DRAFT AGENDA AS OF APRIL 2

Wednesday, April 15

6:00-6:40 p.m. RECEPTION Lobby

6:40-6:45 p.m. WELCOME Main meeting room
  ➢ Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School
  ➢ Karel Lannoo, Chief Executive Officer, CEPS

6:50-8:00 p.m. KEYNOTE ADDRESSES Main meeting room
  ➢ Daniel Gallagher, Commissioner, U.S. Securities and Exchange Commission (via video conference)
  Introduced by: Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School
  ➢ Johannes Beermann, Member of the Executive Board, Deutsche Bundesbank
  Introduced by: Karel Lannoo, Chief Executive Officer, CEPS

8:00-9:30 p.m. DINNER Restaurant

9:30 p.m. AFTER-DINNER COCKTAILS

Thursday, April 16

7:30-8:20 a.m. BREAKFAST BUFFET Restaurant

8:25-9:30 a.m. PANEL SESSION Main meeting room
  The search for bail-inable debt: Total Loss Absorbing Capacity (TLAC) and cross border resolution

  Panelists will introduce and discuss issues relevant to the topic. Each panelist will make a 5-7 minute presentation, followed by a plenary discussion, before all of the participants are broken into small, working groups.

  ➢ Moderator: Greg Baer, Managing Director and Head of Regulatory Policy, JPMorgan Chase & Co.
  ➢ Charles Goodhart, Norman Sosnow Professor of Banking and Finance, London School of Economics and Political Science
  ➢ Levin Holle, Director General, Financial Markets Policy Department, German Federal Ministry of Finance
  ➢ Etay Katz, Partner, Allen & Overy LLP
9:35-10:55 a.m.  SMALL GROUP SESSIONS

Participants are divided into 6 working groups for facilitated discussions with the views raised by the panelists serving as a foundation for the discussions. A facilitator encourages conversations which occur under Chatham House Rules, and a rapporteur will record the major themes (sans attribution) for use during the sessions on the final day.

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10:55-11:10 a.m.  REFRESHMENT BREAK

11:15-11:40 a.m.  PANEL SESSION

Reform of capital markets in the US and EU. Is the US the model for the EU?

Panelists will introduce and discuss issues relevant to the topic. Each panelist will make a 5-7 minute presentation and take one or two questions before all of the participants are broken into small, working groups.

- Troy Beatty, Assistant Director, International Regulatory Policy, Office of International Affairs, U.S. Securities and Exchange Commission
- Daniel Trinder, Global Head of Regulatory Affairs, Deutsche Bank AG

11:40-1:00 p.m.  SMALL GROUP SESSIONS

Participants are divided into 6 working groups for facilitated discussions with the views raised by the panelists serving as a foundation for the discussions. A facilitator encourages conversations which occur under Chatham House Rules, and a rapporteur will record the major themes (sans attribution) for use during the sessions on the final day.

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1:00-2:00 p.m.  BUFFET LUNCH

2:05-2:35 p.m.  KEYNOTE ADDRESS

- David Wright, Secretary General, IOSCO

Introduced by: Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School

2:40-4:00 p.m.  PANEL SESSION - PLENARY

Regulation and supervision for EU and US banks: Does Banking Union ease transatlantic cooperation?

A moderator will facilitate a discussion giving all panelists equal opportunity to participate before incorporating the audience as well. Panelists remarks will provide a point of view that offers Symposium participants the benefit of analysis and insight on the topic.

Moderator: Stefan Gavell, Executive Vice President and Head of Regulatory, Industry, and Gov’t Affairs, State Street

- Christopher Bates, Partner, Clifford Chance LLP
- Elizabeth McCaul, Partner-in-Charge, New York Office, Promontory Financial Group, LLC & Chief Executive Officer, Promontory Europe

4:00-6:30 p.m.  FREE TIME/RAPPOREURS MEETING

6:30 p.m.  GROUP BUSES DEPART FOR RESTAURANT SCHWARZENSTEIN

Please meet in the front lobby. It is a 20 minute bus ride to Gourmet Restaurant Schwarzenstein.
Friday, April 17

7:30-8:20 a.m.  BREAKFAST  
Restaurant

8:30-9:00 a.m.  KEYNOTE ADDRESS  
Main meeting room

Hal Scott, Nomura Professor and Director, PIFS, Harvard Law School on The Proper Role of Lender of Last Resort: Bank of England, European System of Central Banks, and the Federal Reserve

9:05-10:05 a.m.  PANEL SESSION  
Main meeting room

The effect of Quantitative Easing on capital markets

Panelists will introduce and discuss issues relevant to the topic. Each panelist will make a 7-10 minute presentation before turning it over to the audience for Q&A.

- Gabriel Bernardino, Chairman, European Insurance and Occupational Pensions Authority (EIOPA)
- Colin Ellis, Chief Credit Officer, Moody’s
- Burkhard Ober, Head of the Allianz SE, European Affairs Office Brussels

10:05-11:05 a.m.  PRESENTATION & DISCUSSION  
Main meeting room

The search for bail-inable debt: Total Loss Absorbing Capacity (TLAC) and cross border resolution

Panelists will moderate a plenary discussion that uses a synthesis of the small group sessions from the previous day as the basis for session.

- Mauro Grande, Board Member, Single Resolutions Board
- Paul Saltzman, President, The Clearing House Association

11:05-11:15 a.m.  REFRESHMENT BREAK

11:15-12:15 p.m  PRESENTATION & DISCUSSION  
Main meeting room

Reform of capital markets in the US and EU: Is the US the model for the EU?

Panelists will moderate a plenary discussion that uses a synthesis of the small group sessions from the previous day as the basis for session.

