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Press Release

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EXTRACTS OF SPEECH BY MR CHRISTOPHER TUGENDHAT, EEC COMMISSIONER RESPONSIBLE FOR THE BUDGET AND FINANCIAL INSTITUTIONS, TO THE INSTITUTE OF BANKERS IN SCOTLAND, EDINBURGH, MONDAY, NOVEMBER 6, 1978.

I. E.M.S.

I am sure it would be in Europe's interest to have a European Monetary System consisting of all nine Community countries. But of course the terms must be fair - every prospective member will rightly want to be sure of that - and the system must be durable. A successful EMS will help to create the conditions of monetary stability that are essential for the success of soundly based domestic growth policies. But to be successful the EMS must take equal account of the interests of all prospective members and must be built on firm foundations.

I hope I will be able to convince those of you who have serious doubts what is being proposed and those who are still trying to make up their minds that participation in a viable EMS is in the interest of all the Member States. Nothing I can say will convince the professional anti-Europeans and those who in reality oppose the Government's policy of making the fight against inflation its main priority and who will attack anything that serves to reinforce monetary disciplines...

The countries of the European Community are particularly inter-dependent. The UK send 36% of her total exports to other Member States, Germany 46%, and France 51%. Moreover, as the UK is more dependent on external trade than Germany, or France, the share of its GDP accounted for by imports from the rest of the Community is higher. In 1977 the proportion was 10%, compared with 9.7% for Germany and 9.2% for France.

Thus strictly on grounds of national self interest every Member State - Britain included - should look sympathetically at a proposition, such as EMS, which is designed to shield the countries of Europe from the worst effects of the extreme fluctuations in exchange rates that have arisen since the breakdown of the Bretton Woods system, and to provide a basis for effective coordination of national economic policies.....

The need to accompany EMS with appropriate national policies implies obligations for both weak and strong countries. Inevitably these obligations will in one sense fall more heavily on the former, for the system will only endure if there is greater convergence than at present between the performance of the Community's nine national economies and convergence should obviously be towards the standards of the best and not worst. Nor should the stronger economies have to bear the cost of others' indiscipline. But of course to aspire to do as well as the best in the fight against inflation and in response to their other economic problems ought to be the weaker countries' objective anyway.

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I must stress that participation in EMS cannot be a substitute for the political determination to carry out the national policies that are needed to achieve these objectives. But the advantage of pursuing them within the framework of EMS is that this will give the weaker economies a greater chance of securing complementary policies from the stronger countries than would otherwise be obtainable.....

But having looked at EMS in terms of the Community as a whole, I would also like, since this is a British audience, to point out some of the consequences specifically for Britain of refusing to participate in a viable system. Unfortunately it seems unlikely that these would be restricted to the non-enjoyment of the benefits of joining. It is important not to be apocalyptic, but there is a real danger that if Britain rejects or appears to reject EMS in principle rather than because the details of the specific scheme on offer are seriously inadequate then she will not merely miss a great opportunity, but will also substantially exacerbate her present national difficulties.

First, because such a stance could all too easily be interpreted at home and abroad as an indication of unwillingness on the part of the Government genuinely to get to grips with Britain's economic problems. Since, as I have said, membership of a properly organised EMS would require the government to do no more than to pursue the policies which are necessary anyway, foreign investors, currency market dealers, and domestic management and organised labour might well assume that voluntary non-membership implied that the government lacked the necessary resolve - and they would act accordingly. Proving that it has this resolve might well prove harder outside EMS than in.

Second, because Britain's ability to influence major decisions which profoundly affect her would be reduced. As I emphasised at the outset, Britain's economy is now intimately linked with its partners. But if EMS does not include all nine Member States, decisions concerning its management will have to be taken outside the framework of the Community's institutions. This could well mean that Britain would have no effective say in how her partners manage their respective currencies either in relation to each other or in relation to currencies outside the system, including sterling.

Non participation might also diminish Britain's capacity to make her views felt in other areas of Community policy. It is frankly difficult to assess the extent and scale of this risk. Community level decisions outside the sphere of EMS would continue to be taken within the Community framework. This means that Britain would enjoy the same legal rights and safeguards concerning them as at present. But in my view there can be little doubt that her unwillingness to undertake obligations which others had accepted would in practice substantially reduce the readiness of her partners to listen to Britain's views about issues such as the need to reform the CAP and to tackle the problem of perverse resource flows.

Of course EMS may fail, and then those who have stayed out will look quite clever. But the failure will do nobody any good. Success on the other hand could bring great economic advantages. I must however stress yet again that to be successful the scheme must take account of the interests of all nine Member States and be both durable and soundly based.

