



2010

The French banking and insurance  
market in figures, 2010





# 2010

## The French banking and insurance market in figures, 2010

This annual report provides statistics for the French banking and insurance sector in 2010. It also includes an initial review of how international principles on compensation policies have been applied at major banks in France and in leading foreign countries.



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# Introduction

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### **The earnings and financial position of French banks and insurers improved markedly in 2010 compared with 2009.**

Despite a volatile environment, French banks and insurers took the steps needed to consolidate their financial position.

The consolidated net income of the main banks<sup>1</sup> rose by 77%. In addition to reducing their risk-related costs (by 35.9% compared with 2009) as a result of the mild economic upturn, banks were buoyed by attractive market refinancing costs, which enabled them to increase interest income. All lines of business performed strongly, with net banking income growing by 10% on average. French banks also significantly scaled back their exposure to “toxic” assets, by 18% compared with 2009.

The main banks allocated a large proportion of profits to reserves and distributed more earnings in the form of scrip. As a result, their aggregate Tier One ratio rose to the historically high level of 10.7% at end-2010 (70 basis points higher than in 2009).

Developments in the insurance sector were equally favourable. In 2010, life underwriting income totalled 5.1 billion, up 11% on 2009, while non-life underwriting income rose more than 10% to 3.6 billion. Investment income in non-life insurance grew by 11%, offsetting the increase in claim payouts owing to the year’s significant loss experience (one-off weather events, Atlantic Storm Xynthia, flooding in the Var region, etc.) and the decline in gross new funds going into life insurance (1% lower than in 2009).

Coverage ratios for regulated commitments were also satisfactory.

At end-2010, the coverage ratio without unrealised gains was 126% for life insurers. Ultimately, however, the ratio was down slightly in 2010 in all categories of insurers. Moreover, the coverage ratio with unrealised gains was lower in all categories because of the decline in unrealised gains on bonds at year’s end.

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1. Data for BNP Paribas, Société Générale, Crédit Agricole group, Crédit Mutuel group, BPCE group, HSBC France and Dexia Crédit Local.



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Sound banking system,  
uncertain environment

# 1. Population

## 1.1 Population of credit institutions and investment firms

France's banking and financial system continued to consolidate and adjust in 2010. As a result, the population of credit institutions shrank further, from 706 at end-2009 to 683 at end-2010. The bulk of the decline involved financial companies (13 fewer institutions) and banks (six fewer). Specialised financial institutions were proportionately more affected, as their number fell from five to three. The number of mutual and cooperative banks stayed the same.

The number of investment firms supervised by the Autorité de contrôle prudentiel (ACP) fell by one. At end-2010, four payment institutions were authorised to do business in France (three authorised by the ACP, one under the freedom of establishment). The number of credit institutions authorised to do business in Monaco decreased by two to 24.

### Credit institutions, investment firms and payment institutions in France, and credit institutions in Monaco

A - CREDIT INSTITUTIONS AUTHORISED IN FRANCE	2009	2010	Change (number)
I. INSTITUTIONS AUTHORISED TO ENGAGE IN ALL BANKING TRANSACTIONS	331	325	-6
1.1 Banks	212	206	-6
1.2 Mutual and cooperative banks	101	101	-
1.3 Municipal credit banks	18	18	-
II. FINANCIAL COMPANIES	300	287	-13
III. SPECIALISED FINANCIAL INSTITUTIONS	5	3	-2
SUB-TOTAL	636	615	-21
<b>B - BRANCHES OF EEA CREDIT INSTITUTIONS DOING BUSINESS UNDER THE FREEDOM OF ESTABLISHMENT</b>	<b>70</b>	<b>68</b>	<b>-2</b>
<b>TOTAL FRANCE</b>	<b>706</b>	<b>683</b>	<b>-23</b>
C - CREDIT INSTITUTIONS AUTHORISED IN MONACO	2009	2010	Change (number)
I. INSTITUTIONS AUTHORISED TO ENGAGE IN ALL BANKING TRANSACTIONS	25	23	-2
1.1 Banks	24	22	-2
1.2 Institution similar to a municipal credit bank belonging to FBF(*)	1	1	-
II. FINANCIAL COMPANIES			
Financial companies engaging in different types of business and belonging to ASF(**)	1	1	-
<b>TOTAL MONACO</b>	<b>26</b>	<b>24</b>	<b>-2</b>
<b>TOTAL FRANCE AND MONACO</b>	<b>732</b>	<b>707</b>	<b>-25</b>

(\*) French Banking Federation

(\*\*) French Association of Financial Companies

INVESTMENT FIRMS	2009	2010	Change (number)
I. Investment firms authorised by the ACP	98	97	-1
Branches of investment firms doing business under the freedom of establishment	53	59	+6
II. Portfolio management companies authorised by the Autorité des marchés financiers (a)	591	629	+38
<b>TOTAL</b>	<b>689</b>	<b>726</b>	<b>+37</b>

(a) Data taken from the GECO database available on the website of the Autorité des marchés financiers.