- Alan Houmann, Head of Government Affairs for Europe, Middle East & Africa, Citi
- Speaker to be announced

12:15-1:00 p.m.  ADJOURN AND LUNCHEON  
Restaurant
Final Report

2015 Symposium on Building the Financial System of the 21st Century: An Agenda for Europe and the United States
The thirteenth Europe-US Symposium was held at the Bundesbank Training Center in Eltville am Rhein, Germany from April 15-17, 2015. Sessions addressed the search for bail-inable debt, reform of capital markets in the EU and US, regulation and supervision of banks in the EU and US, and the effect of quantitative easing on capital markets. With most of the pieces of the global financial regulatory agenda in place, participants shifted their concerns to reconciling differences in regulatory regimes between the EU and US, as well as within the EU. They also expressed a growing urgency for promoting capital market development in Europe in order to support economic growth and resilience of the financial system. And despite relative confidence about the improved ability of financial systems to withstand crises, there was a pervading concern about the long-term effects of slow growth and low interest rates on the health of developed country financial institutions and economies.
The Search for Bail-inable Debt—TLAC and Cross-Border Resolution

In Session 1, participants discussed bail-inable debt. While most of the discussion focused on the FSB requirement of total loss-absorbing capacity (TLAC), a number of participants also brought up the minimum requirement for own funds and eligible liabilities (MREL), mandated under the EU Bank Recovery and Resolution Directive (BRRD). Participants discussed the effectiveness of bail-inable debt in recapitalizing banks in a crisis, mechanisms for converting existing bank debt into bail-inable debt, and possible market reactions to its issuance and utilization.

TLAC AND TOO BIG TO FAIL

Participants discussed at length the potential effectiveness of TLAC in managing the failure of a Global Systemically Important Bank (GSIB). Many agreed that it would indeed contribute to the ability of regulators to manage a bank failure and help prevent contagion. They saw it as the final essential piece of the effort to eliminate the problem of “too big to fail,” in tandem with enhanced capital and leverage requirements and resolution plans. They also expressed hope that TLAC implementation would be the last major requirement imposed on banks to prevent a recurrence of financial crisis.

Some felt that it would only work as planned in the event of an idiosyncratic bank failure, and suggested that in the event of more widespread failures, public money might be needed to backstop the system. A number of participants also worried about its cost. However, despite the cost, many participants considered it a better solution than enforced restructuring of large banking groups.

Although TLAC was seen as likely to address the issue of capital base in the event of a major
crisis, many participants worried about the additional problem of liquidity provision if a bank failure were to occur in the US. As one participant put it, “Strong resolution may end too-big-to-fail, but it cannot on its own prevent contagion.” Participants noted with concern that the Federal Reserve’s ability to provide liquidity to non-banks, including non-bank affiliates of bank groups, had been vitiated under the Dodd-Frank Act.

Finally, the question was raised as to whether bail-in was really better than bail-out as a principle on which to manage bank failures. Several participants pointed out that bank resolution regimes are really about allocating losses. Much of the justification of the enhanced GSIB rules, including TLAC and the capital surcharge, was to avoid taxpayer-funded bail-outs, which participants agreed was an important goal. However, some participants argued that the main investors in bail-inable bank debt would inevitably be insurance companies and asset managers investing on behalf of their clients’ retirement needs. One participant quoted an insurance executive’s summary of TLAC as “You want to take the money of my policy holders to bail out your depositors.”

**TLAC IN A CRISIS**

Participants discussed at length how TLAC (or MREL) would work in a crisis. In principle, if all equity were completely or partially wiped out, then TLAC would be used to recapitalize the bank, or bank holding company under the FDIC’s single point of entry approach, by converting it to equity. This raised the question of how much bail-inable debt would be enough to maintain the bank as a going concern, to avoid imposing loss on short-term funders that could spark contagion, and to reassure counterparties that the bank or bank holding company would indeed honor its commitments, so as to prevent a further run. Participants noted that the FSB’s proposed guidelines called for a floor of 16-20% of risk-weighted assets, but many felt that amount to be arbitrary and excessively high. Several argued that historical experience suggested that 8-16% would be sufficient—even if capital were completely wiped out over a weekend, they argued, a bank reopening on Monday morning would be compliant with Basel requirements and still have a healthy buffer. While recognizing the counter-argument that a bank undergoing bail-in would need extra capital to reassure its creditors and counterparties, they asked whether there was any level of capital that could guarantee that. They worried that there would be no limit to the level of capital that might eventually be demanded, which could be very costly to banks.

A second question about the operation of bail-inable debt was where it should be held within a globally active bank. For those GSIBs with a holding company structure, under which restructuring would take place at the holding company level, many participants agreed that it would be logical to hold bail-inable debt at the holding company level. The issue would then be how capital could be downstreamed to the operating subsidiaries where the losses were incurred. However, due to regulators’ concerns about how bail-in would work across borders, it seemed likely to many participants that national regulators would in some cases require prepositioning of loss-absorbing capacity, which some termed “internal LAC.” Indeed, the BRRD would require MREL to be located in each subsidiary, with no consolidation credit. (This would only be relevant to larger EU banks. Most EU banks were expected to have MREL set to zero, as they would be expected to go through bankruptcy rather than resolution as a going concern.)

Participants saw several likely results of internal LAC. On the positive side, it promised to
protect host country taxpayers, as it guaranteed that the local subsidiary would be recapitalized, without having to depend on the good will of the holding company or the home regulators. However, many participants argued that it would actually make banking groups more brittle, as they would be expected to keep the minimum internal LAC in each subsidiary, which would prevent redeployment of capital across borders in the event of a crisis. From the point of view of cost, they also noted that in some cases the sum of required internal LAC across all of a group’s subsidiaries might exceed the TLAC that would be required at the group level if it were calculated on a consolidated basis. Another effect of prepositioning would be a de facto shift to multiple point of entry resolution, as the bail-inable debt would not be available to the group as a whole. One participant thus predicted a “massive retreat from single point of entry.”

Even under ring-fencing of this nature, however, some participants felt that there would still be an advantage to the single point of entry approach. The reasoning was that, even though the flexibility of the banking group would be significantly limited by the need to preposition capital, at least some flexibility would remain to move capital where it was most needed.

MANAGING CONVERSION OF EXISTING SENIOR DEBT

Participants agreed that the mandate to build up high levels of bail-inable debt would create significant challenges for banks. While it would be relatively easy to issue new debt with bail-in clauses, the sheer scale of TLAC required under the proposed GSIB rules appeared to require that a great deal of existing debt would need to be converted to bail-inable debt. Three solutions to the problem were discussed in the European context: statutory, contractual, and structural.