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II. Financial Services

It is not difficult to see that a common market, in not just banking but financial services generally, would benefit from a European monetary system which over a period of time resulted in the lowering of exchange control barriers and freer flows of capital across frontiers. It is equally the case however that as the Community moves towards a freer monetary regime, it will become not merely desirable, but necessary to accompany it with the necessary prudential mechanisms some of which I shall discuss later in this speech. At the same time the Commission's aim is to try to avoid the creation of yet another Community institution - say a European Prudential Commission since we believe that this is not necessary. What however will be necessary is the closest possible cooperation between supervisory authorities. Such cooperation has already begun: the Commission aims to foster it still further so that as the Community moves towards monetary union, governments, supervisors, the industry and the public can have the confidence that the security of the system appropriately matches its growing freedom.

An ambitious aim you may say. But it is not new. The Treaty of Rome provides for freedom of financial service. Yet, twenty years after the Community's creation, progress towards freedom in financial services lags far behind the freedom achieved in comparable areas such as trade in goods, and relative ease of movement of people within the Community. But when one stops to think, it should be no more difficult for banks or insurance companies to set up networks of branches throughout the Community than for industrial undertakings to become established throughout the Community or people more fully.....

1. Why coordination? Why is this necessary?

First, the banks and insurance companies in all the Member States are becoming increasingly international in scope. Were supervisory authorities to remain restricted to exercising control only within their national boundaries, many operations would escape their view altogether. On a large scale this becomes undesirable. As financial institutions become international so therefore supervisory authorities must follow their lead. This in turn means that national supervisory authorities must cooperate which implies the creation, over a period of time, of a common supervisory policy, i.e. comparable means of exercising supervision. This coordination must be achieved through a combination of continuous close consultation between supervisory authorities and directives harmonising essential aspects of the law.

The second reason for coordination derives from the interest of those supervised. The creation of an enlarged market, a Community in which borders disappear or are at any rate easily crossed, an economic area made up of the territories of nine States and in which centralised direction, integrated book-keeping and uniform cash management become feasible, offers banks and insurance companies the opportunity to achieve considerable rationalisation of their existing operations as well as the chance to expand. As I am speaking in Britain I should like at this point to say a particular word about British financial institutions. They have a strong export record which has brought great benefit to this country. This achievement should be recognised. At the same time it is right to acknowledge that continental Europe has not always been at the centre of their attention and has not historically been the area of greatest concentration of effort. But the pattern of UK trade flows is changing and financial services cannot and should not ignore the implications of this shift. I am confident they will not and I trust in the future, as the market for financial services opens up they will regard this "single" market, as it is called in Community jargon as part of the domestic market that it will have become.

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The third reason is the benefits to be derived by customers. These are particularly clear in the insurance field. We want to create a situation where initially large industrial firms - and then later all other sections of the market taking out insurance - can select from the insurers offering the best terms in the entire Community. Bringing about free competition in an enlarged market - an additional aim - also requires coordination since such competition can take place on fair terms only if the different practices of the various supervisory authorities do not lead to distortion of competition and if those insured enjoy equivalent protection, no matter where they take out their insurance.....

2. Method of coordination

This can be done through the implementation of two well-known Community principles - "freedom of establishment" and "freedom to provide services". We intend to create an enlarged open market for credit institutions, insurance undertakings, investment companies and stock exchange dealers. We intend to remove the obstacles presented by frontiers and to introduce rules and regulations only where these are necessary to ensure fair competition and investor protection. We are therefore basically concerned to satisfy a demand: the demand from European financial institutions for simplified procedures and broader opportunities. We will only introduce Community legislation where national laws have brought about complex and inward-looking systems which must be opened up and dovetailed into a Community system.....

3. Coordination of banking law

After initially - and unsuccessfully-attempting a comprehensive and far-reaching harmonisation of laws,the Commission switched in 1973 (the year of the accession of the United Kingdom, Denmark and Ireland) to a more pragmatic approach. The aim is to integrate banking systems gradually over a period of several years. To this end, the Commission submitted in 1974 the first general proposal for a directive - the First Coordination Directive - which merely outlined the basic principles of a harmonised banking law.....

It represents the first step in our plans to harmonise banking law by stages.

