and learn from the experiences of the first year.

Finance Watch is committed to transparency, independence and good governance.

The governance structure has been designed with these values in mind and allows for a clear separation of responsibilities.

COMMITTEE OF TRANSPARENCY AND INDEPENDENCE

The Committee of Transparency and Independence (CTI) comprises between three and five people, proposed by the Board and approved by the General Assembly for a term of three years, renewable once. None of the current CTI members are Members of Finance Watch. The Committee must approve all applications from new Finance Watch Members and all funding proposals above EUR 10,000. It is responsible for safeguarding the independence of Finance Watch's advocacy and avoid-

ing conflicts of interest concerning membership and funding. The Committee members are not paid for their services.

The Committee of Transparency and Independence for 2011-2014 was appointed by the General Assembly on 10 November 2011 and modified once during the General Assembly meeting of 20 November 2012.

SECRETARY GENERAL

The Board of Directors appoints the Secretary General for a term of five years, renewable once. The Secretary General reports to the Board and can be dismissed by them. The Secretary General has day-to-day responsibility for the staff, strategy, operations and output of Finance Watch.

COMMITTEE OF TRANSPARENCY AND INDEPENDENCE

COMPOSITION for 2011-2014



Michael Wiehen (German) with Transparency International since 1995, previously with the World Bank and Dresdner Bank in Frankfurt (chair).



William Dinan (Irish), School of Social Sciences, University of the West of Scotland, expert on lobbying practice and governance. He sits on the steering committee of ALTER-EU, a European NGO Alliance for Lobbying Transparency and Ethics Regulation.



Anne-Catherine Husson-Traore (French), chief executive of Novethic, a research centre on Corporate Social Responsibility. Board director of Transparency International France and a member of the ethics committee of the investment fund "Liberté et solidarités".

“ In less than two years, we have seen Finance Watch develop from a start-up into a professional expert organization, raising its voice constructively in a debate affecting all of us. ”

Rogier van der Weerd, Director of programs, Adessium Foundation

MEMBER ORGANISATIONS

as of 31 Dec. 2012

LIST

AUSTRIA

- Ecosocial Forum Europe

BELGIUM/EU

- Austrian Federal Chamber of Labour - Brussels Office
- Bureau Européen des Unions de Consommateurs (BEUC)
- CECODHAS Housing Europe
- Centrale Nationale des Employés (CNE)
- European Trade Union Confederation (ETUC)
- Friends of the Earth Europe
- Oxfam International
- Réseau Financement Alternatif
- Rosa Luxemburg Foundation, Brussels Office
- Solidar
- Transparency International - EU Office (TI-EU)
- UNI Europa

FRANCE

- Attac France
- CCFD-Terre Solidaire
- Confédération Générale du Travail (CGT)
- Fédération CFDT des Banques et Assurances
- Fédération Européenne des Cadres des Établissements de Crédit (FECEC)
- Fédération nationale de la finance et de la banque (FFB CFE-CGC)
- FIDH
- Institut pour le Développement de l'information économique et sociale (IDIES)
- Institut Veblen pour les réformes économiques
- Secours Catholique-réseau mondial Caritas
- UNSA Banques et Assurances

GERMANY

- Deutscher Gewerkschaftsbund (DGB)
- Foodwatch
- Heinrich Böll Stiftung
- ver.di (Vereinte Dienstleistungsgewerkschaft)
- VZBV (Verbraucherzentrale Bundesverband)
- Weltwirtschaft Ökologie & Entwicklung (WEED)

ITALY

- Fondazione Culturale Responsabilita Etica

NORWAY

- Norwegian Confederation of Trade Unions

SPAIN

- Fundacio Seira

SWEDEN

- Nordic Financial Unions (NFU)

SWITZERLAND

- Observatoire de la Finance

THE NETHERLANDS

- Stichting Onderzoek Multinationale Ondernemingen (SOMO)

UNITED KINGDOM

- Centre for Banking, Finance and Sustainable Development, University of Southampton
- ShareAction
- new economics foundation (nef)
- TUC/Unite
- World Development Movement

USA

- Revenue Watch

QUALIFIED INDIVIDUAL

MEMBERS

as of 31 Dec. 2012

BELGIUM

AYADI Rym

FRANCE

CHAVAGNEUX Christian
COLIN Gregori
CRINETZ Michel
GEIGER Rainer
KLEINKNECHT Patrick
LAGER Philippe
LIGER-BELAIR Philippe
LOUMEAU Philippe
MONNET François-Marie
PERRUT Dominique
REVALIER Pierre
SCIALOM Laurence

GERMANY

FRIEDERICHS Karl
KÖHLER Wolfgang
LENZ Rainer
MARTIN Pablo
NITSCH Manfred
REINERS Suleika
SCHUMANN Harald
SCHWABE Hans-Joachim

SWEDEN

KELLERMAN Christian

SWITZERLAND

BOHR Bärbel
CHESNEY Marc
SANTI Michel

THE NETHERLANDS

VAN DEN BURG Ieke

UNITED KINGDOM

GRIFFITH-JONES Stephany
LINES Thomas

MEMBERS



Finance Watch welcomes two types of Members: Organisations and Qualified Individuals.

Member organisations include consumer groups, housing associations, trade unions, foundations, think tanks, NGOs and other groups involved in promoting the interests of society. Collectively, these Members represent many millions of European citizens.

Qualified individual Members are experts in fields related to financial reform and include a number of well-known financial experts and academics.

Applications to become a Member are vetted by the Committee of Transparency and Independence (CTI) before approval by the Board. The CTI verifies that applicants are independent from the financial industry and its lobby, and from political parties, ensuring also that:

- candidate's qualifications relate to Finance Watch's objectives,

- candidates are free from conflicts of interest,
- candidates will not threaten the independence of Finance Watch in taking positions or producing expertise.

The CTI met twice physically in 2011 and held three conference calls in 2012 to discuss new membership applications. To date, all the recommendations of the CTI were followed

by the Board, including some 14 recommendations to reject membership, mainly concerning individuals who, while having good intentions and ideas, remained active in the financial industry and could not be approved without compromising Finance Watch's independence. In addition, all the founding Members of Finance Watch were reviewed by the CTI at the end of 2011.

BENEFITS OF MEMBERSHIP

MEMBERS ARE INVITED TO HELP DETERMINE FINANCE WATCH'S STRATEGIC AND OPERATIONAL PRIORITIES BY PARTICIPATING IN CONSULTATIONS AND GENERAL ASSEMBLIES. ALL MEMBERS ARE ELIGIBLE TO STAND FOR ELECTION TO THE NINE-PERSON BOARD OF DIRECTORS. IN ADDITION, MEMBERS ENJOY THE FOLLOWING BENEFITS:

- Participation in working groups that meet regularly in person and via conference call to coordinate actions with other Members and with the secretariat (in 2012, six working groups were active, focussing on MiFID II, PRIPs, CRD IV, Shadow Banking, Long-term Financing and Banking Structure - Liikanen).
- Access to all Finance Watch technical and educational materials, which can also be used in Members' own campaigns.
- Invitations to private workshops, roundtables with policymakers and priority seats at Finance Watch's public conferences.
- Regular email updates on key EU legislative dossiers (around 30-40 emails a year).
- Access to technical assistance on-demand in all Finance Watch areas of expertise.
- Access to Finance Watch's documents and contacts and to selected speaking and media opportunities.

For 2013, the Board has left membership fees unchanged at EUR 1,000 per year for organisations and EUR 80 per year for qualified individuals.

Finance Watch's founding AGM on 30 June 2011



SECRETARIAT

OPERATIONS

Head of Operations
Sylvie Delassus



12

Operations Officer
Adriaan Bayer



13

SECRETARY GENERAL

Thierry Philipponnat



1

POLICY ANALYSTS

Advisor
to Secretary General
Aline Fares



2

Sen. Pol. Analyst
Benoît Lallemand



5

Sen. Pol. Analyst
Frédéric Hache



6

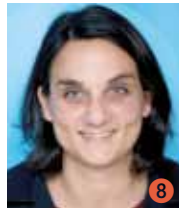
Sen. Pol. Analyst
Duncan Lindo



7

MEMBERS' COORDINATION

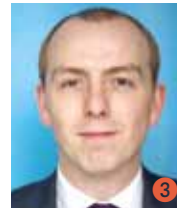
Expertise and
Campaigns Coordinator
Anouchka Nicolet



8

PUBLIC AFFAIRS

Head of Public Affairs
Joost Mulder



3

Public Affairs Officer
Katarzyna Hanula-Bobbitt



4

SECRETARIAT

The secretariat was an initial seven members in November 2011, building to 13 including one temporary contractor plus two part-time consultants in the second half of 2012. It attained its current “sustainable” minimum level of staffing in November 2012.

Staff are organised into three teams – policy analysis, public affairs and communications – supported by an advisor to the Secretary General, an expertise and campaigns coordinator, a head of operations and an operations officer.

COMMUNICATIONS

Head of Communications
Greg Ford



9

Communications Officer
Charlotte Geiger



10

Community Manager
Matthieu Lietaert



11

We would like to acknowledge the hard work and fantastic commitment of our interns who worked at Finance Watch in 2011 and 2012: Marie Fièrè and Fabien Hassan.

1 Thierry Philipponnat
Secretary General

Thierry (French) is responsible for Finance Watch's strategy, advocacy, output and staff. After graduating from the Institut d'Études Politiques de Paris and training as an economist (Diplôme d'Études Approfondies en économie), Thierry started a career in finance in 1985. His 20+ years' experience ranges from trading to devising structured equity products. In 2006, Thierry joined Amnesty International, with a particular emphasis on the impact of the financial sector on human rights. He was later elected as an Executive Board member of Amnesty International France.

2 Aline Fares
Advisor to Secretary General

Aline (French) advises the Secretary General on strategy and output, and graduated from HEC Paris. She has more than nine years' experience in banking. In her last position, she was advisor to Dexia's head of retail and commercial banking.

3 Joost Mulder
Head of Public Affairs

Joost (Dutch) coordinates Finance Watch's advocacy work, and tracks securities markets and retail issues. A former financial industry lobbyist, Joost spent four years at a leading public affairs firm and three years before that in the European Parliament advising a key member of the ECON

and IMCO Committees. His previous lobbying experience includes legislation on hedge funds, short selling, taxation, capital requirements and conglomerates.

4 Katarzyna Hanula-Bobbitt
Public Affairs Officer

Katarzyna (Polish) works with Joost Mulder on advocacy, and focuses on banking issues. Her expertise is in European financial law and regulation, government relations and strategic alliances. Most recently, she worked in public administration for the Polish Financial Supervision Authority in the analysis and international cooperation department.

5 Benoît Lallemand
Senior Research Analyst

Benoît (Belgian) is an expert in market infrastructure, asset servicing and data reporting. He has ten years' experience in the clearing and settlement industry, most recently as senior internal consultant at Euroclear. He also has roots in the NGO world as a founding member of ATTAC-Bruxelles.

6 Frédéric Hache
Senior Research Analyst

Frédéric (French) specializes in financial markets, investor protection and banking regulation. He has twelve years' investment banking experience and has worked on the foreign exchange derivatives desk of BNP Paribas as specialist in structured transactions, and similar roles at Credit

Suisse and KBC Bank. He trained in corporate treasury.

7 Duncan Lindo
Senior Policy Analyst

Duncan (British) is a former UBS investment banker who has recently completed a PhD thesis analysing banks and derivatives. He has 12 years' banking experience: first in market risk control and Value-at-Risk (VaR) and second, on a derivative counterparty risk management desk. He focuses on banking regulation.

8 Anouchka Nicolet
Expertise and Campaign coordinator

Anouchka (Swiss) has over ten years' experience in investment banking and development finance at HSBC, Swiss Re & UBS Warburg and the African Development Bank in the area of treasury risk management, and lending activities in post-crisis countries.

9 Greg Ford
Head of Communications

Greg (British) is responsible for Finance Watch's media relations and external communications. A former financial journalist, Greg spent nine years at the Financial Times Group's online service, dealReporter, covering mainly mergers and acquisitions. He was previously a tax consultant at PricewaterhouseCoopers.

10 Charlotte Geiger
Communications Officer

Charlotte (German) works with Greg Ford on press and

communications. She is a specialist in press relations, social and new media and publishing. She previously worked as press officer for a consumer organisation after gaining journalistic experience across national and cultural borders (e.g. arte TV).

11 Matthieu Lietaert
Community Manager

Matthieu (Belgian) is a multi-media strategist in the field of social media and creative visual communication. He is an award-winning filmmaker and also holds a PhD in European Political Economy.

12 Sylvie Delassus
Head of Operations

Sylvie (French) is an experienced operations manager and fund-raiser in the non-profit sector. She graduated from Ecole Polytechnique (France). She has more than twenty years' experience including eleven years in senior operations roles, and experience in start-up structures. She has previously been in charge of fund-raising for the Institut Pasteur in Paris.

13 Adriaan Bayer
Operations Officer

Adriaan (Dutch) is responsible for the day-to-day management of the office. After graduating from the College of Europe in 2008, Adriaan worked as a volunteer at two microfinance institutions in Rwanda and as an analyst at BNP Paribas Investment Partners before joining Finance Watch.

FUNDRAISING

Finance Watch does not accept money from the financial industry, the financial lobby or from political parties.

Current sources of funding include a major EU grant for 2012 administered by the European Commission, grants from philanthropic foundations and associations, membership fees and donations from private individuals (see page 40 for the financial report).

As of 31 December 2012, Finance Watch's core funding came from the following sources:

- The European Union,
- Adessium Foundation, a public benefit organisation based in the Netherlands that sponsors projects to further integrity, justice and a balance between people and nature,
- Maecenata Stiftung, a German philanthropic institute with an interest in civil society,
- Fondation pour le Progrès de l'Homme, a private Swiss grant-making foundation that supports activities which contribute to human progress through science and social development,
- Novethic, the French research centre linked to Caisse des Dépôts that specialises in corporate social

responsibility and socially responsible investment,

- Public donations from 446 private individuals,
- Membership fees from 71 Members.

The EU grant for the year 2012 was obtained through a tender administered by the European Commission for a pilot project entitled "Capacity building of end-users and non-industry stakeholders in Union policy making in the area of financial services". Finance Watch was awarded a maximum of EUR 1,025,000 to cover up to 60% of its expenses from February to December 2012, which represented our largest financial resource in the first 18 months of Finance Watch. An application under a similar tender has been made for 2013.

Finance Watch's long-term fundraising strategy is to secure reliable and diversified long-term financial resources that will guarantee both its ability to conduct its mission and its independence.

Our medium-term funding goals are to attain a good balance between institutional grants, private foundation grants and general public donations, and to build a financial buffer of 4-6 months of expenses. These goals are both expected to take some years to achieve.