Many participants preferred the statutory solution in principle. In this approach, a national government would pass a law that would automatically make all debt (or all debt of particular classes) bail-inable. This solution was seen as much faster and simpler than having to renegotiate or redeem and reissue outstanding debt. It would also solve the principle of “no creditor worse off” (i.e., no creditor should be worse off in the event of bail-in than it would have been if the bank became insolvent), which could lead in practice to litigation and uncertainty. However, three important questions remained unanswered at the time of the Symposium. First, would statutory conversion be legally viable? Participants noted that Germany was seeking to implement a statutory solution, but that its legality would be decided by the court system, not the legislature. Second, would it be politically viable? A number of participants predicted that there would be significant political resistance in many jurisdictions, particularly over the potential impact on retirement savings when the holdings of life insurers and pension funds were forcibly made bail-inable. Third, how would markets react to such a law (or the prospects of such a law)?

The contractual solution of renegotiating every bond issue was universally seen only as a fallback option if statutory solutions turned out not to be feasible. Participants worried that the process of conversion to bail-inable debt would be slow and uncertain. It would also raise issues of fairness, in that it would penalize those creditors who were converted relative to those who were not. Some participants predicted that litigation could drag on indefinitely if a contractual the bail-in clause actually had to be invoked, causing differential losses among debt holders.

As an alternative approach, some participants proposed a structural solution as a way of avoiding the problems of the contractual solution. This would involve issuing new debt.
from a holding company, which would be subordinated to subsidiaries—this is how the problem would be handled in the U.S. It would avoid legal hurdles, but would be workable only within a holding company structure, which some major European banks did not substantively have. There were also questions about how it would affect borrowing costs at the holding company level.

**MARKET REACTIONS**

A major unknown in all the discussions of TLAC and bail-inable debt was how markets would react and whether there would be demand for it. A number of participants observed that no one was really sure how to gauge or price the risk attached to bail-inable debt. Therefore, they predicted high prices and lack of demand for such debt. Some pointed to the positive experience of banks with issuing CoCo’s as a reason for optimism; however, others countered that the sheer scale of TLAC as well as continuing uncertainties about how conversion would be triggered made the comparison less apt.

A related question was who would buy bail-inable debt. According to FSB guidelines, purchasers should not include banks (in order to prevent interconnected failures) or retail investors (for consumer protection reasons). Many participants observed that the main purchasers were likely to be pension funds and insurance companies, but this made some nervous—they did not feel comfortable with the idea of forcing retirement funds to absorb losses in the place of depositors. For some participants, shifting the cost of failure to the government (i.e., broad-based taxpayer funding) appeared fairer. Finally, it was argued that, in such a low interest rate environment, investors were willing to buy nearly anything, and with low risk premiums. But what would happen when interest rates finally rise?

Participants noted some peculiarities of TLAC. With regard to market liquidity, there were a number of participants who predicted that demand would likely dry up faster than other types of securities in the event of warning signs at a given bank or even concerns about other banks, since most bondholders would strongly prefer to avoid being bailed-in. Some participants also expressed concern about what they called a “phoenix problem” after a resolution. Although bondholders would rise from the ashes of a resolution as shareholders, questions were raised about how long they would be locked into equity and how the transition back to normalcy (including reissuance of sufficient new TLAC) would work. This was seen as likely to contribute to weak market demand for TLAC debt in normal times, and potential collapses in liquidity in the face of warning signs.

Importantly, the proposed guidelines were seen as privileging structured debt over derivatives. This could create the potential for lengthy litigation on the basis of “no creditor worse off” if debt were actually bailed-in in the event of a resolution. Moreover, it struck many participants as odd that derivative products would be privileged over plain-vanilla bonds, and they questioned whether that was wise policy—or if there was even a good justification for it.

Finally, participants raised the possibility that the valuation of bail-inable debt would vary by jurisdiction, rather than just by characteristics of the issuing banks. In particular, they pointed to several factors. First, it was argued that banks based in countries with more credible regulatory and supervisory systems would enjoy lower prices for that debt. Similarly, bail-inable debt would likely also be less costly for banks based in countries that investors saw as more likely to
bail out a failing institution rather than quickly invoking. These participants saw the likelihood of bail-out as a function of both capability and intention. Capability would largely be a function of the size of an economy, or at least the size of the backstop (as in the SRM). As for intention, a number of participants argued that some countries, such as China and Japan, had regulatory cultures that preferred bail-outs to managing failures; their banks would be rewarded with a competitive edge versus international rivals due to lower cost of TLAC.
Reform of Capital Markets in the US and EU—Is the US the Model for the EU?

Session 2 considered the reform of capital markets in the US and EU. Much of the discussion revolved around the idea of promoting “capital markets union” in the EU. Participants also discussed prospects for European capital market development, challenges to capital markets, and whether there were elements of the US model that might be relevant to Europe.

THE PROMISE OF A CAPITAL MARKETS UNION

There was considerable interest among participants about the prospect of a European capital markets union. There was, however, much confusion about what the term was actually meant to signify. For many participants, the lack of clarity had not been dispelled by the European Commission’s recent Green Paper on the subject, which they felt did not adequately define “capital markets union” or set clear priorities. While some saw the Green Paper as little more than a list of suggestions, others were more optimistic, arguing that it had been left deliberately open-ended in order to gain information on industry preferences rather than dictate solutions.

Although “capital markets union” as a political project was seen as still undefined, many participants agreed that the basic goals of improving access to financing businesses across Europe, diversifying their sources of funding, and increasing market efficiency were important ones for improving financial intermediation and economic growth. A major concern for many participants was Europe’s lackluster growth, perhaps best exemplified by the nearly 25 million unemployed workers across the EU. They argued that any measures that would improve funding to employers—particularly SMEs—could only help to improve Europe’s economic performance. A number of participants also argued that a more diversified financial system would be more resilient, observing that Europe’s bank-based financial systems had taken longer to bounce back than the more diversified financial systems of the US and UK.

While most participants were receptive to the idea that European financial markets could be improved, some were skeptical of some of the more optimistic claims of capital markets union.
supporters. Several questioned whether the EU was really suffering from a dearth of capital. Pointing to historically low interest rates, they argued that weak credit growth was primarily due to lack of demand and an unwillingness to accept risk. There was more sympathy for the idea that SMEs might be systematically underfunded, but a number of participants questioned the feasibility of SME funding through capital markets, noting the difficulty of doing so in the public markets even in the US, although the private venture capital market did play such a role. Finally, some participants raised questions about the geographical impact of capital markets union. Despite what they saw as a widespread assumption that, once barriers were removed, capital would flow from areas of surplus savings to areas were capital was more scarce and thus reduce inequalities within the EU, they worried that unequal access to capital might actually be further concentrated in countries or regions seen as lower risk. In other words, the rhetoric about capital being “trapped” in high-savings areas like Germany and not being able to seek out opportunities for higher returns might have the story backwards—perhaps capital was actually trapped in less developed areas in Eastern and Southern Europe and those investors would welcome the chance to pursue greater security. One participant even warned of the possibility that intra-EU capital flight might create “mini-Detroits.”