In particular it contains provisions on the licensing procedure for credit institutions, and all the Member States must either introduce corresponding rules or adapt them where they already exist. The main licensing conditions are the requirement that companies must have sufficient capital (the level and composition of which is, however, not defined in detail), and requirements concerning proper management, and legal form and similar criteria. The new banking law planned in the UK, as proposed in the White Paper of July 1978, has already adopted the requirements in the Directive, so the Community Directive should pose no real problems for the United Kingdom.

Unfortunately the Directive says little about freedom to set up branches anywhere in the Community. Our aim is that undertakings which have obtained authorisation in one of the Member States should be free to establish branches without further authorisation in all the other States. The Directive I am discussing makes it only slightly easier to establish branches in other Member States and on this point clearly shows the need for further coordination.

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The same is true of continuous supervision of credit institutions. Our first Directive merely adheres to the principle that credit institutions should be supervised on the basis of solvency and liquidity criteria; the details are left open and are to be determined through cooperation between the supervisory authorities. Our principle is nevertheless clear: we wish to achieve a system in which banks operating throughout Europe remain, wherever they are working, under the supervision of their national authorities and subject to home-country rules.....

This brings me to the question of the next steps in our work in the banking sector. We have drawn up a work programme which for the time being is still an internal Commission working document, and we are consulting all the governments on it. I am in the process of a tour of all the Nine capitals; in a month's time the top Member States' officials responsible for banking will meet in Brussels, in order to discuss the future work programme and its priorities.....

4. European Insurance Law

Here the Commission's general approach has been very similar to that in banking: the insurance sector, to a greater extent than banking is one where the legislation route is appropriate. The Commission has however only made proposals after extensive consultation of both the industry and government authorities concerned......

Let me now turn to indemnity insurance. Freedom of establishment here has been largely achieved. A Directive published as early as 1973 harmonises the fundamentals of the system of supervision and thus makes it easier for insurance undertakings to set up in several EEC countries at the same time. Harmonisation in particular also covers the fundamental financial rules, especially the minimum requirements for the size of individual companies own capital. The great step which has still to be taken is that of the freedom to provide services. Insurance undertakings from one EEC State must be able to sell their policies across frontiers, even if they have set up no establishments in the Member States concerned......

We want to extend the freedom to provide services in the insurance sector in general. In the first instance we must however confine ourselves to major risks such as transport or suretyship risks for example, or to especially large fire insurance policies. Especially large or specifically commercial contracts of this kind without exception involve the participation of insurers who can themselves assess the security and adequacy of the guarantees offered.

The complete freedom to provide services which would also enable the man in the street to insure himself abroad against sickness costs for example or private fire damage, would require the harmonisation of the laws on insurance contracts as well as other changes. The first steps towards measures of this kind are now at the discussion stage in the Commission. A degree of approximation of the basic aspects of insurance contract law is important for international cover of major risks. We need for instance to agree broadly on insurance contract payment obligations or rights relating to termination and so on. When it comes to the "small" policy holder, such points will have to be settled in detail. But for the stage we have so far reached, that of big risks, it is sufficient to stipulate a few general provisions and allow the parties concerned to choose the law they want the contract drawn in.......

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In conclusion I should like to deal briefly with the problems of life assurance. Here our efforts are still at the stage of the freedom of establishment, that is we are working on the approximation of laws which should make it easier for life assurers to open branches in other Member States in order to offer their services in the host country. Here coordination is mainly concerned with own capital requirements. The aim is for a life assurance company in an EEC country other than its own to be able to submit a certificate from its national authorities stating that it possesses sufficient solvency in the country in which its head office is situated. It would then not have to raise new capital in the host country: this would represent a substantial liberalisation but this cannot become fully effective until the many additional requirements, for example those on the valuation of assets, have been made subject to comparable rules.

One of the major problems we come up against in this connection is the differing structure of insurance undertakings. Sometimes these undertakings are "specialised" and sometimes "composite" insurers, i.e. in some countries undertakings can handle several or all branches of insurance at the same time, while in other countries the law requires them to specialise in certain branches, in particular life assurance. This naturally makes the integration difficult. But this is precisely the point on which a compromise put forward by the United Kingdom delegation is in sight. The British Government would be willing to accept the following situation: insurance companies which are newly established would have to specialise in all the Member States. However, composite insurers which already exist now (such as the insurance companies in the United Kingdom and Belgium), can continue to operate as all-purpose undertakings. But if they move to a country where specialisation is compulsory, they must comply with this requirement by creating a separate activity for each of the two areas - an independent subsidiary for the life assurance business and a separate branch for indemnity insurance. The Commission regards this compromise proposal as very constructive and supports it in the hope that it will provide the basis for the Council's early adoption of the life assurance directive.....

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