Fundraising activities undertaken in the period include:

- Formal applications for multi-annual core funding were sent to private grant-making foundations in the UK, Germany, France, Switzerland, Austria, The Netherlands and the USA with programmes that fit Finance Watch's work.

All funding above EUR 10,000 must be approved by the Committee of Transparency and Independence to ensure that it:

- is unconditional,
- does not create any conflict of interest with Finance Watch's objectives,
- does not threaten the independence of Finance Watch's positions,
- complies with money laundering standards.

Finance rules the world.

Let's change the rules.

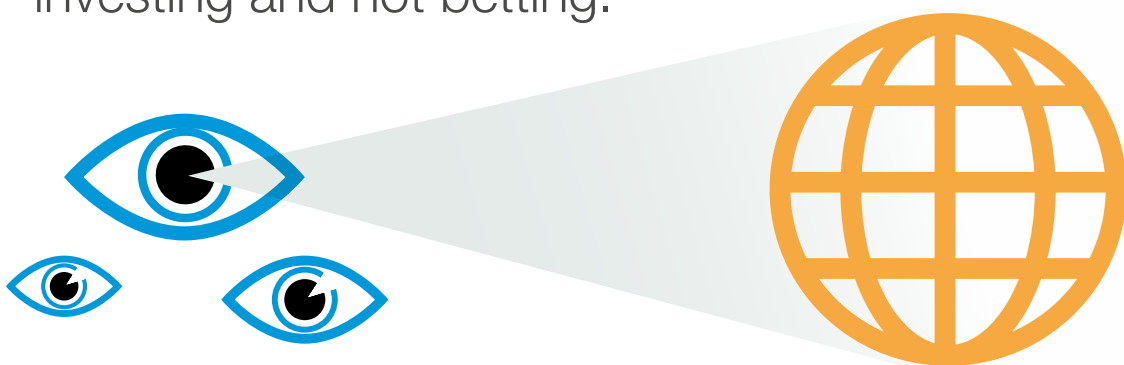


- Letters of inquiry were sent to a number of foundations for project specific funding. The first such project was a report on the EU's Bank Recovery and Resolution proposals, completed in the last quarter of 2012 with financial assistance from the Hans-Böckler-Stiftung in Germany.
- Finance Watch was approved under the "Transnational Giving Europe" (TGE) network in June 2011 after a thorough review process conducted by the Fondation Roi Baudoin.
- An upgraded online donation facility for private individuals was installed on the website.

In addition, Finance Watch has engaged a fundraising agency to build-up a strategy aimed at the general public, private foundations and other grant giving institutions. Following a competitive tender in mid-2012, the Paris-based agency, BRIEF, was assigned specific tasks including producing documentation, devising a graphical identity for fundraising and advising on fundraising strategy, which are expected to lay the groundwork for fundraising in 2013.

FINANCE WATCH'S VISION

Finance Watch's motto is "making finance serve society" - **OUR VISION** is for a sustainable financial system that serves society and is founded on investing and not betting.



We would like to see:

- a banking system that is resilient and effective and that directs credit to productive use without extracting economic rents or transferring credit risks to society, and
- financial markets that encourage productive investment in the real economy and discourage excessive or harmful types of speculation.

Before either of these can happen, our leaders and civil society must act together to break the intellectual capture and dominance of the powerful financial industry lobby.

Finance Watch is working to share this vision with the public, regulators, political leaders, academics, think-tanks, the media, economists, and the bankers and business leaders of tomorrow.

We see the following measures as essential steps towards realising our vision:

- Reduce the overall level of financialisation of society.
- Build a resilient banking system that serves society and is not founded on moral hazard (including under a Banking Union).
- Raise awareness of the policy implications of credit and money creation by the banking sector.
- Build a financial system geared towards sustainable investing.
- Limit excessive speculation (e.g. commodity speculation, HFT...).
- Channel savings into sustainable long-term investments in the real economy.
- Regulate the financial sector effectively.
- Protect the interests of the general public.
- Restore ethical behaviour to the actors of the banking and financial sectors.

"Finance Watch provides an indispensable

independent voice to counter

the power of industry lobbying"

Professor John Kay

WALK ON THE LOBBIES SIDE

Brussels is the lobby capital of Europe: several thousand industry lobbyists there target lawmakers across many industry sectors.

The financial sector has dozens of trade associations in Brussels and employs in-house public affairs staff, professional lobbying firms and law firms to make its case. Finance Watch estimates that up to 700 people are employed directly or indirectly to lobby Brussels lawmakers on behalf of the financial services industry.

Although civil society groups are present and heard by policymakers as an alternative voice, their numbers are low and coordination is sometimes difficult. A lot of the counter-expertise is present inside Member States rather than in Brussels. Users of financial services and employees in the sector are often represented in stakeholder groups but these groups are in majority composed of industry representatives.

Much of the EU's law and policy is made in stages. In theory, the proposals improve at each stage as more information comes to light. For this to happen, policymakers need to speak with different groups including different parts of the financial industry, regulators, academics, consumer groups and NGOs, among others. Each group lobbies for its own changes, leaving policymakers (the European Parliament, Council and Commission) to decide which changes to adopt and which to ignore. Some lobbying aims not to push for changes but simply to derail or delay legislative proposals.

All these groups can be described as engaging in a dialogue with policy makers in order to influence them, or lobbying.

At Finance Watch, most direct lobbying takes place in organised meetings, written exchanges and telephone calls. Conferences, events and informal meetings are also part of the process.

The target audience is often small: for example the "swing vote" in Parliament, a few Member States that could make or break a majority, or half a dozen Commission officials with responsibility for the area in question.

Public awareness has a role to play. Press and broadcast coverage sets much of the context in which lobbying takes place and informs the democratic processes; if the public is aware of an issue and concerned about it then policymakers are more likely to attach weight to it. Like politicians, lobbyists use the media to get their message across.

Lobbying requires a high level of political, technical and administrative knowledge, combined with good communication and networking skills. It is not the same as campaigning, although they are complementary and often share the same goals.

Lobbyists seek to influence European primary legislation ("Level 1") but also the pre-legislative agenda ("thought leadership" is a common Brussels buzzword) and the post-legislative technical implementation (Level 2). Like its counterparts in the financial lobby, Finance Watch aspires to be present in these areas as well.



FOCUS ON BRUSSELS AND LOBBYING

LOBBYING IN ACTION: THE CRD IV CASE

Influencing legislation is only one goal of Finance Watch's lobbying. Other goals, no less important, include introducing new ideas that were not previously on policymakers' tables and providing counter-arguments to financial industry proposals or arguments that undermine the public interest.

It is nearly impossible to measure the impact of any single actor in these situations as the outcomes are a result of many different factors and circumstances. However, it is possible to analyse final legislative outcomes to see how far Finance Watch's public interest concerns were taken into account.

At the time of writing, the CRD IV dossier was nearing completion and we provide a preliminary analysis of the outcome below. Outcomes of the other two dossiers to have completed so far (Short selling and CRA 3) can be found in Part 2.

Improvements to the legislative text

Following publication of the CRD IV proposals, financial industry lobbyists started to put forward the argument that the new rules on delever-

aging and increased capital would lead to a reduction in credit to the real economy. Finance Watch then successfully called upon EU leaders to make sure that the **deleveraging process** would be supervised. This would avoid banks meeting the new requirements by reducing lending, making sure they reduce speculative activities instead. A provision calling for supervised deleveraging was included in the 26 October 2011 Eurozone Summit conclusions.

As to the impact of increased capital requirements on **real economy financing**, we suggested that lending to retail consumers and small- and medium-sized companies (SMEs) should be stimulated through a 33% reduction of the "risk weight" applied to such loans. Members of the European Parliament largely agreed with us and applied a 24% reduction in risk weight for SME lending.

Worsening

The Basel agreement to introduce a **leverage ratio cap** in 2018 was removed from the EU's implementation during the negotiation phase. Investment banks, among others, who are often extremely leveraged, will welcome this reprieve, although

the cap may be reintroduced in a full and heavy legislative process in 2018. Thanks to small and regional banks who lobbied MEPs to hide their high leverage from public and market scrutiny, this is another large win for investment banks with even higher leverage.

Unchanged

Despite requests from Finance Watch, several bank supervisors and academics to significantly raise general capital levels to 15-20%, the European institutions chose not to do so and retained the 8% minimum total capital as defined in the Basel agreement.

Finance Watch's proposals to introduce a **residual risk weight for transferred exposures** as well as the **benchmarking of standard risk weights** using data from banks with internal models did not make it into the inter-institutional compromise despite Parliament majority support.

We proposed to **disclose the return on assets for banks**, and were supported by some MEPs. Unfortunately there was no majority in Parliament to include this requirement and the text was left unchanged on this point.

FROM GREEN PAPER TO LAW

The European Parliament cannot initiate legislation

Unlike most national parliaments, the European Parliament does not have the “right of initiative”. Only the European Commission can initiate legislation. MEPs who want legislation in a certain area have various ways to push the Commission into action, but they cannot simply start drafting a law themselves. One of the common mechanisms used by the Parliament is drafting a non-legislative report, asking the Commission to consider legislative action in a certain area. Often these “own-initiative” reports are linked to Commission consultations, where the Commission asks for confirmation of planned legislative action (White Papers) or is more generally asking for views on a certain topic (Green Papers).

Many European laws are based on international agreements

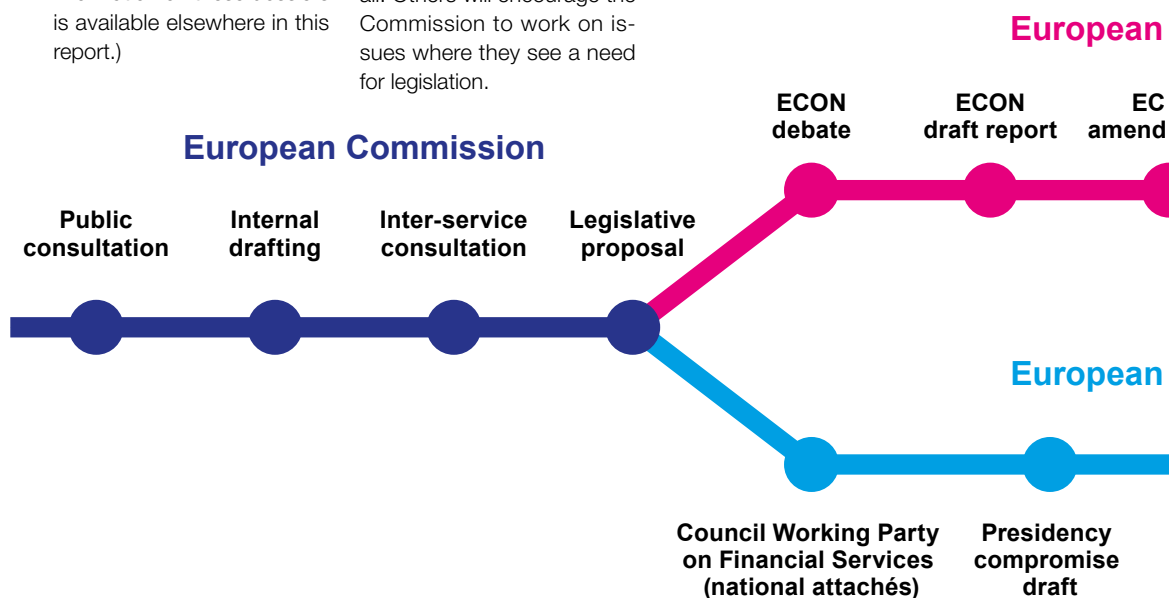
In textbook law-making, the Commission takes the time to analyze and discuss policy options in a Commission Green Paper, followed by legislative measures in a White Paper, which are then transformed in a draft law (legislative proposal for a Directive or for a Regulation). Much of the legislation proposed by the Commission these days is simply transforming international agreements into legal drafting, adding details and differentiates where needed. Examples of these are the Basel Committee’s package on bank capital requirements implemented in Europe as the CRD IV, or the G20 Pittsburgh Summit declaration which led to the development of the European Markets Infrastructure Regulation (EMIR). (More information on these dossiers is available elsewhere in this report.)

Stakeholders lobby the Commission to reflect their interests

Although a large part of the legislative agenda follows from international commitments, it is still very important to engage with the European Commission ahead of legislative proposals. When considering legislation, the Commission will hold formal and informal meetings with “stakeholders” in order to better understand the sector it is regulating, and stakeholders can respond to written Commission consultations in an attempt to influence the Commission’s thinking. Lobbyists will try to make sure that whatever the Commission proposes is in line with their interests and some lobbyists may even try to convince the Commission not to issue a legislative proposal at all. Others will encourage the Commission to work on issues where they see a need for legislation.

The Commission consults internally on the draft

Inside the Commission, financial services legislation is generally prepared by the Internal Market and Services Directorate-General (DG MARKT). Before publishing a legislative proposal, other DG’s which work on different issues such as consumer protection, industrial policy or agriculture, give their opinion on DG MARKT’s draft in a process called “inter-service consultation”. Once this is completed, the full College of Commissioners will formally adopt the legislative proposal, after which it is published and sent to the Parliament and Council so that they can give their opinion.



Parliament's rapporteur tries to find a compromise with colleagues

The Parliament's Economic and Monetary Affairs Committee (ECON) handles most financial services legislation. ECON appoints a rapporteur to negotiate on behalf of the Parliament, who starts by writing a draft report with amendments to the Commission's proposal. Some MEPs have a special role as shadow rapporteur for their political group and will try to reach agreement on compromise amendments with the rapporteur. These are voted in Committee to form the Parliament's starting position for negotiations with the Council and Commission. Lobbyists will meet with key MEPs at any stage in this process to ask them to present favourable amendments or to prioritise certain issues in the compromise negotiations.

National experts and attachés negotiate a position on behalf of their Minister

In order to define the position of the European Council, national experts and attachés from all 27 member states gather in Brussels in meetings of the Council Working Party on Financial Services, chaired by the country holding the rotating EU Presidency. Very controversial political issues are escalated to ambassadors (COREPER II) or Finance Ministers (ECOFIN), who also sign off the final negotiation position (called a General Approach) on behalf of their governments. Lobbyists will target any of these officials at any stage, in some cases up to the night before the final Finance Ministers meeting if very large interests are at stake.