Viewing the uncertain benefits and the difficult road to capital markets union, some participants argued that the focus on capital markets union was misguided. If the goal were to quickly improve allocation of capital in order to help the nearly 25 million unemployed, they reasoned, the EU might be better off focusing instead on completing the partially-finished mission of banking union.

**US AS MODEL?**

While most participants were wary of the idea of trying to emulate US financial markets, many agreed that the US system offered some lessons for the EU as it sought to develop capital markets and lower intra-EU barriers to investors. Even among those who saw valuable lessons in aspects of the US financial system, there was not necessarily agreement about which lessons should be drawn.

A number of participants praised the prevalence of market-based finance with a strong equity component, in contrast to many European economies’ reliance on banks for financial intermediation and capital formation. Among the principles they saw as undergirding US capital markets, one was an understanding among investors of the relationship between risk and return, and a willingness to accept risk. In contrast, several bemoaned the risk-averse nature of some European societies, as evidenced in a preference for safe assets and an unwillingness to allow second chances to entrepreneurs whose business ventures had failed. These participants were correspondingly pessimistic about the potential for a large-scale shift to market-based finance in Europe.

From a regulatory perspective, participants emphasized two key principles in particular of the US system. One was transparency, as seen in rules on disclosure and reporting. Despite flaws, participants saw the US capital markets as benefiting from abundant and free-flowing information about issuers and markets. The second was predictability of market practices. A number of participants praised the SEC and other regulators for their strong and consistent enforcement of market conduct rules. (However, the SEC also came under some criticism for its lapses in prudential regulation prior to the financial crisis.) The separation of
market conduct regulation from prudential and banking regulation was seen by some participants as an advantage of the US system, since it prevented market concerns from being subordinated to bank supervision; others were less positive about the separation, which they saw as simply one more manifestation of a highly fragmented regulatory regime.

A number of participants also drew contrasts between US and European market structure, institutions, and legal infrastructure. One common observation was about the comprehensiveness of the US investor base, which ranged in character from individual retail investors to a variety of institutional investors, in size from small to large, and in function from seed financing to secondary markets. Moreover, they noted that institutional investors were relatively unconstrained in their ability to make investment decisions. In contrast, the EU maintained a variety of restrictions on major institutional investors, including prudential rules on insurance companies, pension funds, and UCITS. This was seen as significantly limiting the appetite for risk in European markets overall.

A number of participants argued that a key element of US financial markets that Europe ought to adopt was the capacity for private placements (including venture capital); there was a sense among many that the EU should enact its own version of Regulation D in order to provide more venues for issuers—including issuers of complex products and SME finance—to address their funding needs. Some participants also argued that Europe could learn from the US experience with securitization, which significantly expanded the capacity for market-based finance to service the needs of a variety of borrowers throughout the economy. They noted that mortgages in the EU remained trapped on banks’ balance sheets—even those issued with covered bonds. (Under the EU version of Basel rules, covered bonds benefit from a lower risk weighting than securitizations in general and can count to a limited extent towards the bank’s short-term liquidity requirements. They are also eligible as collateral for central bank lending. But new leverage requirement in Basel III will make the assets more expensive for the banks to hold, as they will have to hold capital against them regardless of their degree of risk.) Others were less convinced, arguing that the US legal model was less central to the success of US securitization markets than the existence of huge semi-public, government-sponsored financial institutions that process and guarantee mortgages (Fannie Mae, Freddie Mac, Federal Home Loan banks) and student loans (Sallie Mae). However, while these institutions may promote securitization, they felt that these GSEs engendered moral hazard and systemic risk, had contributed greatly to the creation and spread of the subprime crisis, and should therefore not be emulated. Most of all, however, the sheer size of internal domestic markets was seen as driving liquidity and variety; for some participants, the positive US example was another reason to push for capital markets union, even if it would likely take years.

Problems of the US Financial System
Although participants noted a variety of strengths of the US financial system that European regulators could adapt to local conditions, they also pointed out a variety of problems in US financial market.

One of these was listing requirements (as well as restrictions on shifting listings to other countries). The costs and complexity of these requirements were seen by many participants as something that other jurisdictions should avoid. The problem of excessive listing requirements was seen as being partially offset by the prevalence of private placements, as noted above. Perhaps more importantly, many participants spoke approvingly of provisions of the JOBS Act that facilitated equity financing for SMEs—both in the pre-public phase and in
less onerous requirements for IPOs, including temporary relief from some obligations under the Sarbanes-Oxley Act. They urged EU legislators and regulators to consider similar measures to facilitate SME financing.

A second serious criticism of the US financial system was the prevalence of securities class-action suits. Many participants saw class-action as a major disincentive to foreign companies or private companies considering US listing, and it was argued that this was leading to a decline in the competitiveness of the US capital markets.

Third, while some participants had praised the idea, embodied in the SEC, of an autonomous market conduct regulator that was not also tasked with prudential regulation, others felt that it was not a model to emulate. They felt that functionally segregating regulatory bodies in this way only contributed to fragmentation of regulation and supervision, multiplication of compliance costs, and possibilities for problems to fall between the regulatory cracks. Several participants also disputed the generally positive evaluation of the SEC’s market conduct regulation, noting some important failures that had contributed to the US financial crisis.

Many participants felt that the Dodd-Frank Act exacerbated the problems of US capital markets, and of the financial system in general. Moreover, a number of provisions, including the Volcker Rule, were seen as disincentivizing market-making, which would likely reduce liquidity in some securities at crucial moments. Participants therefore cautioned against Europe adopting such regulatory overreach.

EU CAPITAL MARKETS: WHAT ARE THE BARRIERS?

Over the course of the Symposium, participants discussed a number of impediments that they saw as particularly important, including limited investor base, market fragmentation, household saving preferences, and prevalence of relationship banking practices. Many of these phenomena were seen to result from—or at least be exacerbated by—regulation.