PAYMENT INSTITUTIONS	2010
I. Payment institutions authorised by the ACP	3
Branches of payment institutions doing business under the freedom of establishment	1
<b>TOTAL</b>	<b>4</b>

Source: General Secretariat of the ACP

## 1.2 The banking sector in 2010

### 1.2.1 Diversified ownership

The French banking and financial system is very open. At end-2010, 70% or 479 of the 683 credit institutions doing business in France were under French ownership, and 30%, or 204, were foreign-owned. Of this total, 74% were owned by banking groups, including 38% by French mutual banking groups, and 26% were controlled by shareholders in other economic sectors, with 9% belonging to manufacturing, trade and service groups, 3% owned by insurance groups, 7% owned by other financial groups or a mix of shareholders, 4% mainly in the hands of private individuals and 3% held by the public sector. Industrial and trade groups have always held a significant stake in France's population of credit institutions, which is not necessarily the case in comparable countries such as Germany, Italy or the United States. By contrast, insurance groups hold a relatively small stake in banks in France

#### French-owned credit institutions by type of ownership at end-2010

Ownership	Number of credit institutions in 2010					Number of shareholding groups in 2010
	Banks	Mutual banks	Financial companies	Others*	Total	
Large private-sector banking groups	31	0	63	0	94	2
Public-sector banking institutions	2	0	3	20	25	4
Mutual banking groups	65	100	98	0	263	4
Insurance companies	4	1	6	0	11	7
Manufacturing, trade, services, construction, business groups	14	0	21	0	35	23
(of which public sector)	(1)	0	(1)	0	0	(1)
Institutions with mixed ownership (credit institutions, institutional investors)	6	0	24	1	31	25
Owned by private individuals	10	0	10	0	20	17
<b>TOTAL</b>	<b>132</b>	<b>101</b>	<b>225</b>	<b>21</b>	<b>479</b>	<b>82</b>

(\*) Municipal credit banks and specialised financial institutions.

Source: General Secretariat of the ACP

#### Foreign-owned credit institutions by type of ownership and geographical origin at end-2010

Ownership	Number of credit institutions at end-2010								Total number of groups
	Banks				Financial companies and specialised financial institutions				
	OECD		Third countries	Total	OECD		Third countries	Total	
	EEA	Other countries			EEA	Other countries			
Banking group branches	68	8	15	91	0	0	0	0	106
Banking group subsidiaries	13	5	10	28	23	1	3	27	
Insurance companies	4	2	0	6	2	0	0	2	6
Financial groups	2	4	0	6	0	7	0	7	13
Manufacturing, trade, services	1	3	0	4	8	15	0	23	12
Owned by private individuals	0	3	1	4	0	0	0	0	4
Mixed banking and financial ownership	1	1	1	3	3	0	0	3	5
<b>TOTAL</b>	<b>89</b>	<b>26</b>	<b>27</b>	<b>142</b>	<b>36</b>	<b>23</b>	<b>3</b>	<b>62</b>	<b>146</b>

Source: General Secretariat of the ACP

The French banking and financial system is also very open to international markets. This is evidenced in the large number of foreign-owned institutions in France and the presence of French-owned credit institutions in other countries.

### 1.2.2 Open to foreign capital

France's banking and financial system is very open to foreign-owned institutions<sup>2</sup>.

At end-2010, a total of 204 foreign controlled credit institutions were doing business in France. This breaks down into 142 banks, 61 financial companies and one specialised financial institution, along with 76 investment firms and 74 representative offices.

Of the 204 foreign controlled credit institutions, most were from the European Union. This was the case of 125 institutions, including 32 from the United Kingdom, 22 from Germany, 15 from Belgium, 14 from the Netherlands and 12 from Italy.

The 79 credit institutions controlled by third-country owners are mainly American (34, including 11 banks, 21 financial companies and one specialised financial institution).