'Trialogues' have short-circuited the formal system of first, second and third readings

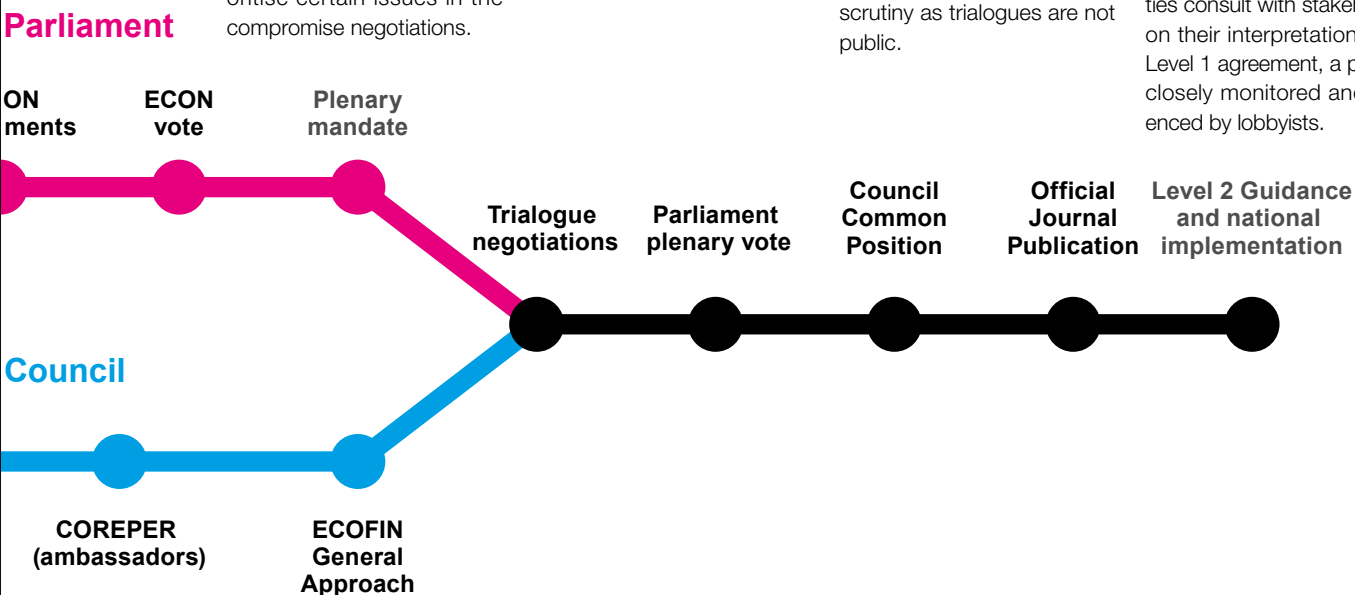
In theory, the Council issues its opinion on the Committee report voted by Parliament in plenary. If Ministers reject Parliament's position, they present their "Common Position" and the proposal makes a second tour of the institutions (second reading).

In practice, Parliament, Council and Commission representatives gather in informal dialogues to hammer out an agreement that all can accept. That agreement can then be approved in a single amendment when Parliament votes on its report in plenary, after which the Council will formally endorse the Parliament's text. Although this system usually speeds up decision-making, it comes at the expense of democratic scrutiny as dialogues are not public.

Lobbying continues on Level 2 technical standards

Approval by the Council completes the "Level 1" process, after which the text is translated and published in the Official Journal to apply from a specified date. Regulations apply directly throughout the EU while Directives must be implemented into national law, generally within 18 to 24 months.

Lawmakers can delegate the power to adopt non-legislative acts (delegated and implementing acts) on certain non-political issues to the Commission. The Level 1 text may also delegate to the Commission the power to adopt "binding technical standards" that have been drafted by the three European Supervisory Authorities (EBA, ESMA and EIOPA). In this "Level 2" process, the Commission and the authorities consult with stakeholders on their interpretation of the Level 1 agreement, a process closely monitored and influenced by lobbyists.



3 LEVELS OF INTERVENTION

POLICYMAKERS

Lawmakers, officials and regulators are targeted with meetings, events, position papers, consultation responses, hearings and written evidence, speeches, articles, letters and other policy communications.

GENERAL PUBLIC

Popular support for our mission is essential; it helps to sustain political interest in financial reform and builds Finance Watch's legitimacy to represent the wider public interest. In addition to media coverage, we target the public with newsletters to "Friends of Finance Watch", social media, the website, cartoons, blogs, postcards and non-technical summaries, all produced in three languages.

CIVIL SOCIETY

The core of Finance Watch's mission is to strengthen the voice of civil society in the reform of financial regulation. In addition to its own advocacy, Finance Watch provides tools and expertise to its Members and makes its materials freely available online for other civil society organizations and citizens who wish to engage in the policy process.

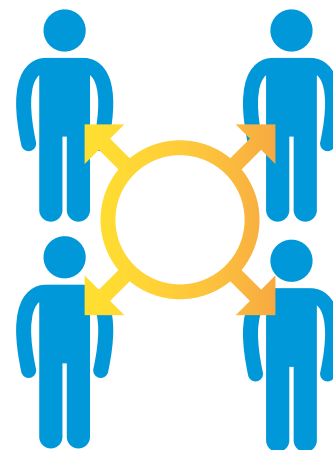
The core work of Finance Watch's secretariat consists mainly of expertise production and advocacy. This begins with analyzing legislative proposals to produce positions, and then communicating these positions to policymakers and the wider public.

EXPERTISE PRODUCTION



Analysis

European legislative proposals are analysed from a public interest perspective by the policy analysis team, which then prepares technical responses and positions.



Sharing

Expertise is shared between and among our Members via Working Groups. These groups meet in person and via regular conference calls to discuss policy issues and priorities, to share policy analysis and coordinate actions. This is facilitated by Finance Watch's expertise and campaigns coordinator.

HOW WE CHOOSE DOSSIERS

The EU has published more than 30 legislative texts on financial issues since 2010 and these only cover areas where regulators have agreed that reform is both necessary and possible. To achieve its vision with limited resources, Finance Watch has to be highly selective in choosing which legislative dossiers to react to and on which other issues to engage proactively.

Its guidelines for choosing both **reactive** and **proactive** topics are as follows:

- Topics on which the **impact of finance on society and public interest** is particularly important.
- Topics on which Finance Watch has the **capacity to deliver** given limited resources.
- Topics on which Finance Watch can **make a difference** through its depth of analysis.
- Topics on which Finance Watch can have a **meaningful impact** through an efficient lobby.
- Topics on which Finance Watch can **voice the general interest of society as expressed by its Members collectively**, and go **beyond specific particular interests** of individual Member organizations.

HOW FINANCE WATCH WORKS

ADVOCACY



Communication

Press and broadcast coverage is used to reach policy makers, for example with targeted press releases, and the general public using accessible materials across a range of platforms. Media interviews are a central part of this work.



Engagement

The public affairs team engages in a dialogue with politicians, civil servants and supervisors, acting in close coordination with Members via the Working Groups. Engagement also includes hosting public events and speaking engagements carried out by the Secretary General and other staff at external conferences and events.

The secretariat's daily work also includes essential fund-raising and operational work.

The choice of topics is approved by Members at a General Assembly, acting on a proposal from the Board. The Board's proposal is based on advice from the secretariat and consultation with Members. Topics approved by the General Assembly become mandatory for the secretariat. The secretariat can work on other topics in addition to mandated topics provided that they meet the criteria above and there is sufficient resource.

Annual work plans are submitted for Members' approval in advance every year in November. In addition, a three year strategic plan for the period 2013-2016 is now being developed with Members.

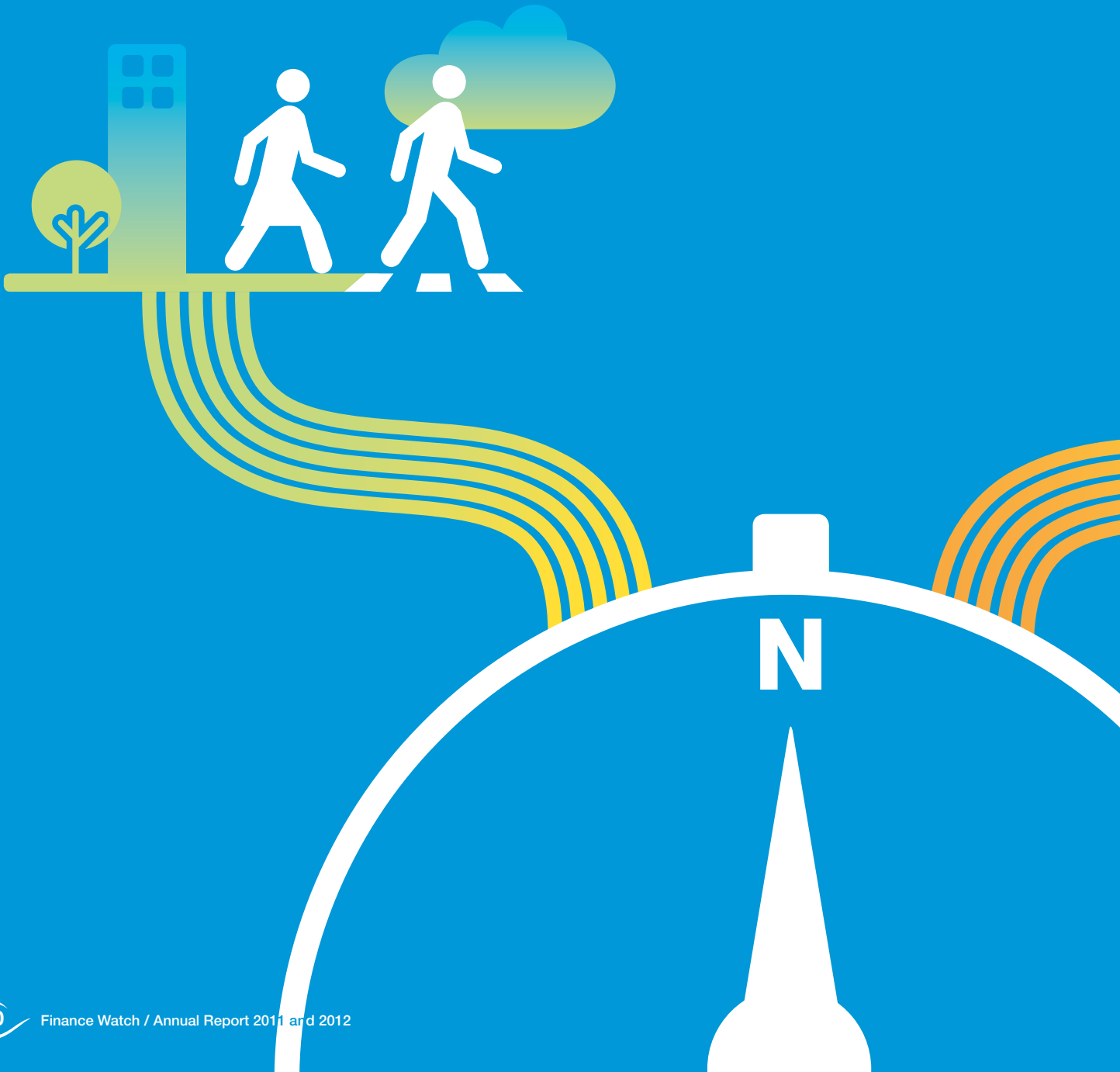
The Board's draft Strategic Plan for 2013-2016 was presented to Members at the 19-20 November 2012 General Assembly. Members were invited to comment in writing by 5 January 2013. The Board's revised Strategic Plan was approved by Members at the 19 April 2013 General Assembly.



Finance Watch

Making finance serve society

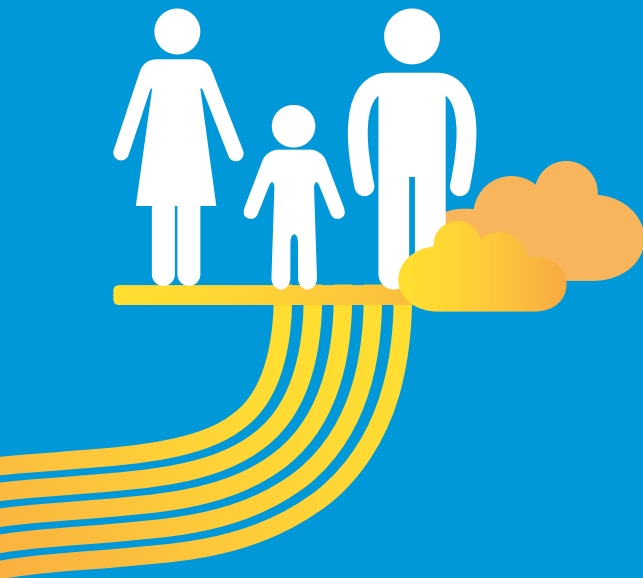
DOSSIERS



FINANCE WATCH WORKED ON THE FOLLOWING DOSSIERS IN 2011-2012:

- P 22** CRD IV* – the EU’s implementation of Basel III international standards on bank capital
- P 24** Liikanen / Banking structure – the structural reform of large universal banks
- P 26** Banking Union – European plans for bank recovery and resolution, deposit protection and supervision
- P 27** Shadow Banking – regulation of non-bank credit intermediation
- P 28** MiFID II/MAD II* – rules on financial markets
- P 30** Benchmarks – regulation of price benchmarks and indices such as Libor, Euribor
- P 31** Short selling – rules about speculative short trading positions
- P 32** PRIIPs* – consumer protection for complex investment products
- P 33** UCITS V* and future of UCITS consultation – consumer protection for standard products
- P 34** CRA 3 – credit ratings agencies
- P 35** Long-term financing – measures to increase the allocation of capital for long-term use
- P 36** Other interventions

* Topics mandated by the General Assembly for 2011-2012 (see page 19).





CRD IV

/ CAPITAL REQUIREMENTS DIRECTIVES

CRD IV is the EU's legislative proposal to implement Basel III, the international agreement on bank capital standards agreed at G20 level.

It replaces the EU's earlier capital requirements directives with a package consisting of a new Directive and a Regulation, also known as CRD IV/CRR. The CRD IV package raises capital and liquidity requirements for European banks to make banks more robust in a crisis and harmonises the European framework for bank supervision through the implementation of a "single rulebook".



CALENDAR

May 2013

Formal approval of agreement by Council

April 2013

Formal approval of agreement by Parliament

27 February 2013

Tentative agreement between the Parliament and Council

30 May 2012

Parliament report adopted by ECON and tabled for plenary

16 May 2012

Finance Watch
"Basel 3 in 5 Questions"

15 May 2012

ECOFIN General Approach

27 March 2012

Finance Watch conference
on fragility and effectiveness
of the financial system

1 April 2012

Finance Watch cartoon version
of Basel III

2 February 2012

Finance Watch position paper
"To end all crises?"