For many participants, one of the main impediments to capital market development was what they saw as a limited investor base, in terms of both retail and institutional investors. With regard to retail investors, a number of participants made the point that there appeared to be a clear preference for less risky assets such as savings and life insurance products (although the real risk of life insurance products might be considerably higher than policyholders believed—see later discussion of quantitative easing). There was some question about whether this was due to a cultural aversion to risk-taking in some parts of Europe or simply a lack of knowledge. Several participants noted that, in addition to possible differences in cultural acceptance of risk, the prevalence of defined-contribution pensions in the US had made US households much more familiar with securities investing than their European counterparts. There was a general call for more financial education, including by brokers, to reduce fears of risky products, although opinions were mixed as to how big an effect such efforts might have.

Many participants felt that the limited institutional investor base was a larger impediment to capital market development than the caution of retail investors. They also felt that it would be more practical to use policy measures to expand the institutional investor base than the retail investor base, because many of the problems they identified were caused by regulation or policy. Weaknesses of the institutional investor base ranged across investor types, including pension funds, insurance companies, and UCITS.
Participants noted that there were relatively few private pension funds, which formed a large part of the US institutional base. This reflected the preference for public pension schemes throughout the continent. European pension funds were, moreover, generally highly regulated with regard to the types of assets they could purchase as well as their asset allocation, and that those rules were oriented toward risk minimization (e.g., sovereign bonds and high-quality bonds) rather than risk management or diversification. Participants observed that insurance companies, another potential set of institutional investors, also tended to be conservative in their investments. They warned that this tendency would likely be further entrenched by the impact of Solvency II. Finally, some participants pointed out that even UCITS—the closest European analogue to US mutual funds—also faced regulatory constraints in terms of their investment choices. While they are free to invest in more risky products such as equities or high-yield bonds, they are legally allowed to invest only in liquid assets. Unlike US mutual funds, therefore, they could not use derivative products to hedge risk, simulate an index, or for other purposes. Participants felt that this contributed to reduced liquidity not only in derivative products themselves, but also in standard securities.

Mirroring the constraints on the investor side were constraints on the supply side. While one of the putative reasons for promoting capital market development was to improve funding mechanisms for SMEs, many participants were skeptical of the prospects for shifting SME finance to the capital markets. They made several points in this regard. First was what some saw as a continued preference for relationship banking out of a desire of owners not to surrender control over their firms, either by diluting their ownership through equity issuance or by becoming indebted to anonymous bondholders. It was suggested that this might also be due to cultural differences with the US; unlike US-style start-ups, where owners and early investors might be looking for the opportunity to cash out, these participants believed that many European SMEs that in principle might benefit from capital market financing were family firms whose owners wanted to pass them along to their heirs. Some participants also pointed out that there were likely to be significant costs for many firms of shifting to market-based finance. One example given was accounting issues. It was argued that many SMEs had accounting systems that did not conform with listing rules; to change them would require considerable cost. In some cases, idiosyncratic accounting might be part of a strategy of tax evasion, in which case firms would be even more unwilling to improve transparency. Even inheritance tax systems were seen to discourage SME owners from listing their firms—for example, under German law, heirs could receive an inheritance tax waiver when they inherited a family company, but on the proviso that they maintained ownership and did not reduce employment for seven years.

A number of participants also pointed to issues with intermediaries. Market-making was a particular concern. Participants noted that Europe had few broker-dealers outside of banking groups; however, EU and US banks were constrained by leverage requirements from acting as market-makers, and US banks were additionally so constrained by the Volcker Rule. The constraints on market-making were seen as particularly problematic because of the lack of a private placement option.

REGULATION AND FRAGMENTATION

All of these issues were seen as being further exacerbated by market fragmentation. A number of participants argued that the roots of home-bias in investing extended beyond the issue of regulatory fragmentation, and in many cases reflected retail investors’ discomfort.
with investing outside their own countries. It was even noted that, according to surveys, many European residents were not even aware that they were allowed to invest freely anywhere in Europe.

Still, in many ways, participants saw regulatory fragmentation as the key challenge to capital markets development, which was one reason why the capital markets union concept was so alluring. In principle, they agreed, regulatory fragmentation should be minimized by the rulemaking authority of ESMA. However, both implementation and enforcement remained under the purview of national authorities. Moreover, national regulators often had entrenched procedures and bureaucracies that would be hesitant to cede their prerogatives to the “29th regulator.” And while the EU capital market regulatory system suffered from significant geographical fragmentation, it did not benefit from functional segregation of market conduct regulation from prudential regulation (which some participants saw as a strength of the US system, with its strong and autonomous SEC). A final complication, participants observed, was that even if securities laws were enforced uniformly across the EU, fragmentation would still result from inconsistencies in taxation (both rates and rules), accounting rules, bankruptcy laws, corporate governance regimes, and other regulatory issues.

Parliament—and for the first time since the crisis, attention to capital markets meant promotion rather than seeking to regulate away risk.

Perhaps most importantly, participants felt that the political dynamics were shifting. Much of the thrust of post-crisis regulatory reform had been about how to reduce risk and improve consumer protection, without taking into account the costs of added regulation. Moreover, the desire of politicians and their supporters to punish financial institutions for the financial crisis made it difficult for financial institutions to resist very strenuously. Seven years after the onset of the crisis, however, the increasing desperation of the EU’s nearly 25 million unemployed workers plus the lack of success of governments in addressing the problem through other means appeared to provide an opportunity to reassess financial regulation. A number of participants argued that the time had come when political parties could make a case for financial liberalization as a means of addressing the problems of unemployment and stagnation. The questions remained, however, of whether any parties would dare to make the case, and whether voters would accept a narrative that connected capital markets and growth.

REASONS FOR OPTIMISM?

D espite the often sober analysis of impediments to capital market development in the EU, some participants emphasized that there were also reasons for optimism that significant progress could be made. The effort by ESMA to create a single rulebook was seen as an important step toward supervisory convergence. Moreover, they felt that it was important that capital markets had gained the attention of the Commission and
Regulation and Supervision for EU and US Banks—Does Banking Union Ease Transatlantic Cooperation?