#### Foreign presence in France's banking and financial system

	2001	2002	2003	2004	2005	2006	2007	2008	2009	2010
<b>BANKS</b>	<b>188</b>	<b>176</b>	<b>168</b>	<b>164</b>	<b>161</b>	<b>161</b>	<b>161</b>	<b>155</b>	<b>147</b>	<b>142</b>
<b>Branches</b>	<b>83</b>	<b>79</b>	<b>80</b>	<b>82</b>	<b>81</b>	<b>84</b>	<b>88</b>	<b>93</b>	<b>93</b>	<b>91</b>
European Economic Area	55	51	52	55	55	59	64	70	70	68
Third countries	28	28	28	27	26	25	24	23	23	23
<b>Companies incorporated in France</b>	<b>105</b>	<b>97</b>	<b>88</b>	<b>82</b>	<b>80</b>	<b>77</b>	<b>73</b>	<b>62</b>	<b>54</b>	<b>51</b>
European Economic Area										
Subsidiaries of foreign-owned banks	59	56	47	40	40	34	33	21	16	13
Companies controlled by non-bank investors	11	8	10	8	8	9	9	9	7	7
Mixed banking and financial ownership	0	0	0	1	1	1	0	0	1	1
Third countries										
Subsidiaries of foreign-owned banks	18	17	16	16	15	15	14	16	15	15
Companies controlled by non-bank investors	15	14	13	15	14	15	14	13	13	13
Mixed banking and financial ownership	2	2	2	2	2	3	3	3	2	2
<b>FINANCIAL COMPANIES (companies incorporated in France)</b>	<b>123</b>	<b>110</b>	<b>95</b>	<b>83</b>	<b>78</b>	<b>75</b>	<b>76</b>	<b>74</b>	<b>66</b>	<b>61</b>
European Economic Area										
Financial companies for various purposes	91	81	68	58	57	55	54	53	42	36
Third countries										
Financial companies for various purposes	32	29	27	25	21	20	22	21	24	25
<b>SPECIALISED FINANCIAL INSTITUTIONS</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>1</b>	<b>2</b>	<b>1</b>	<b>1</b>	<b>1</b>
<b>TOTAL CREDIT INSTITUTIONS</b>	<b>312</b>	<b>287</b>	<b>264</b>	<b>248</b>	<b>240</b>	<b>237</b>	<b>239</b>	<b>230</b>	<b>214</b>	<b>204</b>
<b>INVESTMENT FIRMS (*)</b>	<b>70</b>	<b>61</b>	<b>55</b>	<b>53</b>	<b>52</b>	<b>56</b>	<b>67</b>	<b>75</b>	<b>71</b>	<b>76</b>
European Economic Area	56	48	44	42	41	43	54	63	61	66
Branches	(24)	(23)	(23)	(24)	(23)	(28)	(41)	(52)	(53)	(59)
Unpassport branches	-	-	-	-	(1)	(1)	(1)	-	-	-
Companies incorporated in France	(32)	(25)	(21)	(18)	(17)	(14)	(12)	(11)	(8)	(7)
Third countries	14	13	11	11	11	13	13	12	10	10
<b>REPRESENTATIVE OFFICES</b>	<b>89</b>	<b>82</b>	<b>75</b>	<b>78</b>	<b>75</b>	<b>74</b>	<b>78</b>	<b>80</b>	<b>77</b>	<b>74</b>
European Economic Area	42	34	35	39	31	28	31	32	29	27
Third countries	47	48	40	39	44	46	47	48	48	47

(\*) Excl. portfolio management companies.

Source: General Secretariat of the ACP

2. This paragraph deals only with majority holdings in credit institutions doing business in France.

## 1.3 Widespread use of the European passport

### 1.3.1 Access to the French market

#### BRIEFING

##### Freedom of establishment

Freedom of establishment means that a market participant from a Member State of the European Economic Area is entitled to provide services in another Member State through a permanent establishment such as a branch or an agency.

##### Freedom to provide services

Freedom to provide services means that a market participant from a Member State is entitled to provide services in another Member State without having a permanent establishment there.

#### Freedom of establishment

Of a total of 127 branches of European credit institutions and investment firms (23 branches of credit institutions and investment firms from outside Europe are also established in France), those belonging to UK parent companies form the largest contingent, with 64 business locations in 2010, after several years of strong growth following implementation of the Markets in Financial Instruments Directive (MiFID). MiFID gave investment firms incorporated in European Union countries the benefit of mutual recognition for a wider range of services and instruments, and more particularly for instruments such as contracts for difference and commodities derivatives. The directive also allows firms to use tied agents. Many investment firms have sought to take advantage of MiFID-related opportunities. However, these branches are very often small, with fewer than ten employees.

The European passport is widely used to set up establishments in France, but it is also used by institutions from outside the European Economic Area (EEA). With just a single authorised entity in one of the EEA countries, these institutions can exercise their passport rights to do business in one or more other EEA countries. Of the total number of passported branches in France at 31 December 2010, 48 belonged to groups owned by non-EEA shareholders. These branches accounted for 32% of the passported branches located in France.

#### Branches opened by credit institutions or investment firms in France

	2000	2007	2008	2009	2010
<b>Notifying countries</b>	<b>75</b>	<b>104</b>	<b>122</b>	<b>123</b>	<b>127</b>
United Kingdom	30	49	59	60	64
Germany	15	16	17	16	15
Italy	5	6	6	7	7
Netherlands	3	6	6	7	7
Spain	8	6	6	6	6
Other countries	14	21	28	27	28
<b>Passported branches where the ultimate owners are outside the EEA</b>	<b>7</b>	<b>30</b>	<b>44</b>	<b>45</b>	<b>48</b>
United States	3	19	28	28	30
Japan	1	3	4	4	4
Switzerland	1	2	3	3	3
Lebanon	1	1	1	1	1
Other countries	1	5	8	9	10

Source: General Secretariat of the ACP

## Freedom to provide services

Freedom to provide services (FPS) is the alternative way of using the EEA passport to do business in another EEA country without having a permanent establishment there. The only metrics available for assessing this activity are the number and change in the number of institutions notifying their intention to exercise FPS. As of 31 December 2010, 518 European credit institutions, 2,153 European investment firms and 43 European payment institutions were authorised to do business in France under FPS (see table below).

The number of institutions giving notice of their intention to do business in France increased by 14% over the year, after an increase of 5% in 2009.