14 December 2011

Parliament draft report

11 October 2011

Finance Watch gives evidence at
ECON hearing

20 July 2011

CRD IV proposal from European
Commission

LEGISLATIVE ACTIVITY

- The Basel Committee on Banking Supervision finalised the Basel III accord in 2011, partly as a response to the financial crisis. The agreement requires bank supervisors around the world to demand that banks have higher capital, less leverage and better liquidity, among other things.
- The European Commission published its CRD IV / CRR proposal on 20 July 2011. In addition to implementing Basel III, the legislation aims to "strengthen the resilience of the EU banking sector while ensuring that banks continue to finance economic activity and growth". Key elements of the package included the introduction of a leverage cap and of liquidity ratios, a strengthening

of the amount and definition of capital and some measures to address shadow banking issues.

- Parliament rapporteur MEP Othmar Karas (EPP, Austria) published his draft report on CRD IV/CRR on 14 December 2011 and the ECON Committee adopted the report after various debates on 30 May 2012. In the European Council, Finance Ministers adopted a "General Approach" on 15 May 2012, which started compromise negotiations with the Parliament. On 27 February 2013, a tentative agreement between the institutions was announced. Implementation is foreseen by January or July 2014.



FINANCE WATCH'S VIEWPOINT

The financial crisis of 2007/2008 revealed a double failure in bank capital: equity was too low and debt was not allowed to play its loss-absorbing role because banks were not allowed to fail.

The CRD IV package should improve individual bank resilience by increasing equity. However, the capital levels proposed are below what is needed to absorb most of the bank losses experienced in the last crisis.

CRD IV does not address the problem of too-big-to-fail, in which banks are effectively insured by the state against failure and so take bigger risks (also known as moral hazard). It also does not reduce the systemic risk caused by high levels of bank inter-connectedness. These are being partly addressed by other bank reforms (see Banking Union including bank resolution and recovery plans, Shadow Banking, and Liikanen/ Banking structure).

Finance Watch's recommendations for CRD IV / CRR include:

- raising the Tier 1 Capital requirement to 10% of risk weighted assets (RWA) which would be closer to average historical levels over the last 100 years;
- introduction of a binding leverage cap between 5% in normal times and 3% in times of crisis (20x to 33x), calculated using gross derivatives exposure. Such a cap would reduce the risk

of pro-cyclical deleveraging while capping the level of risk, and should be binding from 2015 with disclosure before then;

- reducing potential conflicts of interests linked to credit risk transfer, through requiring a 25% residual risk weight requirement against transferred exposures;
- measures to ensure that loans to non-rated businesses do not receive an unfavourable treatment compared to loans to rated entities by replacing the Standardized Approach for calculating risk weights for unrated business loans with the average risk weight calculated under IRB for similar businesses (calculated for each country by the European Banking Authority);
- reducing the risk of risk weight manipulation through requiring a benchmarking of banks' internal models against a standard portfolio;
- measures to reduce investors' focus on return on equity by disclosing return on assets among a bank's key performance indicators;
- other measures on the governance of banks, on zero risk weighting (including for sovereign debt), and on implementation dates.

Finance Watch also made proposals in its position paper about structural separation, supervised deleveraging, the tax treatment of debt, and shadow banking.

Finance Watch Members have been very active on the dossier,

with 18 individual and organisational Members

forming a Working Group to coordinate their actions.



ACTIONS OF FINANCE WATCH

As a centrepiece of the EU's financial reforms (and Finance Watch's first technical dossier), CRD IV/CRR proved central to much of Finance Watch's work in 2011 and 2012.

Finance Watch Members have been very active on the dossier, with 18 individual and organisational Members forming a Working Group to coordinate their actions. The Working Group held regular conference calls throughout the year and attended a **workshop** organised by Finance Watch staff in Brussels entitled "How to Reorganize the Banking Sector" on 24 February 2012.

Secretary General Thierry Philipponnat gave evidence on the legislative proposals at a European Parliament **ECON Committee hearing** on 11 October 2011. His evidence focussed on the importance of leverage as a prudential tool, among other things.

In the same month, as fears were growing that the Eurozone crisis could threaten the solvency of banks in Europe, the European Banking Authority (EBA) lifted capital requirements temporarily. Finance Watch

published an **open letter** on 19 October 2011 calling on Heads of State and Government of the European Union to ensure that any bank deleveraging that resulted would be done without hurting the real economy. One week later, the Council included a reference to the need for "**supervised deleveraging**" in its 26 October Eurozone Summit statement. EBA followed up on 8 December with details of a recapitalisation strategy for European banks that included recommendations not to restrict lending to the real economy.

Finance Watch's **position paper** on CRD IV/CRR, "To end all crises?", was published on 2 February 2012. The 38-page document, which presented the recommendations above with a full overview of supporting analysis, was praised by policymakers for its quality and was quickly translated into proposals for MEPs legislative amendments.

The following month, Finance Watch hosted a **conference** in the cinema at Galleries de la Reine in Brussels, entitled "Finance and Society

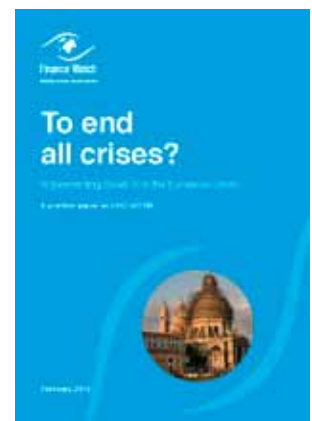
Conference 2012 - addressing fragility and effectiveness of the financial system". The speakers included Commissioner for Internal Market and Services Michel Barnier, along with FT economics commentator Martin Wolf, Société Générale CEO Frédéric Oudéa, EBA chair Andrea Enria, Eurofi chair Jacques de Larosière, and Stanford Professor Anat Admati, among others. For more details, see "Events" on page 43.

The technical nature of the dossier led to calls for Finance Watch to provide non-technical explanations of its position and of the regulation on bank capital. This led to publication on 1 April 2012 of a **cartoon version of Basel III**, which was widely circulated on social media and viewed more than 2000 times on YouTube, and a 20-page simplified **primer on bank capital** called "Basel 3 in 5 questions" published in pdf form on 16 May 2012. Both were translated into French and German.

For more details on the outcome of this dossier, please see "Lobbying in action" on page 15.



Senior policy analyst, Frédéric Hache, in an online debate about bank reform.



Position paper on CRD IV



Weak proposals on bank leverage are about as useful as a 400km/h speed limit on roads.



LIIKANEN

/ BANKING STRUCTURE

The EU's High Level Expert Group on structural aspects of the EU banking sector, led by Bank of Finland Governor Erkki Liikanen, was appointed by the European Commission to examine whether the current EU banking regulatory reform agenda should include structural reforms to increase stability and customer protection.



Erkki Liikanen at Finance Watch AGM 20 November 2012.

LEGISLATIVE ACTIVITY

In November 2011, Commissioner Michel Barnier announced his intention to set up a High-level Expert Group (HLEG) to consider in depth whether there is a need for structural reforms of the EU banking sector or not. The Group started its work in February 2012 and ceased its operation after publication of the final report in October 2012. During the course of its work the Group invited any interested parties to submit their comments and responses to its consultation related to bank structural reform. From 3 May until 1 June 2012 the Group received 80 responses, among them a Finance Watch contribution.

The five main HLEG recommendations in the final report presented to the European Commission on 2 October 2012 are:

- Banks' proprietary trading and other significant trading activities should be placed in a separate legal entity (but this entity can remain as part of a banking group) if above a given threshold;

- Resolution authorities should request further separation if necessary to enhance the operational continuity of critical functions;
- Bail-in liabilities should be more clearly defined, both to increase overall loss absorbency and to provide greater certainty to creditors;
- Risk weights should be more robust; and
- Various corporate governance reforms.

On 3 October 2012 the Commission announced that it would seek public feedback on the Expert Group's report. The consultation closed on 13 November 2012. Finance Watch submitted its written contribution. The Commission working plan for 2013 indicates that the legislative follow up based on the HLEG findings should be published around summer of 2013.

FINANCE WATCH'S VIEWPOINT

Finance Watch believes that current legislative initiatives including the Capital Requirements Directive (CRD IV), bank recovery and resolution framework, and Banking Union would have a positive impact only if combined with structural reform.

Implementation of those measures without a simultaneous reform of banking structure would risk missing the stated objective of breaking the vicious circle between banks and sovereigns and possibly increasing the negative consequences of the moral hazard situation currently prevailing in the banking sector.

In its consultation response from November 2012, Finance Watch explained why the public interest arguments claimed by the banking industry in support of the so-called "universal banking model" are substantially incorrect. At the same time, it explained why separation

would benefit both investors and the economy.

Finance Watch's response to the Liikanen recommendations, submitted to the Commission's consultation in November, argued that:

- Additional measures are needed to prevent the leakage of risk between the trading and deposit-taking parts of banks. Under stressed circumstances there is a high risk that the owners of a financial group could use funding resources available in the group (e.g. from the deposit bank) to try and avert a failure of the trading entity and therefore of the entire group.
- The proposed thresholds and boundaries above which trading activities must be separated from commercial activities could be adjusted to increase their effectiveness. We propose a threshold of 5% of assets held for trading, compared with the 15-25% range

proposed, having in mind the objective to tackle moral hazard, the consequences of keeping under the same roof activities of a radically different nature and the necessity of building a workable resolution and recovery framework.

- The analysis that capital adequacy requirements should be materially higher than under Basel III/CRD IV as stated in the Liikanen report is correct and should be reflected in EU bank regulation.
- Proposed changes to bank remuneration and governance should be welcomed, including the use of bail-in bonds as part of the variable remuneration of bank employees.

Finance Watch believes that any reform less ambitious than that proposed by the Liikanen Group would be economically meaningless, making little or no impact on the current structure of the European Banking system.

The Liikanen proposals are not just another regulatory initiative; they are the heart

of the matter. Problems linked to bank structure, activities and size have been profoundly

negative for the EU's economy. Structural reform is an essential first step to putting that right.



ACTIONS OF FINANCE WATCH

Finance Watch has been an active participant in the debate about bank structure.

On 29 March 2012, Finance Watch attended a hearing before HLEG members, where it questioned whether the current structure of the banking industry was efficient at channelling resources to serve the needs of banks' customers and at creating a sufficient level of competition between banks. Finance Watch proposed four possible solutions to establish a safe, stable and efficient banking system that serves the needs of citizens and of the EU economy, with a particular emphasis on the reduction of systemic risk and moral hazard and the promotion of competition.

On 1 June 2012, Finance Watch submitted an 18-page written response to the HLEG's consultation. The response detailed the size and implications of the public funding subsidy to large banks and related moral hazard, and proposed a number of near and longer term solutions to address these problems. These ranged from full separation to better disclosure and focussed on ways to control the size and use of large publicly-underwritten bank balance sheets.

On 24 October 2012, Finance Watch was invited to participate as a panellist in the CEPS lunch: "Reshaping the EU banking sector structure".

On 25 October 2012, Finance Watch presented an opinion on "Why the EU needs to reform banking structure in parallel with building banking union" at a DG MARKT meeting for EU Officials.

On 13 November 2012, Finance Watch published its 17-page response to the Commission's HLEG consultation, following publication of the final report. In summary: **"The Liikanen diagnosis is right but the medicine may not be strong enough."**

Finance Watch's position on Liikanen has been widely picked up in the press, especially in France and Belgium, with headlines including *"Modèle économique des banques: les six mesures de Finance Watch"* (La Revue Analyse financière de la Société française des analystes financiers, SFAF, 1 October 2012), *"EU review wants bank trading ringfenced"* (Financial Times, 2 October 2012), *"La séparation des activités est un enjeu démocratique"* (Le Monde, 8 October 2012), *"Les propositions du groupe Liikanen*

sont un strict minimum', selon Finance Watch" (La Tribune 14 November 2012), and *"Liikanen : un strict minimum pour mettre les finances publiques à l'abri des faillites bancaires"* (RTBF, 29 November 2012).

On 20 November, Erkki Liikanen presented his proposals to Finance Watch Members at their Annual General Meeting in Brussels and participated in a question and answer session with Finance Watch Members. Among other things, he told the Finance Watch General Assembly that "investment and commercial banking cultures should be separated" and that "society needs a new social contract with banks".

Meanwhile, some European countries have announced their own national reforms to banking structure in moves that could pre-empt the Liikanen proposals. France announced a plan to reform the French banking sector on 19 December 2012 and Germany and the UK have also tabled their own reforms. Starting with an open letter in December 2012, Finance Watch has been engaging with policymakers on the French reform to try and add substance to it.



CALENDAR

Q3 2013
Commission expected to publish legislative follow-up

13 November 2012
Finance Watch responds to the Commission consultation

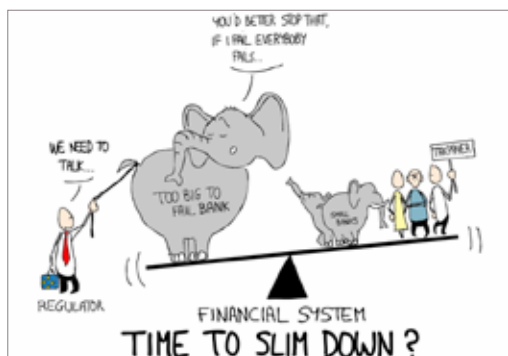
2 October 2012
HLEG presents its final report to the Commission

1 June 2012
Finance Watch submits written consultation to the HLEG

29 March 2012
Finance Watch gives evidence at HLEG hearing

February 2012
HLEG members appointed. Finance Watch's vice-chair, Monique Goyens (BEUC), is selected to serve on the 11-person panel

November 2011
Commission announces creation of High-level Expert Group (HLEG) on reforming the structure of the EU banking sector, led by Erkki Liikanen



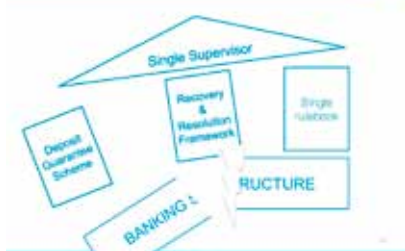
Despite all the bank reforms proposed, the problem of too-big-to-fail banks has not yet been fixed.



BANKING UNION

The European Banking Union is a political vision for more EU integration with the objective to strengthen and extend the regulation of the banking sector. Its four pillars are a single rule book for financial institutions, a Single Supervisory Mechanism (SSM), a harmonised system of deposit guarantee schemes (DGS), and a Single Resolution Mechanism.

WHAT IS THE PROPOSITION FOR FINANCE WATCH?



CALENDAR

13 December 2012

Finance Ministers agreement on establishing a Single Supervisory Mechanism (ECB and EBA powers)

28 November 2012

vote in ECON Committee on the Single Supervisory Mechanism (ECB and EBA powers)

24 and 26 October 2012

Finance Watch presents its position on Banking Union and bank structure to European Commission staff and the Finethikon conference

2 October 2012

High level Expert Group on reforming the structure of the EU banking sector final report (Liikanen Report)

12 September 2012

Commission proposes a Single Supervisory Mechanism

29 June 2012

Eurozone leaders call for Banking Union legislation

6 June 2012

Commission proposes EU framework for bank recovery and resolution

LEGISLATIVE ACTIVITY

The goal of the Banking Union is to foster financial stability in Europe. The European sovereign debt crisis has led to claims that financial stability cannot be managed effectively at the national level because of the “vicious circle between banks and sovereigns”, and that this can be resolved with a Banking Union that breaks the sovereign-bank “doom loop”.