In Session 3, participants discussed the implications of European banking union for Transatlantic regulatory and supervisory cooperation. In particular, they questioned whether it would improve trust among regulators. While some expressed cautious optimism, others argued that on key issues such as derivatives regulation, ringfencing, and cross-border resolution, the prospects for convergence remained limited.

**REGULATORY DIFFERENCES**

Despite efforts ranging from the G20 consensus on financial regulatory reform to Basel III to FSB designation of GSIBs, participants agreed that there remained significant differences between the financial regulatory regimes of the US and EU. For example, as some participants noted, in the 2014 Basel Committee’s Regulatory Consistency Assessment Program (RCAP), the US was rated as largely compliant with Basel III, while the EU was rated as “materially non-compliant.” On a number of measures related to capital, liquidity, leverage ratio, and credit risk, the US and EU had actually diverged according to some participants, with the US approach characterized as “gold-plating” and the EU approach as “appeasing bankers.” Outside of banking, participants saw even less consistency—particularly with regard to derivatives and central clearing, which remained topics of considerable contention between regulators on the two sides of the Atlantic.

Differences within the EU remained as well, as the result of regulation by national authorities, as well as differing laws concerning accounting, taxation, and bankruptcy. However, the introduction of the Single Supervisory Mechanism (SSM) raised the possibility, as one participant put it, of making Europe a “one-stop shop” for US financial institutions (or, more...
likely, a “two-stop shop,” given the importance of London as a financial center and the low probability of the UK signing on to SSM). Thus, the SSM could significantly reduce compliance costs for European banks as well as foreign banks doing business in the Eurozone.

A number of participants remarked on the importance of having the ECB take over supervision of banking. Until 2014, the ECB did not supervise banks. Now, it supervises 9 GSIBs, more than any other jurisdiction (the US has 8, UK 4, and Japan 3) and twice as many bank assets as any other leading international supervisor. Actual supervision was still largely delegated to national central banks, but with ECB involvement and oversight. Over time, a number of participants argued, this would eliminate many of the remaining differences in supervision among Eurozone countries. Others cautioned against overemphasizing the unitary nature of European banking supervision, given the continuing roles of the European Banking Authority, the Commission and Parliament, non-Eurozone member states (especially the UK), as well as other financial regulatory bodies. Even in the SSM, conduct regulation would remain the responsibility of national authorities. There was also a concern expressed that putting banking supervision under the ECB roof would reduce coordination with other financial market regulation and would lead to an overemphasis by the ECB’s macroprudential regulation on the banking sector.

US-EU REGULATORY COOPERATION

Participants discussed issues of transatlantic regulatory cooperation at length. They noted that both US and EU banks were deeply exposed to host country regulation in the other jurisdiction, which made regulatory cooperation a very important objective. There were some differences in the type of supervisory relations: all the European GSIBs were subject to host state regulation by the US, whereas only two US groups were directly supervised by EU regulators (although other US-based GSIBs were exposed to EU supervision through their European subsidiaries).

From the perspective of US regulators, European banking union promised to improve the quality of cooperation not only because it could reduce the number of interlocutors, but also because it would significantly increase the credibility of European bank supervision across three key dimensions: horizontal supervision (including risk management and governance), macroeconomic information (with the ECB’s role as supervisor ensuring consideration of macroprudential concerns even when supervising individual banks), and stress tests. These factors could encourage greater US buy-in regarding EU supervision.

Still, transatlantic cooperation had been weakened due to the crisis, and some participants spoke of a loss of EU faith in US regulation that resulted. They pointed to structural banking solutions on both sides of Atlantic that were premised on lack of trust. The results included ringfencing, capital limits, activity limits, and exposure limits, which many participants feared might trap capital and liquidity in a crisis, when it is most needed. A variety of questions remained about the possibility of forced subsidiarization and whether European investment banking operations could be maintained in the US. Questions also remained as to whether the changes would enhance or detract from the ability to supervise and resolve financial institutions.

For many participants, the most important question mark in US-EU bank regulatory cooperation was over the issue of resolution. Participants agreed that the process of planning for a cross-border resolution had been made
simpler by banking union. However, there was much more concern about execution. It was noted that using the SRM was very complicated, and that it might be difficult for the FDIC to deal with it in the midst of a crisis. It was, moreover, not the resolution mechanism for all banks, which meant that the problem of cooperation with 28 national authorities had still not gone away.

What happens over longer run? These rules haven’t been created to reduce cooperation, so maybe they can be relaxed on a case by case basis. There was also the hope expressed that the ECB would be less captured by particular national interests and would be likely to be much more transparent. This should help cooperation. Finally, one participant pointed out that, under the SSM, the de facto language of European banking regulation was now English. While this would likely make transatlantic cooperation easier, it could well create tensions for mid-sized regional banks, which were less likely to do business in English.

A number of participants expressed frustration that, despite efforts to create effective supervision through colleges of regulators and many MOUs, crisis cooperation remained uncertain. Some participants responded that the key issue would be fostering trust between regulators, since formal mechanisms of cooperation might not be reliable in the event of an emergency. Thus, it would be important to improve communication by having more forums in which officials would cooperate in formulating solutions to concrete problems before crises occur.

Others expressed skepticism of the notion of trust, stating that it sounded like the triumph of hope over experience. They wondered whether and how experience in “peacetime” might relate to cooperation in time of crisis, given the strong interest of each national regulator not to lose taxpayer money—and perhaps even more importantly, not to use taxpayer money to bail out foreign creditors.

Some participants also questioned whether regulators were actively seeking to build up trust. One raised the problem of “entrepreneurial enforcement” in the US, particularly by New York state regulators. Another question was whether building trust would be frustrated by differences in the flexibility of EU and US regulators. In general, it was observed that US regulators seemed have more discretion than their EU counterparts, which could cause frustration in trying to gain cooperation.
The Effect of Quantitative Easing on Capital Markets

In Session 4, participants discussed the effects of quantitative easing on capital markets. While they focused particularly on quantitative easing in Europe, they noted that an extremely low nominal interest rate environment had become the norm among developed economies around the world. Much of the discussion considered the impact of low interest rates on insurance companies and asset managers. In particular, participants expressed concern about the viability of life insurance and defined-benefit pension systems.