### FPS notifications in effect at 31 December 2010

Country	Free provision of services in France		
	Notifications from 518 credit institutions authorised in another EEA country	Notifications from 2,153 investment firms authorised in another EEA country	Notifications from 43 payment institutions authorised in another EEA country
Germany	82	43	1
Austria	28	23	0
Belgium	30	23	1
Bulgaria	0	2	0
Cyprus	5	33	0
Denmark	15	11	1
Spain	21	20	0
Estonia	1	1	0
Finland	8	4	0
Greece	2	9	0
Hungary	7	2	0
Ireland	37	50	3
Iceland	4	0	0
Italy	27	7	0
Latvia	0	0	0
Liechtenstein	3	10	0
Lithuania	0	0	0
Luxembourg	60	34	1
Malta	8	4	0
Norway	3	22	0
Netherlands	55	85	0
Poland	2	0	0
Portugal	18	6	0
Czech Rep.	1	1	0
Romania	0	1	0
United Kingdom	91	1,752	35
Slovakia	0	0	0
Slovenia	0	1	1
Sweden	10	9	0
<b>TOTAL</b>	<b>518</b>	<b>2,153</b>	<b>43</b>

Source: General Secretariat of the ACP

## 1.3.2 Passporting by French institutions

### Freedom of establishment

French institutions use EEA passports primarily to open establishments in Germany, Italy, the United Kingdom, Spain and, to a lesser extent, Belgium. The number of passported branches opened by French institutions in other EEA countries has been stable since 2008 and totalled 166 at the end of 2010.

## Branches opened by French credit institutions and investment firms in other EEA countries

	2000	2007	2008	2009	2010
<b>Main notifying countries</b>					
United Kingdom	21	24	23	24	24
Germany	18	22	26	26	26
Italy	13	21	24	25	24
Spain	15	20	21	21	23
Belgium	9	17	17	15	16
Other countries	30	46	54	54	53
<b>TOTAL</b>	<b>106</b>	<b>150</b>	<b>165</b>	<b>165</b>	<b>166</b>

Source: General Secretariat of the ACP

### Freedom to provide services

As of 31 December 2010, a total of 1,181 notifications had been received from 155 French credit institutions and 571 notifications from 52 French investment firms seeking to do business in another EEA country. The main countries targeted by French credit institutions were Italy (99 notifications), the United Kingdom (95), Belgium (90), Germany (82) and Spain (75), while French investment firms targeted Belgium (48 notifications), the Netherlands (43), the United Kingdom (37), Germany (37) and Italy (35).

### FPS notifications in effect at 31 December 2010

Country	FPS in other EEA countries	
	Notifications from 155 credit institutions authorised in France	Notifications from 52 investment firms authorised in France
Germany	82	37
Austria	49	22
Belgium	90	48
Bulgaria	13	6
Cyprus	16	9
Denmark	43	18
Spain	75	35
Estonia	16	11
Finland	37	21
Greece	38	15
Hungary	25	13
Ireland	48	22
Iceland	12	8
Italy	99	35
Latvia	15	10
Liechtenstein	15	10
Lithuania	15	10
Luxembourg	74	31
Malta	14	9
Norway	26	15
Netherlands	71	43
Poland	29	14
Portugal	63	29
Czech Rep.	21	13
Romania	21	6
United Kingdom	95	37
Slovakia	20	12
Slovenia	14	10
Sweden	45	22
<b>TOTAL</b>	<b>1,181</b>	<b>571</b>

Source: General Secretariat of the ACP



## 2. Higher net banking income and lower risk-related costs boost profitability

In 2009, some institutions were still feeling the effects of the crisis. In a positive sign, however, the intermediate operating totals for France's seven largest banks<sup>3</sup> improved in 2010.

### Intermediate operating totals

EUR billion	2008	2009	2010	2009/2010 change in %
Net banking income	107.8	132.1	145.1	9.8
General operating expenses	79.7	85.7	91.1	6.4
Gross operating income	28.1	46.4	54.0	16.3
Risk-related costs	21.1	28.0	18.0	-35.9
Operating income	7.1	18.4	36.0	95.7
Consolidated net income	4.3	12.2	21.7	77.2