The summit of euro area heads of state and governments on 28-29 June 2012 put the objective of creating a European Banking Union on the political agenda, leading to a set of European Commission proposals, namely:

- consultative work on the structure of the European banking industry, initiated by the

Liikanen report, which should lead to a legislative proposal;

- legislative proposal for a bank recovery and resolution framework ;
- proposal for a Banking Union, including an SSM at European level supported by a single rule book, combined with improved deposit guarantees.

In its “Roadmap towards a Banking Union”, the European Commission proposed on 12 September 2012 how to establish an SSM. A bank recovery and resolution mechanism had already been proposed on 6 June. Finally, on 2 October the High Level Expert Group on reforming the structure of the EU banking sector chaired by Erkki Liikanen published its report.



FINANCE WATCH'S VIEWPOINT

Banking Union can be an important step towards building a resilient EU banking sector, provided that several other conditions are met. Finance Watch believes that each of the associated proposals is a crucial piece in the overall framework but the problems will not be resolved by a European Banking Union alone unless it goes hand in hand with a thorough reform of banking structure and appropriate resolution mechanism for failing banks.

The Banking Union proposal as such does not address moral hazard: it simply moves it up to the European level. Taken on its own, Banking Union might actually increase moral hazard unless adequately funded crisis management and bank resolution measures are implemented, a robust bail-in mechanism is put in place and banks are subject to structural separation of their commercial and investment banking activities.



ACTIONS OF FINANCE WATCH

In October 2012, Finance Watch Secretary General Thierry Philipponnat spoke at the Third Congress on Finance Ethics in Zurich, the “Finethikon”, as well as at a European Commission (DG Internal Market and Services) conference about the problems of moral hazard and banking structure that needed to be taken into consideration when establishing

a European Banking Union. In his **presentation** he gave an overview on the three different reform initiatives that are closely linked (Banking Union, bank recovery and resolution mechanism, and the Liikanen report on banking structure) and proposed a way how to make the Banking Union work:

1. reform the banking structure with a view to drastically

reducing moral hazard and the threat it represents to resolution and supervision mechanisms,

2. put in place resolution mechanisms that allow banks to fail without putting taxpayers' money at risk,
3. appropriate governance and accountability of the Single Supervisor.



SHADOW BANKING

LEGISLATIVE ACTIVITY

The debate on how to regulate shadow banking was initiated by G20 leaders in Seoul in 2010 and followed up with the conclusions of the Cannes summit in 2011. Leaders assigned responsibility for overseeing the tasks to the FSB, which initiated five regulatory workflows to develop policy recommendations. The **FSB's five workflows**, most of which reported in the last quarter of 2012, are:

- interaction between banks and shadow banking entities (BCBS)
- mitigation of systemic risks of Money Market Funds (IOSCO)
- assessment of existing securitisation requirements (IOSCO with BCBS)
- other shadow banking entities (FSB)
- securities lending and repos (FSB)

The European Commission published a **Green Paper** on shadow banking on 19 March 2012. The paper gives an overview of current shadow banking initiatives and analyses the outstanding issues, with the aim of proposing an appropriate regulatory framework and system of supervision.

Parliament adopted a non-legislative report on shadow banking in plenary on 20 November 2012. The report suggests different ways to identify systemic risk by creating a central EU database on repo transactions, setting up a central registry for risk transfers and introducing measures to consolidate off-balance sheet entities, such as SIVs and conduits, for accounting purposes.

The Commission's legislative follow up is expected in Q2, 2013.

Shadow banking is the system of credit intermediation that involves entities and activities outside the regular banking system and its regulation, according to the Financial Stability Board (FSB). Shadow banking entities include Special Purpose Vehicles (SPVs), conduits and Special Investment Vehicles (SIVs) which are often funded by banks, money market funds, Exchange Traded Funds (ETFs) and some hedge funds, among others.



FINANCE WATCH'S VIEWPOINT

Shadow banking provides an additional pro-cyclical supply of credit to the economy and can create several systemic issues, from the provision of enormous additional leverage outside the scope of the regulator but highly interconnected with the traditional banking system, to a weakening of bank capital

regulation, since a significant part of shadow banking only exists for regulatory arbitrage purposes.

The main goal of regulation in this area is not to stop non-bank credit intermediation altogether but to ensure that the risks it generates are monitored and addressed.



ACTIONS OF FINANCE WATCH

Finance Watch organised a **Members' workshop** on Shadow Banking on 13 March 2012 and followed up on 1 June 2012 with a 16-page **response to the Commission's consultation** on its Green Paper.

The consultation response broadly supported existing regulatory initiatives and identified some key areas of risk: new channels of contagion; conflicts of interest

in areas such as mortgage securitisation; flawed credit risk transfer; and shadow banking's contribution to pro-cyclicality, among others.

It also backed additional regulations and resources to help supervisors monitor the new rules and their possible unintended consequences. Finance Watch warned against US-EU regulatory arbitrage and called for measures

such as redemption gates to make money market funds safer from runs.

The response called for measures to reduce risks from securities lending, repurchase agreements and rehypothecation of client assets. It called for more disclosure of banks' exposure to covered bonds and for higher retention requirements for banks' securitisations.

Parliament's non-legislative report echoed many of the suggestions made by Finance Watch in response to the Commission's consultation, most importantly on ratings, repurchase agreements and asset encumbrance, despite heavy industry lobbying. Parliament also asked the Commission to study the impact of (increased) ETF investments on underlying markets.



CALENDAR

20 November 2012
Parliament adopts non-legislative report in plenary

14 August 2012
Parliament rapporteur MEP Said El Khadraoui (S&D, Belgium) presents draft report

1 June 2012
[Finance Watch responds to Commission consultation](#)

19 March 2012
Commission consults on Shadow Banking Green Paper

27 October 2011
FSB report for G20 on shadow banking



MIFID II

/ MARKETS IN FINANCIAL INSTRUMENTS DIRECTIVE

The review of the Markets in Financial Instruments Directive (MiFID II) aims to make financial markets more efficient, stable and transparent. It is a landmark financial reform for the EU and covers market structure, over-the-counter derivatives trading, high-frequency trading (HFT), commodity derivative speculation and investor protection, among other topics.



CALENDAR

End-2013
indicative date
for legislative agreement

Summer 2013
indicative date for trialogue
negotiations to begin

26 October 2012
Parliament adopts negotiation
position in plenary

11 October 2012
Finance Watch policymaker
event on position limits
at European Parliament

10 October 2012
Finance Watch conference
"Financial Markets –
Serving the real economy?"

18 September 2012
Finance Watch/CEPS event
on inducements at European
Parliament

29 May 2012
Finance Watch gives evidence to
UK's House of Lords

24 April 2012
Finance Watch position paper on
MiFID II, "Investing not betting"

16 March 2012
Parliament draft report presented
to ECON by MEP Markus Ferber
(EPP, Germany)

13 January 2012
Finance Watch responds to
Parliament questionnaire on MiFID II

5 December 2011
Finance Watch gives evidence
at ECON Committee hearing on
MiFID II

20 October 2011
Commission publishes proposals
to revise MiFID

LEGISLATIVE ACTIVITY

The European Commission published its proposals to review the law on financial markets in October 2011, seven years after the original MiFID was adopted in 2004. The liberalisation of Europe's trading landscape that followed MiFID had several consequences, including:

- fragmentation of liquidity across an increasing number of venues
- development of dark pools and over-the-counter trading (reduced transparency due to increased complexity)
- increased high-frequency trading

To create a better regulatory framework for these new developments as well as dealing



The Financial Times' Philip Stafford interviews senior policy analyst Benoît Lallemand about HFT.

with the consequences of the financial crises, MiFID II aims to:

- move trading of "standardised" derivative contracts to regulated markets (exchanges and other trading platforms) and extend the "EMIR" requirements to centrally clear over-the-counter derivatives
- reduce the exemptions for pre-trade transparency which led to the popularity of "dark pools" (where prices and volumes are not made public prior to the trade),
- restrict high-frequency trading and excessive speculation on commodity derivatives (most importantly in agricultural products), and
- improve consumer protection for retail investors who buy financial products.

After debating more than 2,000 amendments, Parliament approved an amended MiFID II text in October 2012. Negotiations in Council working groups continued into 2013, and final legislative agreement is expected towards the end of 2013, once the Parliament and Council agree on a common text.



FINANCE WATCH'S VIEWPOINT

Finance Watch's position can be summarised as follows:

- since MiFID I, individual and institutional investors have increasingly left public markets to trade bilaterally "over-the-counter" or in private "dark" trading clubs, hurting price discovery. Finance Watch wants to end the exemptions that boosted dark trading and bring more trading back onto "lit" markets to improve the quality of public markets;
- a mixture of market fragmentation and new technology led to a boom in ultra-fast algorithmic trading. While the technology led to smaller spreads, it also opened the door to abusive and risky trading strategies by predatory high-frequency traders, harming overall price execution for traditional investors. Exchanges allowed HFT firms to locate their servers close to exchange servers to gain a speed advantage over other traders, and offered them other expensive services such as an enhanced, more complete view of the

order book. Finance Watch wants regulators to have all the tools they need to ensure that traders are treated equally, to inspect trading algorithms, and to set fees and ratios to prevent abusive HFT strategies;

- the popularity of commodity funds has contributed to increased volatility and ultimately to higher food prices for commodity end-users. Finance Watch backs "position limits" to restrict the positions that speculators can take in these markets (which were created for hedging, not for speculation) and proposes a complete ban on financial products that seek to replicate commodity price indexes;
- financial advisors who sell investment products to retail customers are sometimes subject to a conflict of interest, for example if they are paid to recommend some products over others. Finance Watch favours a ban on sales commissions that might lead to advisors recommending what is good for them, instead of what is good for the customer.



ACTIONS OF FINANCE WATCH

Finance Watch Secretary General Thierry Philipponnat attended a public hearing at the European Parliament's **ECON Committee** on 5 December 2011, where he gave evidence about whether financial markets are serving society and the real economy. He said of the original MiFID legislation: *"Finance Watch's view is that MiFID I, despite its stated intentions, is far from having reached the objective of improving market fairness, transparency, liquidity and price competitiveness with a view of improving corporations' access to capital markets and protecting investors."*

On 13 January 2012, senior analyst Benoît Lallemand submitted a 15-page response to rapporteur MEP Markus Ferber's (EPP, Germany) **questionnaire**. The questions allowed Finance Watch to introduce some of its technical recommendations on MiFID.

The full set of Finance Watch's technical recommendations was published on 24 April in a 62-page **position paper, "Investing not betting"**, built around a series of case studies. These expose the practices behind HFT, commodity index investing and dark trading, and explain how these practices undermine the contribution of

financial markets to the real economy.

The paper debunks a number of commonly held beliefs, arguing that: (i) trading venue competition has not benefitted the economy, (ii) HFT does not create liquidity, (iii) commodity index funds are not investment products and (iv) disclosure of sales incentives is not enough to resolve conflicts of interest.

It presents recent academic research on commodity speculation and food riots and social unrest, on the impact of HFT on commodity derivatives and equity market correlations, on the history of stock exchange demutualization, and on the effectiveness of financial markets over time.

The paper includes an explanatory chapter on the role and social purpose of financial markets, as well as a short background to MiFID and a non-technical summary of the paper's key points.

"Investing not Betting" was supported with web pages containing non-technical explanatory materials and multi-media resources about HFT and commodity speculation for the general public and press.

Finance Watch's positions on MiFID generated significant **news coverage**, especially in the specialist press. Headlines include *"Widespread belief MiFid II set to fail retail investors"* (Financial Times, 29 January 2012), *"MiFID 2-MiFIR: Finance Watch spells out recommendations"* (Europolitcs, 25 April 2012), *"Protagonists battle over MiFID II outcome"* (Marketsmedia.com, 26 April 2012) and *"MiFID II set for an early arrival"* (Financial Times, 14 October 2012), among many others. Stories about HFT and commodity speculation were

especially popular.

On 29 May, Finance Watch presented oral evidence to a committee of the UK's House of Lords as part of the UK's legislative scrutiny of MiFID II.

On 18 September, Finance Watch co-organized an **event at the European Parliament** with Brussels think-tank CEPS, entitled "Moving forward on investor protection", co-hosted by shadow rapporteurs Sven Giegold (Greens, Germany), Sirpa Pietikäinen (EPP, Finland), Anni Podimata (S&D, Greece), Olle Schmidt (ALDE, Sweden) and Kay Swinburne (ECR, UK). Speakers included Steven Maijor of ESMA, Theodor Kockelkoren from the Dutch regulator AFM and Alison Gay, head of the FSA's Consumer Panel. Steven Maijor strongly supported Finance Watch's proposal to ban inducements.

On 10 October, when the Parliament compromise position was nearly agreed and attention was starting to turn to Council compromise talks, Finance Watch organised a **public conference** entitled *"Financial Markets – Serving the Real Economy?"* in Brussels. Keynote speakers included Nadia Calviño, Deputy Director General for Financial Services, Directorate General Internal Market and Services, European Commission; MEP Markus Ferber (EPP, Germany and MiFID rapporteur); Thierry Francq, Secretary General, AMF; Laurent Degabriel, Head of Division, Investment and Reporting, ESMA.

The event included panel discussions on HFT and commodities, featuring regulators and a mixture of industry representatives on both sides of the debate, leading to detailed and sometimes heated exchanges,

moderated by Pauline Skypala of the Financial Times and Benoît Lallemand of Finance Watch. All conference materials, including speeches, presentations and an interactive video summary of the panel discussions, were posted online.

The day after the public conference, Finance Watch organized a private **event at the European Parliament** targeting policymakers, hosted by MEPs Olle Schmidt (ALDE, Sweden), Sven Giegold (Greens, Germany) and Arlene McCarthy (S&D, UK), entitled *"MiFID II and beyond: a public interest perspective on market structure, high-frequency trading and commodities markets"*. High-level speakers from the conference who share Finance Watch's views were able to address MEPs, along with a representative of the Commission. The event was well received and cemented bilateral working relationships on the topics.

Throughout the year, Finance Watch staff and Members worked together through our **MiFID Working Group** to explain their technical recommendations to MEPs, with regular conference calls to discuss lobbying and technical matters. The group successfully coordinated a campaign to introduce position limits in the European Council and Parliament position, through lobbying and campaigning at a national and European level.