MACROECONOMIC EFFECTS OF QUANTITATIVE EASING

Participants had mixed opinions as to the macroeconomic effects of quantitative easing. Several pointed to the relatively rapid recoveries of the US and UK, which carried out earlier and more aggressive easing than the Eurozone, as evidence of the potential effectiveness of such policies. Others pointed to what they saw as lackluster effects of aggressive quantitative easing in Japan to suggest that it was not sufficient to address contemporary economic ills. Indeed, some argued that Europe was currently going through a “Japanese experience.” More generally, it was noted that, despite the theoretical expectation that interest changes should change spending and saving decisions, empirical evidence was more equivocal, especially in an open economy.

Participants did agree, however, that the logic of monetary stimulus (including quantitative easing) was that it redistributed wealth from savers to borrowers. Thus, quantitative easing should hurt savers and should challenge the financial institutions that serve them, including life insurers and asset managers. At the same time, the flattening of the yield curve would inevitably cause banks to suffer.

In addition to trying to flatten yield curves in order to make long-term borrowing more
attractive, quantitative easing was also seen as a way of forcing investors to shift their holdings into riskier assets. By doing so, central banks would try to restore growth-oriented investment and reduce credit constraints on firms with growth potential. There was, however, some concern that the policies could lead to excessive risk-taking by investors, particularly financial institutions. On the other hand, there was concern that leverage and liquidity regulation applicable to banks would make it difficult for them to replace low yielding government debt with higher yielding assets.

EFFECTS ON INSURANCE COMPANIES AND ASSET MANAGERS

Participants expressed concern over the viability of life insurance companies and defined-benefit pensions if economic stagnation persisted. The major issue was the mismatch between the promised returns on those products and the actual returns of the assets in which funds had invested.

As a balance-sheet business, insurance companies must pay their policyholders out of the returns on their investments. With current returns in Europe below 1% and limited prospects for improvement, participants saw the ability to make profits as increasingly tenuous. Inevitably, insurers would need to diversify their holdings and increase investment in riskier assets in order to improve returns (albeit at the risk of volatility) to fulfill their obligations to policyholders.

While diversification away from the current concentrated holdings in sovereign bonds and bank debt was seen by some participants to be a good thing in principle, they also cautioned that such a development would require strong risk management by firms and continued scrutiny by supervisors. The question was raised as to whether shifting portfolios might lead to new build-ups of risk in real estate, infrastructure, or some other asset class. Some participants also asked whether investments would necessarily stay in the Europe; one possible winner was US capital markets, which were seen as deeper than those of the EU.

Decelerating returns were seen as particularly challenging for life insurance. Even if diversification were to improve returns on investment somewhat, insurers will have the policies from the 1990s—many with relatively high guaranteed returns—on their books for decades. Even in the property and casualty business, which does not suffer from the problems of maturity mismatch seen in life insurance, the decelerating rate of return would require significant hikes in premiums to retain profitability.

This was seen as a challenge for both insurance companies and regulators. In the most recent European stress tests, it had been concluded that a number of companies would have cash flow and even solvency problems in 8-12 years. However, it was argued that quantitative easing over the interim, which had further flattened the yield curve, was increasing stress on insurers and shortening that time frame. Several participants raised the possibility that regulators would have to intervene to ensure the sustainability of current business models. Among the likeliest remedies were reductions in dividends and commissions paid to brokers, but some participants warned that it was possible that guarantees on life insurance products might need to be modified, as occurred in Japan in the late 1990s. This would require national legislatures to change insurance laws.

At the EU level, participants noted the importance of the upcoming application of Solvency II rules. While Solvency I was not risk-based, Solvency II would be an explicitly risk-based regime. However, a number of participants expressed dissatisfaction with the
new rules. One participant stated that Solvency II requirements should be adjusted to better accommodate firms that were properly matching duration for long-term products. Another issue was the costs of compliance: one firm was said to have to produce 160,000 pages of Solvency II reporting each year for its insurance operations across Europe.

For pension funds, participants agreed that there was considerable variation in viability, based on mostly on whether they were funded or unfunded. However, even plans that had been adequately funded under prior assumptions would lose their viability if returns did not rise significantly. It was also noted that the countries of the EU faced differing pension fund situations, based on differing regulations. Several participants pointed out the particular challenges for Germany, which had relatively large numbers of private, defined-benefit pension funds. German accounting principles had set the expected return at 6%, which appeared unattainable under current conditions. Discussions had begun about lowering that rate to 4.5%, but even that lower rate seemed to participants to be unlikely to be achieved.

If defined-benefit pensions were to be fully funded to meet their actual obligations, companies would have to significantly increase their contributions. This, however, would cut further into profitability, reducing the potential for such companies to grow. Some participants therefore joked that in the future, many European corporations might become pension funds with companies attached, rather than the other way around. For many participants, the situation in Europe called for a shift from defined-benefit to defined-contribution pension systems, following the US model. But how to make that shift was seen as challenging.

Importantly, many participants felt that low interest rates reflected not only quantitative easing or even cyclical downturn, but rather a long-term downward trend in those rates. Eventually, however, many felt that risk premiums would rise, leading to falls in asset prices even if interest rates remained low. In this case, insurers and asset managers would be faced with the dual challenge that the asset side of their balance sheets would decline at the same time that the present value of existing liabilities would be on the rise (due to continued low future interest rates along with higher legacy interest rates). Considering the possibility of such a scenario for insurers, one participant argued that “the Japanese scenario is the upside.” Other participants argued that Europe’s problems were largely cyclical. Noting that 25 million Europeans remained unemployed, they called for more proactive fiscal policy to fill the gap and expressed cautious optimism that good macroeconomic policy could lead to stronger European growth. Stronger growth would in turn improve the prospects for insurance companies and pension funds.
Appendix

Symposium Participants
Symposium Agenda
Sponsor Profiles (forthcoming)
Symposium Participants

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Candida Wolff  
*Executive Vice President and Head of Global Government Affairs, Citi*

David Wright  
*Secretary General, International Organization of Securities Commissions (IOSCO)*

George Zavvos  
*Legal Adviser, Legal Service, European Commission*
Symposium Agenda

Wednesday, April 15

6:00-6:40 p.m.  RECEPTION

6:40-6:45 p.m.  WELCOME

➢ Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School
➢ Karel Lanno, Chief Executive Officer, CEPS

6:50-8:00 p.m.  KEYNOTE ADDRESS

➢ Daniel Gallagher, Commissioner, U.S. Securities and Exchange Commission (via video conference)
➢ Introduced by: Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School

8:00-9:30 p.m.  DINNER AND KEYNOTE

➢ Johannes Beermann, Member of the Executive Board, Deutsche Bundesbank
➢ Introduced by: Karel Lanno, Chief Executive Officer, CEPS

9:30 p.m.  AFTER-DINNER COCKTAILS

Thursday, April 16

7:30-8:20 a.m.  BREAKFAST BUFFET

8:25-9:30 a.m.  PANEL SESSION

The search for bail-inable debt: Total Loss Absorbing Capacity (TLAC) and cross border resolution

Each panelist will make a 5-7 minute presentation, followed by a plenary discussion, before all of the participants are broken into small working groups.