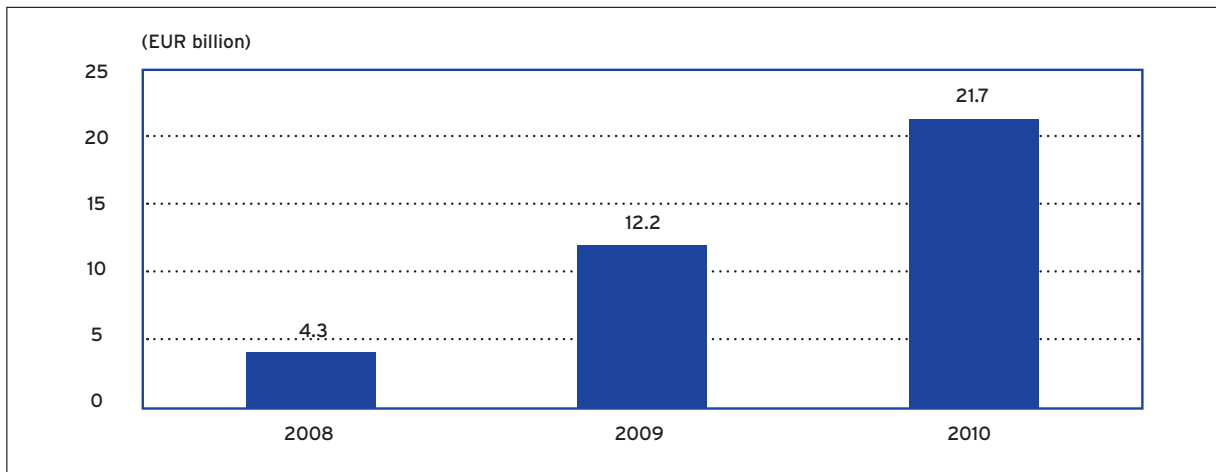
Source: Banks (IFRS data)

Consolidated net income<sup>4</sup> increased by 77%, returning to 2007 levels (EUR 21.3 billion), i.e. before the financial crisis gathered momentum.

3. BNPP, SG, GCA, GCM, GBPCE, HSBC France and Dexia Crédit Local.

4. Net income attributable to the group (or group share) does not include income attributable to minority interests.

## Consolidated net income

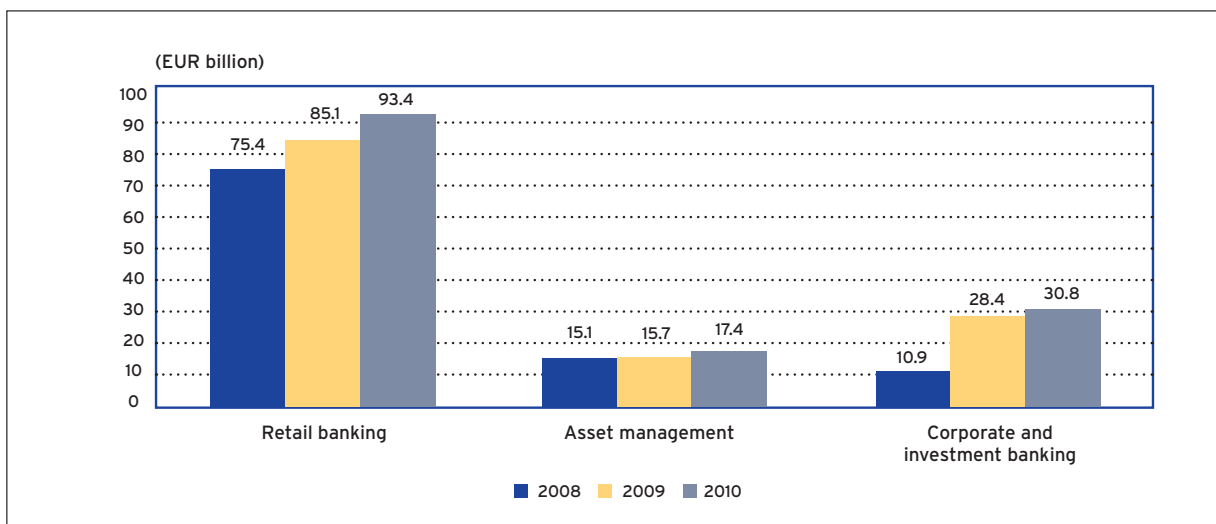


Source: Banks

## 2.1 Higher net banking income

Net banking income rose by almost 10% on sustained business activity. Growth was seen across all lines of business.