BENCHMARKS

“Benchmark” means any commercial index or published figure calculated by the application of a formula to the value of one or more underlying assets or prices, including estimated prices, interest rates or other values, or surveys by reference to which the amount payable under a financial instrument is determined (European Commission’s definition).



The LIBOR scandal shocked regulators and the public alike and has triggered multiple high-value lawsuits.



CALENDAR

29 November 2012

Finance Watch responds to Commission consultation

24 September 2012

Finance Watch speaks at ECON Committee hearing

17 September 2012

Finance Watch responds to Parliament rapporteur’s questionnaire

5 September 2012

Commission launches consultation into a new legislative framework on benchmarks

25 July 2012

Commission proposes additional amendments to Market Abuse Directive

PRE-LEGISLATIVE ACTIVITY

News that a number of large banks had been systemically manipulating LIBOR, a widely-used interest rate benchmark, triggered newspaper headlines and regulatory investigations across a number of other markets around the world where benchmarks are set.

Regulators and lawmakers launched probes into possible manipulation of interest rate benchmarks including Libor, Euribor and Tibor, and of commodity market prices.

In July 2012, the European Commission proposed amendments to the EU’s Market Abuse Directive (MAD) which was already being reviewed, to prohibit manipulation of benchmarks and to extend its criminal sanctions regime to cover benchmark manipulation.

The European Parliament rapporteur followed with a questionnaire on *“Lessons and reform post Libor/Euribor”* and organised a high-level public hearing in the ECON Committee in September 2012.

In the same month, the Commission published a pre-legislative consultation entitled *“A Possible Framework for the Regulation of the Production and Use of Indices serving as Benchmarks in Financial and other Contracts”*.

At international level, the Bank for International Settlements and the organisation of international financial market supervisors (IOSCO) both set up special groups to examine benchmark-related issues and policy, in coordination with the Financial Stability Board.



FINANCE WATCH’S VIEWPOINT

Financial benchmarks, including commodity price indices, are in most cases de facto public goods. They affect investments and mortgages, business contracts linked to commodities and interest rates, and ultimately help to determine the cost of goods and services in the economy.

Their social benefits should therefore be maximized and the possibility for their miss-use tightly scrutinised.

There is currently a regulatory gap: financial instruments are regulated but the benchmarks on which many of them rely are not.

Finance Watch would like to see all financial

benchmarks and indices subject to regulation and strict supervision, with regulatory powers to oversee rate setting and calculation and to hold both the companies and the individuals behind benchmarks accountable for failures that cause losses for investors and consumers.

Indices should be calculated from real transaction prices, not polls or surveys, wherever possible, so they are harder to cheat.

Finance Watch also asked the Commission to consider the negative impact of commodity index funds on the way prices are formed in commodity markets.



ACTIONS OF FINANCE WATCH

Finance Watch submitted a 13-page response to a Parliament **questionnaire**, organised by rapporteur Arlene McCarthy (S&D, UK), on 17 September 2012.

On 24 September, Finance Watch Secretary General Thierry Philipponnat spoke at a public hearing of the European

Parliament’s **ECON Committee**, entitled *“Tackling the culture of market manipulation - Global action post Libor/Euribor”*. The other speakers at the hearing were Gary Gensler, Chairman of the US CFTC; Michel Barnier, European Commissioner for Internal Market and Services; Joaquín Almunia, European

Commissioner responsible for Competition; Masamichi Kono, Chairman IOSCO; Daniel L. Doctoroff, CEO Bloomberg; Joanna Cound, Blackrock; and Andrew Farrell, JMW Solicitors.

On 29 November 2012, Finance Watch submitted a 30-page response to the Commission’s **consultation**.

SHORT SELLING

AND CERTAIN ASPECTS OF CREDIT DEFAULT SWAPS



LEGISLATIVE ACTIVITY

Short selling and the “naked” use of CDS were widely used to speculate against the shares of major European banks during the financial crisis and against the sovereign debt of European countries. The resulting market instability triggered a series of bans and restrictions on those practises by national regulators around Europe.

In September 2010, the Commission proposed a Regulation to bring these measures into a common regulatory framework. The intention was to harmonise short selling rules across the EU, harmonise regulators’ pow-

ers when there is a serious threat to financial stability, and improve coordination between Member States at such times.

The text proposed, among other things, to improve disclosure of short positions and to set restrictions on “uncovered” or “naked” short positions in certain securities. Uncovered short selling is where a security is sold short without the seller first having borrowed an identical security to “cover” their position. The “naked” use of CDS is when speculators buy protection against a default without owning the underlying credit or bond.

Short selling involves selling a security one does not own and replacing it with one bought at a later date to benefit from a fall in price. Credit default swaps (CDS) are derivatives that protect against default, paying out like insurance policies if the creditor (a company or a country) defaults. Their value usually rises as a default looks more likely.

FINANCE WATCH'S VIEWPOINT

When the proposal was announced, derivatives industry representatives responded by claiming that a ban on naked CDS would increase the cost of borrowing for sovereign issuers.

This argument is technically wrong and demonstrates the danger for policymaking when an industry lobby attempts to disguise a private interest agenda behind flawed public interest arguments.

Naked use of CDS cannot lower costs for sovereign bond issuers in the primary market as no underlying bond is bought. Nor can it improve CDS liquidity in the secondary market without creating unstable market conditions, as when the American insurer AIG went bankrupt.

Even though sovereign CDS are not the cause of debt crises, they can make difficult credit situations worse by creating a mechanical “acceleration effect” on the way down.



Finance Watch's first position paper.



ACTIONS OF FINANCE WATCH

The Regulation's progress through Parliament was delayed in July 2011 after MEPs decided to postpone their final plenary vote to allow more time for negotiations with Council. Finance Watch published an 8-page **position paper**, “*Why sovereign credit default swaps do not lower the cost of funding of sovereign borrowers*”, a week after the postponement, with the aim of debunking false arguments which claimed that the naked use of CDS would lower the cost of capital for

sovereign issuers.

After the compromise negotiations, the text that was adopted reflected Finance Watch's viewpoint and included limits on uncovered short sales of shares and sovereign debt and restrictions on the naked use of CDS for sovereign debt.

However, the restrictions on CDS were rather weak as industry successfully argued for an exemption to the rule on sovereign CDSs, namely that there is no need to prove

possession of sovereign bonds if the detention of an asset “highly correlated” to sovereign bonds can be shown. In the Level 2 process it was decided that a “high correlation” (of 80%) between a long and short position was sufficient to qualify as covered. This decision weakens substantially the legislation adopted and opens the door to continued naked speculation on sovereign default.



CALENDAR

- 21 February 2012**
Council endorses inter-institutional agreement
- 15 November 2011**
Parliament plenary adopts agreement
- 18 October 2011**
Parliament and Council agree compromise
- 11 July 2011**
Finance Watch publishes position paper
- 7 March 2011**
ECON Committee adopts its negotiation position drafted by MEP Pascal Canfin (Greens, France)
- 15 September 2010**
Commission publishes draft Regulation



PRIPS

/ PACKAGED RETAIL INVESTMENT PRODUCTS

The European Commission proposed a regulation on “**Key Information Documents for Investment Products**” requiring that product manufacturers provide retail investors with a synthetic information document using plain language before they invest. The aim of this regulation is to make financial information easier to understand and to increase product comparability. We refer to this dossier as “**PRIPs**” (Packaged Retail Investment Products), as we feel this better covers its content.



CALENDAR

July 2013

Parliament plenary vote (earliest estimate)

June 2013

Negotiations between Parliament, Council and Commission

27 May 2013

ECON Committee vote

Q2 2013

Compromise negotiations between MEPs

Q2 2013

Discussions among Member States (estimate)

20 December 2012

Publication of draft Parliament report by Pervenche Berès (S&D, France)

6 November 2012

Exchange of views in European Parliament ECON Committee

31 October 2012

Publication of Finance Watch position paper

3 July 2012

Commission proposal

LEGISLATIVE ACTIVITY

In response to decreased consumer confidence in the financial sector and increased complexity of financial services, the European Commission identified information disclosure to retail investors as one area where action is needed: financial information is often full of technical jargon, too long, not understood by investors, and differs across products.

The scope of the proposal is packaged investment products, which include UCITS funds (undertakings for collective investment schemes), non-UCITS funds, insurance products linked to financial markets and other types of structured retail investment products.

Under the proposal, product manufacturers are required to set up a short synthetic Key

Information Document (KID), summarizing the key information of a financial product. This document must be distributed to retail investors before they invest.

The KID design is based on a similar document already in use for UCITS, the biggest category of investment vehicle covered by the proposal.

The new KID would help consumers to better understand and compare the risks and costs of products and make more informed and suitable investment decisions.

The regulation was proposed in July 2012.



FINANCE WATCH'S VIEWPOINT

Finance Watch thinks the EU's proposals should go further than simply introducing a KID, as effective investor protection requires more than improved disclosure.

Research shows that retail customers are far from rational when it comes to buying investment products: their decisions are often affected by cognitive and emotional biases and they rely a lot on advice from salespeople who do not always understand the risks in the products they sell.

We think the proposal should bring in rules to stop retail investors from being offered products that are not suitable for them, for example because of excessive complexity, unusual risk exposures or packaging features that exploit behavioural biases.

Investment risks cannot meaningfully be summarised in a single grade or number. We

suggest that the “summary risk indicator”, currently a number from 1 to 7, be replaced by a set of indicative performance scenarios.

Fees are only one part of the costs of structured products, as other costs are embedded in the product when it is manufactured. These are never disclosed because they are financed through additional risk-taking by investors instead of being paid in advance. As these costs also reduce returns we believe they should be disclosed, for example by displaying in the KID the theoretical margin at maturity of structured products.

Investment products have a social impact as well as a financial one, including allocating capital to productive or unproductive use. With packaged investment products representing a EUR 9 trillion market, Finance Watch recommends that products be clearly labelled as “investments” or “bets”.



ACTIONS OF FINANCE WATCH

Finance Watch published a 40-page **position paper** on PRIPs entitled “*Towards suitable investment decisions? Improving information disclosure for retail investors*” on 31 October 2012.

Many of our ideas made it into the European Parliament rapporteur's draft report, and the others were presented as amendments. At the time of writing all ideas advanced in our report were on the table

for consideration by Members of the European Parliament. As Member States want to stay close to the Commission proposal, it remains to be seen how many ideas will survive the inter-institutional negotiations.



UCITS V

AND CONSULTATION ON THE FUTURE OF UCITS /

LEGISLATIVE ACTIVITY

UCITS V is the latest update to the EU's regulatory framework for UCITS, which originally dates from 1985. In the UCITS V package presented on 3 July 2012, the Commission proposes to tighten rules on depositaries, setting out their duties and holding them liable if assets go missing. This follows shortcomings in the depositary rules revealed by the Lehman Brothers bankruptcy and the Madoff fraud.

In addition, the Commission issued a consultation on 26 July 2012 on the future of UCITS

focussing on questions about product rules, liquidity management, depositaries, money market funds and long-term Investments. This was done out of a concern that earlier revisions to the UCITS framework had opened up UCITS funds to a very broad range of investments and strategies, raising concerns about the use of derivatives or the interaction with shadow banking entities, for example.

UCITS stands for Undertakings for Collective Investment in Transferable Securities, a popular category of regulated investment vehicle that accounts for around 85% of all European investment fund assets. UCITS are popular as they provide a European-wide standard for cross-border sales of investment products and a certain level of consumer protection.



FINANCE WATCH'S VIEWPOINT

The international success of UCITS shows that robust regulation has benefitted the industry. The EU should protect the popularity of UCITS as a "regulatory brand" by correcting weaknesses introduced in earlier revisions to the UCITS framework.

The UCITS V package copies depositary liability rules and remuneration restrictions from the hedge funds (AIFMD) framework. It also introduces a harmonised sanctions regime for non-compliance with UCITS.

In its public consultation on the future of UCITS, the Commission took the opportunity to ask deeper questions about the social role of the asset management industry and its contribution to the long term funding of the economy.

Finance Watch submitted an 18-page **consultation response** on the future of UCITS on 18 October 2012, linking some of the answers to Finance Watch positions on PRIPs and MiFID.

The main points include:

- only assets that are suitable for retail investors should be eligible for UCITS funds,
- derivatives should not be allowed unless they are standard (i.e. not so-called "exotic" derivatives) and traded on exchanges,
- practices linked to "efficient portfolio

management" (such as securities lending) need careful monitoring and rules; for example collateral should not be reinvested or rehypothecated as this can increase systemic risk and weaken clients' claims over their assets,

- the proposal for a depositary EU passport could introduce new cross-border risks for UCITS investors,
- the role that money market funds (MMFs) play in funding the banking system creates a strong risk of contagion in the event of a run on MMFs,
- MMFs could be divided into short term MMFs and longer term MMFs; short term MMFs should be restricted from investing in long-term assets and structured financial instruments, while longer term MMFs would be free to invest in those assets but should be subject to redemption gates,
- if the EU decides to introduce a special category for UCITS dedicated to long-term investments, this should allow investments in the normal range of UCITS assets (apart from commodity products and possibly real estate) but have longer-term performance measurements, liquidity rules and compensation structures.



CALENDAR

Q2 2013
Commission to present strategy on MMFs (follow-up from consultation)

Q2 2013
Commission to present strategy on eligible assets for UCITS (follow-up from consultation)

25 March 2013
Commission Green Paper on Long-term financing (follow-up from consultation)

March 2013
Start of inter-institutional negotiations on UCITS V

21 March 2013
ECON vote on UCITS V negotiating position

9 November 2012
ECON publishes draft report on UCITS V by MEP Sven Giegold (Greens, Germany)

18 October 2012
[Finance Watch responds to Commission consultation on the future of UCITS](#)

3 July 2012
Legislative proposal on UCITS depositaries, remuneration and sanctions published (UCITS V)



CRA 3

/ CREDIT RATING AGENCIES

A credit rating agency (CRA) provides opinions on the creditworthiness of entities such as companies or governments and of debt instruments such as bonds. The biggest three CRAs are Standard & Poor's, Moody's and Fitch, which together cover approximately 95% of the world market. The second revision of the CRA Regulation (CRA 3) reviews the EU's regulatory framework for CRAs.



Finance Watch gave evidence to the ECON Committee at the European Parliament.



CALENDAR

16 January 2013
Parliament plenary endorses November 2012 inter-institutional agreement

September-November 2012
Negotiations between the European institutions

24 August 2012
European Parliament ECON Committee adopts negotiation position

22 July 2012
Finance Ministers agree negotiation position

15 February 2012
ECON Committee draft report presented by MEP Leonardo Domenici (S&D, Italy)

24 January 2012
Public hearing in ECON Committee (Finance Watch gives evidence)

15 November 2011
Commission presents CRA 3 review proposal

LEGISLATIVE ACTIVITY

During the financial crisis, many ratings that CRAs had issued for structured financial products proved catastrophically wrong. The G20's Financial Stability Board proposed a set of principles in 2010 to reduce reliance on external ratings, leading to regulatory action on CRAs around the world.