➢ Moderator: Greg Baer, Managing Director and Head of Regulatory Policy, JPMorgan Chase & Co.
➢ Charles Goodhart, Professor Emeritus, London School of Economics and Political Science
➢ Levin Holle, Director General, Financial Markets Policy Department, German Federal Ministry of Finance
➢ Etay Katz, Partner, Allen & Overy LLP

9:35-10:55 a.m.  SMALL GROUP SESSIONS

Participants are divided into 6 working groups for facilitated discussions with the views raised by the panelists serving as a foundation for the discussions. A facilitator encourages conversations which occur under Chatham House Rules, and a rapporteur will record the major themes (sans attribution) for use during the sessions on the final day.
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<td>Nick Reinhardt</td>
<td>Seraina Grünewald</td>
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10:55-11:10 a.m.  REFRESHMENT BREAK

11:15-11:55 a.m.  PANEL SESSION

Reform of capital markets in the US and EU. Is the US the model for the EU?
Panelists will introduce and discuss issues relevant to the topic. Each panelist will make a 5-7 minute presentation and take one or two questions before all of the participants are broken into small, working groups.

➢ Troy Beatty, Assistant Director, International Regulatory Policy, Office of International Affairs, U.S. Securities and Exchange Commission
➢ Daniel Trinder, Global Head of Regulatory Policy, Deutsche Bank AG
➢ Neena Gill, Member of the European Parliament

11:55-1:05 p.m.  SMALL GROUP SESSIONS

Participants are divided into 6 working groups for facilitated discussions with the views raised by the panelists serving as a foundation for the discussions. A facilitator encourages conversations which occur under Chatham House Rules, and a rapporteur will record the major themes (sans attribution) for use during the sessions on the final day.

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<td>S 4 (first underground floor)</td>
<td>Richard Kaye</td>
<td>Seraina Grünewald</td>
</tr>
</tbody>
</table>

1:05-2:05 p.m.  BUFFET LUNCH

2:10-2:40 p.m.  KEYNOTE ADDRESS

➢ David Wright, Secretary General, IOSCO
➢ Introduced by: Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School
2:45-4:05 p.m.  PANEL SESSION - PLENARY

Regulation and supervision for EU and US banks: Does Banking Union ease transatlantic cooperation?

_A moderator will facilitate a discussion giving all panelists equal opportunity to participate before incorporating the audience as well. Panelists remarks will provide a point of view that offers Symposium participants the benefit of analysis and insight on the topic._

**Moderator:**
- Stefan Gavell, Executive Vice President and Head of Regulatory, Industry, and Gov’t Affairs, State Street

**Panelists:**
- Christopher Bates, Partner, Clifford Chance LLP
- Elizabeth McCaul, Partner-in-Charge, New York Office, Promontory Financial Group, LLC & Chief Executive Officer, Promontory Europe

4:00-6:30 p.m.  FREE TIME\RAPPORTEURS MEETING

6:30 p.m.  GROUP BUSES DEPART FOR RESTAURANT

Please meet in the front lobby. It is a 20 minute bus ride to Gourmet Restaurant Schwarzenstein.

6:50-7:15 p.m.  RECEPTION AT RESTAURANT SCHWARZENSTEIN

7:20-7:50 p.m.  KEYNOTE ADDRESS

- Ignazio Angeloni, Member of the Supervisory Board, European Central Bank (ECB)
- Introduced by: Karel Lanno, Chief Executive Officer, CEPS

7:50-9:50 p.m.  DINNER AND KEYNOTE

- Hal Scott, Nomura Professor and Director, PIFS, Harvard Law School


10:00 p.m. - 10:15 p.m.  BUSES BACK TO THE TRAINING CENTRE

**Friday, April 17**

7:45-8:45 a.m.  BREAKFAST

9:00-9:30 a.m.  KEYNOTE ADDRESS

- Sylvie Matherat, Global Head of Government & Regulatory Affairs, Deutsche Bank
- Introduced by: Hal S. Scott, Nomura Professor and Director, PIFS, Harvard Law School
9:30-10:30 a.m.  PANEL SESSION

The effect of Quantitative Easing on capital markets

Panelists will introduce and discuss issues relevant to the topic. Each panelist will make a 7-9 minute presentation before turning it over to the audience for Q&A.

➢ Gabriel Bernardino, Chairman, European Insurance and Occupational Pensions Authority (EIOPA)
➢ Colin Ellis, Chief Credit Officer, Moody’s
➢ Burkhard Ober, Head of the Allianz SE, European Affairs Office Brussels

10:35-11:25 a.m.  PRESENTATION & DISCUSSION

The search for bail-inable debt: Total Loss Absorbing Capacity (TLAC) and cross border resolution

Panelists will moderate a plenary discussion that uses a synthesis of the small group sessions from the previous day as the basis for session.

➢ Mauro Grande, Board Member, Single Resolution Board
➢ Paul Saltzman

11:25-11:35 a.m.  REFRESHMENT BREAK

11:40-12:30 p.m.  PRESENTATION & DISCUSSION

Reform of capital markets in the US and EU: Is the US the model for the EU?

Panelists will moderate a plenary discussion that uses a synthesis of the small group sessions from the previous day as the basis for the session.

➢ Alan Houmann, Head of Government Affairs for Europe, Middle East & Africa, Citi
➢ Diego Valiante, Head of Financial Markets and Institutions, Centre for European Policy Studies (CEPS)

12:30-1:10 p.m.  ADJOURN AND LUNCHEON
2015 Symposium on Building the Financial System of the 21st Century: An Agenda for Europe and the United States

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