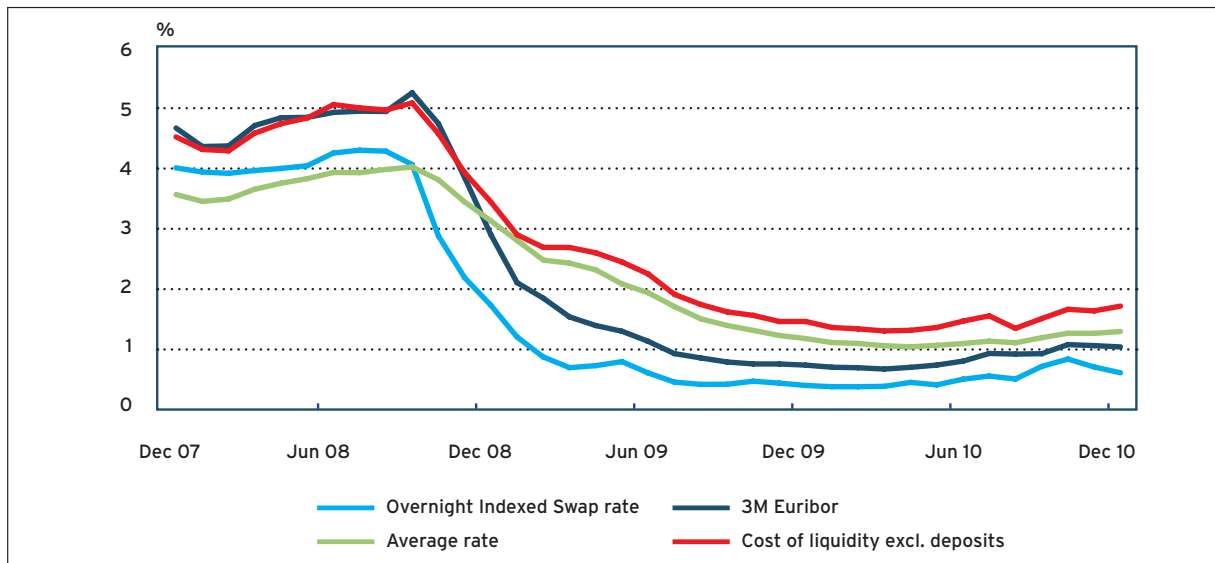
### Net banking income by business line



Source: Banks

In addition to the economic upturn, the cost of liquidity remained moderate in 2010, which certainly played a part in the strong marketplace performance.

## Cost of liquidity



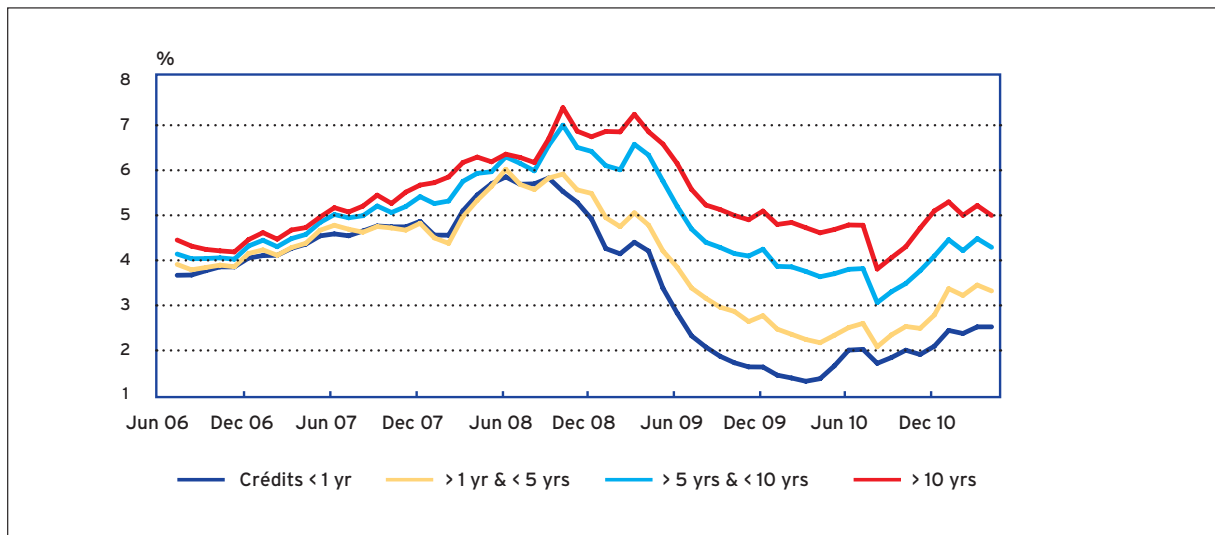
Sources: Bloomberg, Markit, General Secretariat of the ACP

However, refinancing costs started heading upwards again in the final quarter of 2010.

### BRIEFING

The Overnight Indexed Swap rate (OIS) is the overnight financing rate on the interbank market, whereas the 3-month Euribor is the rate for uncollateralised financing up to three months. The spread between the two rates is commonly used to show a loss of confidence on the interbank market.

## Loan refinancing costs



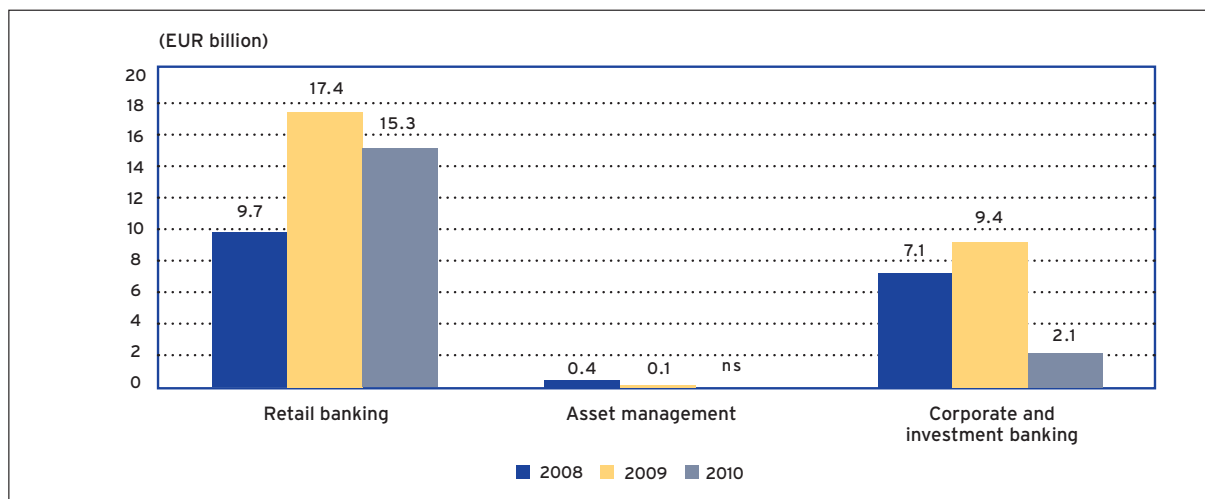
Sources: Markit, Bloomberg, General Secretariat of the ACP