In April 2009, an EU Regulation was agreed that required CRAs to be registered and supervised at a European level. In 2010, the Commission proposed a review (CRA II) to move supervision to the new European Securities and Markets Authority (ESMA), extend the scope to hedge funds using ratings, reduce conflicts of interest and introduce sanctions for non-compliance.

The package agreed between the European legislators in November 2012 would:

- reduce the reliance of fund managers and supervisors on external ratings,
- control the frequency and timing of sovereign rating announcements,
- make CRAs liable if they conduct gross negligence,
- restrict cross-shareholdings of CRAs and entities being rated,
- require mandatory rotation of CRAs for some products,
- publish ratings on a European Rating Platform to improve comparability and visibility of ratings.



FINANCE WATCH'S VIEWPOINT

The central problem with ratings is an over-reliance by the entire financial system on external credit ratings. This is largely caused by three factors: financial regulations such as Basel III and Solvency II make explicit references to external credit ratings; many asset managers have internal rules linking their actions to external credit ratings (e.g. an obligation to buy "investment grade" only); and financial markets react strongly to rating upgrades and downgrades (cliff effects and herding).

Finance Watch wants references to external

credit ratings to be systematically deleted from financial regulations and the internal rules of asset managers. This is a long-term process as it will require updates to several pieces of legislation.

In addition, the letter-based ratings system used by the three large CRAs should be replaced with a simple number expressing the probability of default, backed by a narrative text. These numbers could be centralised, averaged and published by ESMA using the European Rating Index system (EURIX).



ACTIONS OF FINANCE WATCH

Finance Watch's Secretary General Thierry Philipponnat gave evidence at an **ECON Committee** hearing on ratings agencies on 24 January 2012, along with speakers from ESMA, Fitch, the Japanese Credit Rating Agency and Société Générale, among others.

He called for the current letter-based ratings system to be replaced by a simple number

expressing the probability of default. "We need something altogether more technical and less emotional," he said.

When the ECON Committee adopted its draft report in August 2012, the text included a requirement for ratings to be expressed as figures indicating the probability of default, and for ESMA to publish an aggregated rating index for any rated debt instrument and the

average probability of default.

By the time the Parliament voted in plenary in January 2013, that requirement had been diluted somewhat, appearing in the recitals that CRAs "should make investors aware of the data on the probability of default of ratings and rating outlooks based on historical performance reflected on the central repository created by ESMA".

LONG-TERM FINANCING



LEGISLATIVE ACTIVITY

The European Commission started work on a Green Paper on the long-term financing of the European economy in 2012, shortly before the European Council's "Compact for Growth and jobs" on 29 June 2012 highlighted a need for more financing of the economy. Several long-term financing issues of relevance to the EU were raised the following month in a UK report into the equity markets and long-term decision making (The Kay Review).

At international level, G20 leaders meeting in Mexico in November 2012 asked the IMF, OECD, FSB and other international institutions to report in 2013 on factors affecting the availability of long-term investment financing.

The Commission's Green Paper was published 25 March 2013 and looks at: ways to boost long-term financing capacity; the role of financial market intermediaries; access to capital for small and medium-sized enterprises; and the use of public funding to boost LTF objectives, among other things. One of the initiatives suggested in the paper is the creation of a framework for long-term retail investment products modelled after the successful UCITS framework, on which the Commission informally consulted stakeholders in early 2013. The Commission has also started to work on a review of the Shareholder Rights Directive, expected later in 2013. Finance Watch has provided input to the Commission on both of these initiatives.

Long-term financing (LTF) has emerged as a regulatory theme in response to concerns about excessive short-termism in the world's financial markets and its impact on economic performance and sustainable development. The theme connects legislative initiatives to reduce short-termism such as high-frequency trading and a financial transaction tax, to a demand-driven agenda to finance long-term real economy needs.

FINANCE WATCH'S VIEWPOINT

Addressing financial short-termism will require a re-think of our financial system, as well as a list of policy measures.

The efficient-market hypothesis and misinterpretations of Adam Smith's "invisible hand" have been used to underpin a number of fallacies: such as that long-term is simply the sum of short-term periods, that any profitable activity for an individual must also be good for society at large, that society can hedge away its risk, and that regulation is the enemy of efficient

finance, to name a few.

The consequences include a proliferation of short-term incentives among financial intermediaries and practices that encourage short-term thinking, such as mark-to-market accounting and Value at Risk.

A bigger problem is the general confusion among regulators and investors between investing and betting and a failure to take into account of whether money is put to productive use or not.



Professor John Kay was the keynote speaker at this Finance Watch event.

ACTIONS OF FINANCE WATCH

Long-term financing was one of the three internal **Working Groups** created when Finance Watch started its operations. We also organised two large workshops in 2012 to discuss long-term financing. The first, in March 2012, discussed ways to link LTF to the existing EU legislative agenda, including FTT, MiFID, CRD, Solvency II and the IORP review, as well as non-legislative initiatives that could stimulate a move away from short-term and speculative investments.

In the second **workshop** in September, Finance Watch Members were joined by a representative of the European Commission to exchange views on long-term financing and potential cures for market short-termism. On 5 October, Thierry was one of the keynote speakers at a Commission stakeholders workshop on LTF.

On 17 October, Finance Watch organised a **public conference** in Brussels, entitled "*Long Term Investing: What can the EU Learn*

from the Kay Review?" Speakers included Professor John Kay, Trelawny Williams (Fidelity), Philippe Herzog (Confrontations Europe), Jérôme Haas (ANC) and MEP Sharon Bowles (ALDE, UK and Chair of Parliament's ECON Committee). A summary of the event, its key conclusions and an interactive video were published on our website.



CALENDAR

Second half of 2013
Legislative follow-up of Green Paper

April-June 2013
Commission consultation period

25 March 2013
Publication of Commission Green Paper on LTF

17 October 2012
Finance Watch conference "*Long Term Investing: What can the EU Learn from the Kay Review?*"

12 September 2012
Finance Watch Members' workshop with Commission

23 July 2012
Kay Review published in UK

7 March 2012
Finance Watch Members' workshop

OTHER INTERVENTIONS

In addition to its core policy work, Finance Watch has either responded to or engaged in a number of *ad hoc* policy initiatives throughout the period.

28 NOVEMBER 2011 SPEECH TO EUROPEAN ECONOMIC AND SOCIAL COMMITTEE ON CIVIL SOCIETY

Finance Watch Secretary General, Thierry Philipponnat, gave evidence at a public hearing of the European Economic and Social Committee entitled "*The role of civil society in financial regulation*".

The hearing was organised by the Committee's ECO section (Economic & Monetary Union & Economic and Social Cohesion) following an EESC decision in January to draw up an own-initiative opinion on "*How to involve civil society in financial regulation*".

Other speakers included European Commissioner for Internal Market and Services Michel Barnier, EESC President Staffan Nilsson, and the MiFID rapporteur, MEP Markus Ferber (EPP, Germany).

Thierry Philipponnat spoke of the importance of involving civil society in the debate over financial regulation and the difficulty of doing this, given that it often requires specific technical knowledge. He explained how Finance Watch had been created to fill this gap.

22 MARCH 2012 LETTER TO US CONGRESS

Finance Watch wrote to Congress to urge the United States not to weaken its stance on Dodd Frank and the Volcker Rule.

In a letter to the Senate Committee on Banking, Housing and Urban Affairs, Finance Watch said that regulators on both sides of the Atlantic were being told by lobbyists that their reforms would put banks at an international competitive disadvantage and urged the committee to resist this pressure.

The letter said that, contrary to industry claims, regulation leading to a sound banking sector would bring competitive advantage as investors and corporate depositors have more confidence in financial institutions.

US Senator Jeff Merkley read the letter and had it entered into the record at a committee hearing on 22 March 2012 on "*International Harmonization of Wall Street Reform: Orderly Liquidation, Derivatives, and the Volcker Rule*".



26 APRIL 2012 SPEECH TO THE EUROPEAN CENTRAL BANK ON FINANCIAL INTEGRATION AND STABILITY

Finance Watch's Secretary General, Thierry Philipponnat, gave a speech at the European Central Bank's conference on "*Financial Integration and Stability*".

He said that, as long as the euro area does not have a risk-free rate on which to base its financial system and as long as it accepts to be built on moral hazard, then the ingredients of the next financial crisis and of its financial disintegration would remain.

He discussed the transmission mechanism between macro-economic imbalances and financial markets in the euro-area, the impact of the ECB's Long Term Refinancing Operations on the relationship between banks and sovereigns, and the consequences for interest rate divergence and cross-border lending.

Other speakers at the conference included ECB President Mario Draghi, Commissioner Michel Barnier and Peter Sutherland, CEO of Goldman Sachs International.

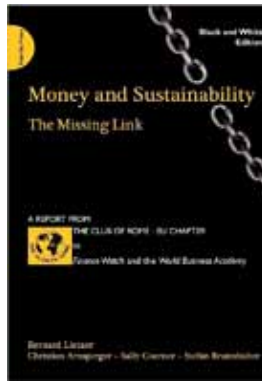
30 MAY 2012 CLUB OF ROME PRESENTED FINANCE WATCH WITH ITS REPORT "MONEY AND SUSTAINABILITY"

The Club of Rome presented its new report "Money and Sustainability – the Missing Link" to Finance Watch and the World Business Academy at an event hosted by the Club's EU chapter in Brussels on 30 May.

The Club of Rome first shocked the policy world forty years ago with its book "The Limits to growth", which raised the awkward but now increasingly accepted idea that resource-based economic growth cannot continue for ever.

"Money and sustainability" is the Club's equally challenging follow-up and makes the case for parallel currencies and competing means of exchange as a route to monetary and economic stability.

The report's lead author, Bernard Lietaer, also presented the report to Finance Watch Members during the 19-20 November 2012 General Assembly.



“ We believe that Finance Watch, beyond the mere scope of finance, is an essential tool for democracy to retain its substance. ”

Matthieu Calame, Fondation Léopold Mayer pour le progrès de l'homme



24 SEPTEMBER 2012 OPEN LETTER TO TRADE COMMISSIONER ON IMPACT OF WTO RULES ON FINANCIAL REGULATION

Finance Watch co-signed an open letter to the EU Commissioner for Trade, Karel De Gucht, on WTO rules, together with four other civil society groups: BEUC, SOMO, EuroFinuse and the Financial Services User Group.

The letter warned of the danger of EU's financial regulation being challenged or watered down as a result of the WTO's General Agreement on Trade in Services (GATS) rules.

For example, GATS prohibits commonly recommended regulatory policies, such as prohibitions on risky financial services, size limits on banks, 'firewalls' between banking and investment services and capital controls as well as other capital management mechanisms.

The letter called on the Commission to take action at an upcoming meeting of the WTO's Committee on Trade in Financial Services.

Monitoring and minor work was also carried on these work streams:

- European Market Infrastructure Regulation (EMIR)
- Corporate Governance Green Paper and Review of Shareholder Rights Directive
- Trading Book Review
- Financial Transaction Tax
- EIB Annual Report
- International trade negotiations (WTO rules on financial regulation, EU-US convergence, regulatory dialogues)



Finance Watch

Making finance serve society

OPERATIONAL REPORT



OPERATIONAL REPORT

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FINANCIAL REPORT

Resources and expenses June 2011 - December 2012

RESOURCES

<i>(in Euro)</i>	
Membership fees	57,233
Donors	1,020,783
Maecenata Stiftung	255,400
Adessium Foundation	566,666
Novethic	50,000
Fondation pour le progrès de l'Homme	60,000
Donations through website	26,577
Private donors (transfer)	62,140
EU grant	881,566
Research projects funded by third parties	7,500
Hans Böckler Stiftung	7,500
Interest on floating capital	3,677
Total	1,970,759

Finance Watch was created in June 2011. This first annual report covers the 18 month period from the founding AGM on 30 June 2011 to the end of 2012. In 2012 a pilot project grant from the European Union represented a major part of Finance Watch's resources. The aim in the coming years is to build a more sustainable funding structure by regular donations from foundations, organisations and private donors.

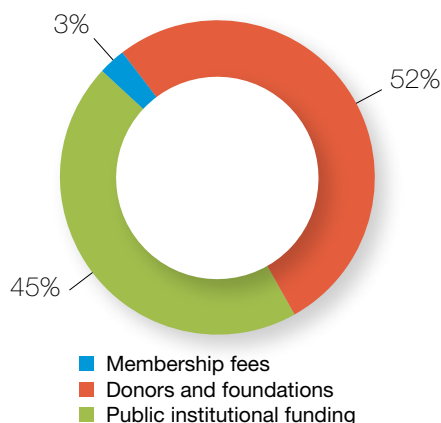
Banks and other financial firms spend hundreds of millions of euros a year lobbying in Brussels and far more than that in Washington and London. It is no wonder that some financial regulations seem to favour the financial industry rather than society. You can help us to fight back on your behalf by making a contribution to our costs so we can operate as a truly independent and effective organisation.

Thank you!

In 2011 and 2012 Finance Watch was grateful to receive donations from individual donors, foundations and pilot project funding from the European Union.

We are also grateful for the continued support of our Members.

RESOURCES 2011-2012

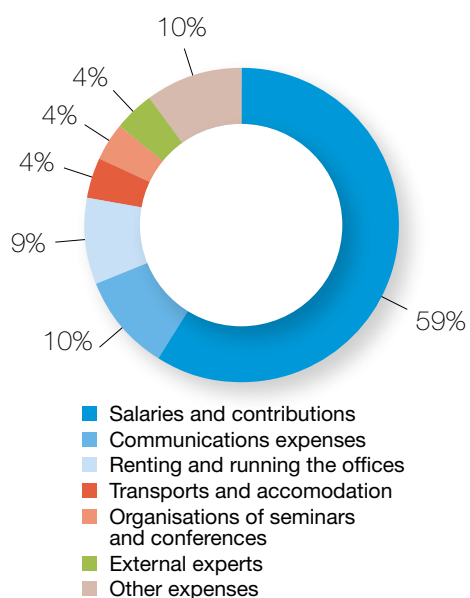


EXPENSES

(in Euro)	
Rent and associated expenses	169,329
Information services	28,570
Counsel and external services	51,857
Communications	182,808
Meetings, Events, Seminars	76,661
Research	69,664
Transport and travel	85,579
Salaries and contributions	1,092,957
Other staff costs	38,666
Investment and depreciation	30,164
Financial services	7,356
Total	1,833,611

Finance Watch's main asset is its ability to produce expertise through its staff, thus the major part of its expenses is human resources. Within the first one and a half years, Finance Watch has grown its team to 13 staff members at the end of 2012. This team size has allowed Finance Watch to work in an effective manner and therefore it is one of the priorities to make this structure sustainable.