General operating expenses rose moderately, with much of the increase due to BNP Paribas' ongoing integration of Fortis. Overall, other groups improved their operating efficiency and hence their cost/income ratios.

## 2.2 Reduced risk-related costs

The change in risk-related costs is another key factor in the improvement in operating income. Risk-related costs fell by 36% across all segments, with an especially steep fall for corporate and investment banking.

### Risk-related costs by business line



Source: Banks

The decline in risk-related costs is attributable to the improved situation in terms of banks' "sensitive" portfolios.

### 2.2.1 Improved situation in terms of "sensitive" portfolios

Total holdings of "sensitive" assets declined by 18%, falling from EUR 28.5 billion to EUR 23.1 billion among France's five main banking groups. In this respect, the writedown on monoline insurers fell by 31%, while the coverage ratio increased to 69%. The coverage ratio for collateralised debt obligations (CDOs) was stable.

### Writedowns of CDO and monoline guarantees

EUR billion	2008		2009		2010	
	CDO	Monolines	CDO	Monolines	CDO	Monolines
Exposure net of hedges	12.1	14.0	16.2	9.0	22.8	5.9
Writedowns	5.1	8.5	9.9	6.0	13.8	4.1
Net exposure	7.0	5.5	6.3	3.0	8.0	1.8
Coverage ratio (%)	42	61	61	67	61	69

Source: Banks (BNPP, SG, GCA, GBPCE and GCM)

#### BRIEFING

Collateralised debt obligations (CDOs): debt securities issued by a securitisation vehicle, usually segmented by risk and backed by a diversified portfolio of bank loans.

There was also a decline in other types of exposure considered to be sensitive (other CDOs, UK or Spanish residential mortgage-backed securities (RMBS) and leveraged buyouts), which went from EUR 84.4 billion at end-2009 to EUR 69.9 billion in December 2010.

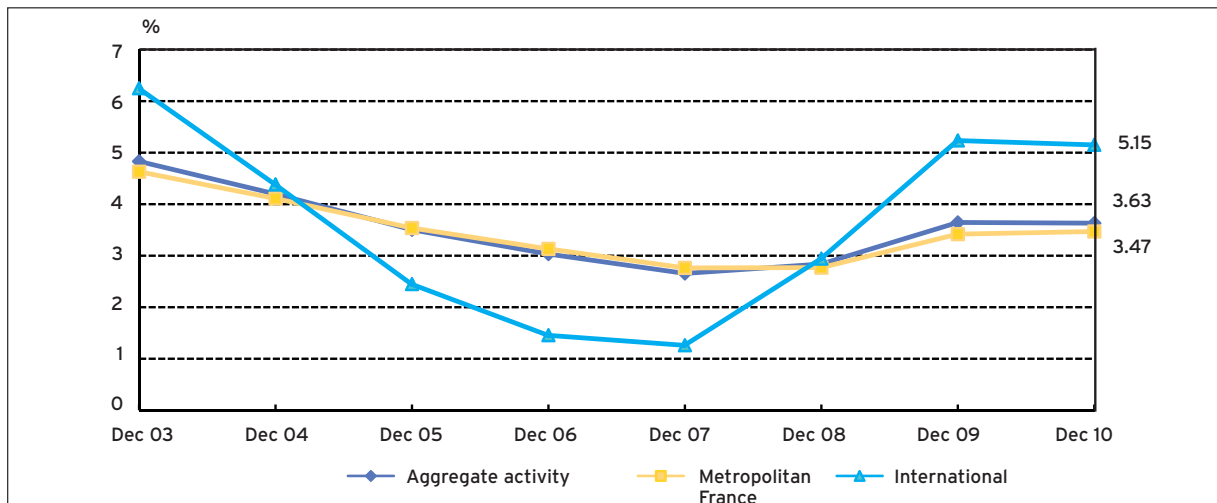
**BRIEFING**

Leveraged buyout (LBO): an LBO is a structured financial transaction whereby investors acquire a company through a special purpose holding company. The holding company borrows from banks (creating leverage) to buy the target company. The purchased firm repays the loan, so investors have to pay only a portion of the total value of the company.