EXPENSES 2011-2012



PUBLIC AFFAIRS MEETINGS

“ Finance Watch helps ensure that the debate on financial regulatory policy is a well informed and balanced one. ”

Trelawny Williams, Global Head of Corporate Finance, Fidelity International

As of 31 Dec 2012	European Parliament and national parliaments	Member state staff in Brussels	European Commission staff	Industry meetings (“incoming”)	Total
Markets (MiFID II/MAD, UCITS, LTI, Shadow banking)	35	16	6	29	86
Banking (CRD IV, supervision, banking structure)	22	9	6	6	43
Retail (PRIIPs)	9	2	2	1	14
Total	66	27	14	36	143

Note: This table includes formal meetings in 2011 and 2012 planned by the Public Affairs team. Informal exchanges, ad-hoc meetings and bilateral meetings between Finance Watch policy analysts or the Secretary General and national attachés, the European Commission, MEPs and their assistants and the financial industry are not included.

“ Finance Watch is exactly what Europe has long needed - an independent, thoughtful and courageous institution whose activities illuminate the necessary steps towards creating a financial system that is not only stable, but properly serves the wider social and economic interest. ”

Martin Wolf, Chief Economics Editor, Financial Times



EVENTS

FINANCE WATCH ORGANISED FIVE EXTERNAL POLICY EVENTS IN 2011 AND 2012

Three of these were public conferences with high-level and influential speakers and panellists that attracted an audience of experts, journalists, policy-makers, civil society representatives and financial industry leaders.

Finance Watch also organized two *ad hoc* events in the European Parliament: one on consumer protection on 18 September 2012 and one on high-frequency trading and commodity speculation on 11 October 2012.

All conference materials, including written summaries and interactive videos, were made available on Finance Watch's website.

"FINANCE AND SOCIETY 2012 - ADDRESSING THE FRAGILITY AND EFFECTIVENESS OF THE FINANCIAL SYSTEM" 27 March 2012

About 180 people attended and the speakers were:

Michel Barnier

European Commissioner for Internal Market and Services (DG MARKT)

Martin Wolf

Chief Economics Commentator and Associate Editor, Financial Times, member of the UK's Independent Commission on Banking

Gerald Epstein

Professor of Economics and Co-Director, Political Economy Research Institute, University of Massachusetts

Frédéric Oudéa

CEO of Société Générale

Andrea Enria

Chairperson of European Banking Authority

Anat Admati

George G.C. Parker Professor of Finance and Economics, Stanford Graduate School of Business

Jacques de Larosière

Chairman of the Strategic Committee of the French Treasury, Chairman of Eurofi and a former Managing Director of the IMF

Gernot Mittendorf

Chief Risk Officer Erste Group and former CEO of ceska sportelna

Martin Hellwig

Director, Max Planck Institute for Collective Goods

James Ferguson

Chief Strategist, Westhouse Securities

Charles Haswell

Global Head, Financial Sector Policy, HSBC

Mario Nava

Head of Banking and Financial Conglomerates Unit, DG MARKT, European Commission

Ed Kane

Professor of Finance at Boston College

Paul Sharma

UK Financial Services Authority, Director Prudential Business Unit, Policy Division

Dennis Kelleher

CEO, Better Markets

Guido Ravoet

Secretary General, European Banking Federation

Peter Thal Larsen

Assistant Editor of Reuters Breakingviews (moderator)

John Rega

Chief Correspondent, MLex FS (moderator)

Nikki Tait

Lex columnist and former Brussels correspondent, Financial Times (moderator)

Michael Robinson

BBC (moderator)

"FINANCIAL MARKETS: SERVING THE REAL ECONOMY?" WITH A FOCUS ON MIFID-RELATED ISSUES 10 October 2012

About 130 people attended and the speakers were:

Nadia Calviño

Deputy Director General for Financial Services, Directorate General Internal Market and Services, European Commission

Markus Ferber

(EPP, Germany), MIFID II rapporteur

Maria-Teresa Fabregas

Head of Unit, Securities Markets, European Commission

Judith Hardt

Secretary General, FESE

Mike Masters

Founder, Masters Capital Management; Founder, Better Markets

David Bicchetti

Economist, Division on Globalization and Development Strategies, UNCTAD

Frédéric Baule

Expert in Products and Derivatives Trading, Risk management Services, Petroleum industry

Thierry Francq

Secretary General, AMF

Mark Hemsley

CEO, BATS Chi-X Europe

Joe Saluzzi

Co-founder and Co-head of equity trading, Themis Trading LLC

Ryan Chidley

Senior Equity Trader, APG Asset

Tim Rowe

Manager of Trading Platforms and Settlement Policy, FSA

Remco Lenterman

Chairman, FIA-EPTA

Laurent Degabriel

Head of Division, Investment and Reporting, ESMA

Pauline Skypala

Deputy Markets Editor, Financial Times (moderator)

Benoît Lallemand

Senior Research Analyst, Finance Watch (moderator)

"LONG TERM INVESTING: WHAT CAN THE EU LEARN FROM THE KAY REVIEW?" 17 October 2012

About 60 people attended and the speakers were:

Professor John Kay

Sharon Bowles

(ALDE, UK) - Chair of ECON

Trelawny Williams

Global Head of Corporate Finance, Fidelity International

Philippe Herzog

President, Confrontations Europe

Jérôme Haas

President of French Accounting Authority, ANC

Thierry Philipponnat

Secretary General, Finance Watch (moderator)



“ I support Finance Watch because of the image it is sending out: experts from the banking world (that cannot be fooled) are strongly convinced to put the regulatory institutions back on the track of common sense. ”

Frédéric Rech, Friend of Finance Watch

Social media

Finance Watch's social media presence has built slowly starting around mid-2012 with the launch of targeted campaigns on Twitter and Facebook. This activity includes commissioning and sharing popular content such as cartoons, infographics and animations as well as launching debates among followers and friends. By the end of the year, the Twitter community had grown close to 2,000 followers and the Facebook community close to 3,000 people, while the videos on the Finance Watch YouTube channel counted almost 10,000 views.

The number of "Friends of Finance Watch" who follow Finance Watch's positions and publications via a regular newsletter increased to around 4,000 at the end of 2011 and more than 6,000 by the end of 2012. Email newsletters were sent quarterly in English, French and German containing news about Finance Watch, cartoons, surveys and publications.

Website

The Finance Watch website (www.finance-watch.org) serves as a library of content and a presentation of the organisation. It presents technical reports and analyses for policymakers and acts as a source of information for Finance Watch Members and other civil society actors engaged in financial reform.

It is also a source of information for the general public about the financial reform agenda in Europe and Finance Watch's mission. Explanatory materials are provided mostly in three languages (English, French, and German) under a variety of formats, such as blogs, videos, and cartoons. A new version of the website was launched in the first quarter of 2013.



PUBLICATIONS



Finance Watch made 25 technical interventions in 2011 and 2012, including 11 position papers and written consultation responses, ten hearings and speeches and four open letters. Dossiers are shown in brackets where relevant.

11 July 2011

Position paper (short selling)

12 October 2011

ECON hearing (CRD IV)

19 October 2011

Open letter on supervised deleveraging (CRD IV)

28 November 2011

EESC hearing on civil society and financial regulation

5 December 2011

ECON hearing (MiFID II)

16 January 2012

Response to Parliament questionnaire (MiFID II)

24 January 2012

ECON hearing (CRA 3)

2 February 2012

Position paper "To end all crises?" (CRD IV)

22 March 2012

Open letter to US Senate Committee on Banking entered into the record

29 March 2012

Hearing before HLEG (Liikanen / Banking Structure)

24 April 2012

Position paper "Investing not betting" (MiFID II)

26 April 2012

ECB conference speech "Financial Integration"

29 May 2012

Hearing before UK House of Lords (MiFID II)

1 June 2012

Response to HLEG consultation (Liikanen/Banking Structure)

19 June 2012

Response to Commission consultation (Shadow Banking)

19 September 2012

Parliament questionnaire (Benchmarks)

24 September 2012

ECON hearing (Benchmarks)

27 September 2012

Open letter on WTO rules and financial regulation

9 October 2012

Hearing before French Commission des Finances (Banking Union)

19 October 2012

Response to Commission consultation (UCITS VI)

24 October 2012

Speech at DG MARKT "Bank structures and banking union" (Banking Union and Liikanen/Banking structure)

31 October 2012

Position paper "Towards suitable investment decisions" (PRIIPs)

14 November 2012

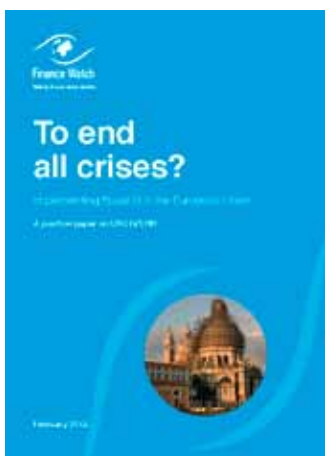
Response to Commission consultation (Liikanen/Banking structure)

4 December 2012

Response to Commission consultation (Benchmarks)

12 December 2012

Open letter on French banking reforms (Liikanen/Banking structure)



A key part of Finance Watch's communication activity is making the content of our technical studies more accessible to the public using a variety of formats, such as easy-to-read summaries, postcards, blogs, webinars and cartoons.

Webinars

In December 2012, Finance Watch started a programme of online webinars for Friends and Members to explain complex financial topics in an easy and interactive way. The first webinar was on high-frequency trading on 13 December. The format involved a live 15-minute online presentation from a Finance Watch expert accompanied by infographics, followed by a 45-minute question and answer session. A recording of the webinar and the visual materials were uploaded to the website and shared via social media channels. More webinars will be added throughout 2013.



Postcards

- Postcard on inducements (MiFID II)
- Postcard on retail investor protection (PRIIPs)



Explanatory blog articles

- High Frequency Trading
- Commodity derivatives

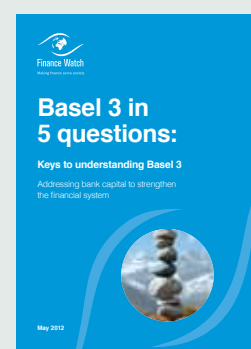


Cartoons

- Cartoon on capital requirements (CRD IV)
- Animation on food speculation (MiFID II)



Easy-to-read summaries



OBJECTIVES FOR 2013

In 2013 we plan to concentrate together with our Members on some major European legislative initiatives on financial and banking regulation:

- Finance Watch will continue the work initiated on **banking structure**, based on its conviction that a separation of banking activities is needed to improve the resilience of the financial sector and put back banks at the service of society. At a European level, we will follow-up on the Commission's expected proposal to separate banks' activities.
- We also plan to work extensively on researching the issue of **long-term financing**, finding the appropriate incentives to be put in place in order to shift our financial system from short term to longer term views. At a European level, this work will take place in the context of the Commission's Green Paper.
- Continuing the work conducted in 2012, we will follow-up on **MiFID II** (Markets in Financial Instruments Directive), **CRD IV** (Capital Requirements Directive) and **PRIPs** (Packaged Retail Investment Products).

“ Lobbying must be balanced to lead to a democratic outcome. [Finance Watch] now plays a key role in making finance serve the real economy and society at large. ”

Michel Barnier, EU Commissioner for Internal Market and Services

Generally speaking, Finance Watch aims to broaden its **recognition as a voice that counts** on financial and banking matters, especially among elected officials and policymakers at European and national levels, by providing them with accurate expertise on the legislative files under debate.

At the same time, Finance Watch is seeking to develop further its **communication towards the general public** by extended materials such as webinars, infographics, comics and non-technical papers. The aim is to share our analyses and messages with a larger community of people. To meet these objectives, Finance Watch will need to **broaden its base of friends, followers and donors**. That is a key challenge to ensure the continuity and efficiency of our action in the medium term.



GLOSSARY AND ABBREVIATIONS

AFM

Autoriteit Financiële Markten, Dutch financial markets regulator

AIFMD

Alternative Investment Fund Managers Directive

ALDE

Alliance of Liberals and Democrats for Europe, political group in the European Parliament

AMF

Autorité des marchés financiers, French financial regulatory agency

ANC

Autorité des Normes Comptables, French Authority for accounting standards

CFTC

Commodity Futures Trading Commission, US options and futures and options market regulator

CRD IV

Capital Requirements Directive IV, legislative package to strengthen the regulation of the banking sector

DGS

Deposit Guarantee Scheme

EBA

European Banking Authority

ECB

European Central Bank

ECON

Committee on Economic and Monetary Affairs of the European Parliament

EIOPA

European Insurance and Occupational Pensions Authority

EMIR

European Market Infrastructure Regulation

EPP

European People's Party, political group in the European parliament

ESMA

European Securities and Markets Authority

ETF

Exchange-traded fund

Euribor

Euro Interbank Offered Rate

FSB

Financial Stability Board

FTT

Financial Transactions Tax

Greens

The Greens/European Free Alliance, political group in the European parliament

HFT

High Frequency Trading

IMF

International Monetary Fund

IORP II

The EU's review of the Directive on Institutions for Occupational Retirement Provision, defines rules for occupational pension funds

IRB

Internal Ratings-Based approach to capital requirements for credit risk

KID

Key Information Document for packaged retail investment products

Libor

London Interbank Offered Rate

LTF

Long-term Financing

MAD

EU Market Abuse Directive, dealing with insider dealing and market manipulation practices

MEP

Member of the European Parliament

MiFID II

The EU's Review of MiFID, the Markets in Financial Instruments Directive

MMF

Money Market Fund

OECD

Organisation for Economic Co-operation and Development

PRIPs

Packaged Retail Investment Products

pro-cyclical

when measures have a reinforcing effect on the state of the economy (e.g. austerity in a downturn)

rehypothecation

when banks or brokers re-use the collateral posted by clients to back other trades and borrowing

S&D

Progressive Alliance of Socialists and Democrats, political group in the European parliament

Solvency II

EU Directive that codifies and harmonises the EU insurance regulation

SSM

Single Supervisory Mechanism

Standardized Approach

requires banks to use ratings from External Credit Rating Agencies to quantify required capital for credit risk

Tibor

Tokyo Interbank Offered Rate

Trialogue

informal meetings between the three main EU institutions (Commission, Parliament and Council) often in the final stages of legislation

UCITS

Undertakings for Collective Investment in Transferable Securities, set of EU Directives on collective investment schemes



Finance Watch

Making finance serve society

Square de Meeûs 38/40

1000 Bruxelles

Tel: + 32 (0)2 401 87 07

contact@finance-watch.org

www.finance-watch.org