**2.2.2 In retail banking, risk-related costs stabilise at a lower level**

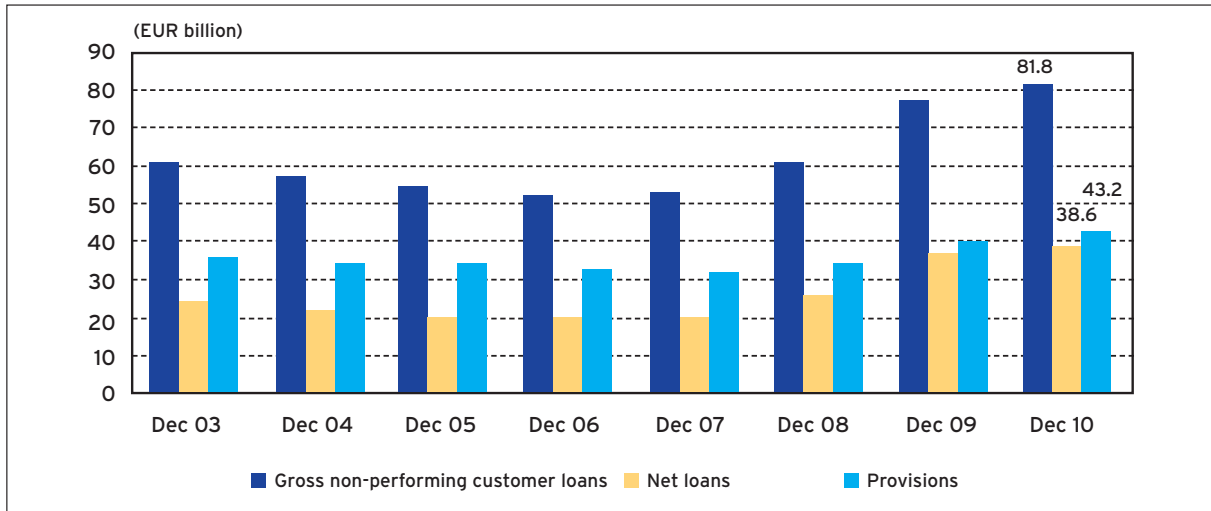
In the retail segment, risk-related costs fell from their 2009 peak but still remain well above the levels seen in 2008, with continued stress in customer transactions. While the ratio of non-performing loans (all customer categories) to gross lending levelled off in absolute terms, non-performing customer loans continued to grow, overtaking the EUR 80 billion mark.

**Gross non-performing loans as a percent of gross lending  
(Aggregated parent-company data)**



Source: General Secretariat of the ACP

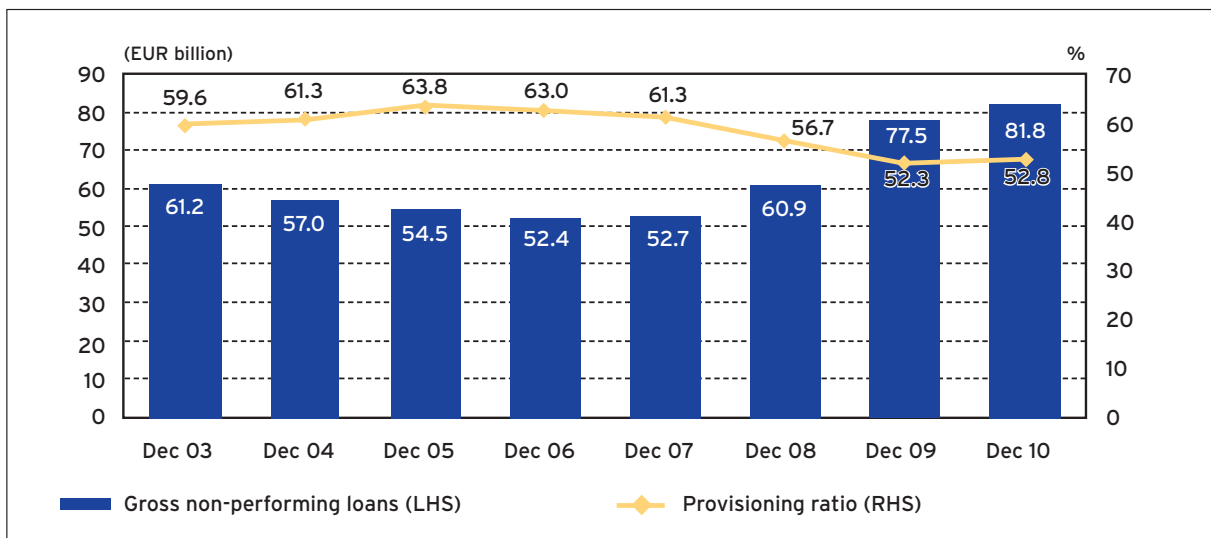
**Non-performing customer loans  
(Aggregated parent-company data)**



Source: General Secretariat of the ACP

Total provisions grew faster than total gross non-performing loans. This can be seen as a need to stabilise the provisioning ratio, which stands at close to 50% following several years of decline, rather than a worsening outlook for collection.

**Overall ratio of provisions to non-performing customer loans  
(Aggregated parent-company data)**



Source: General Secretariat of the ACP

## 3. Capital and solvency ratios at historically high levels

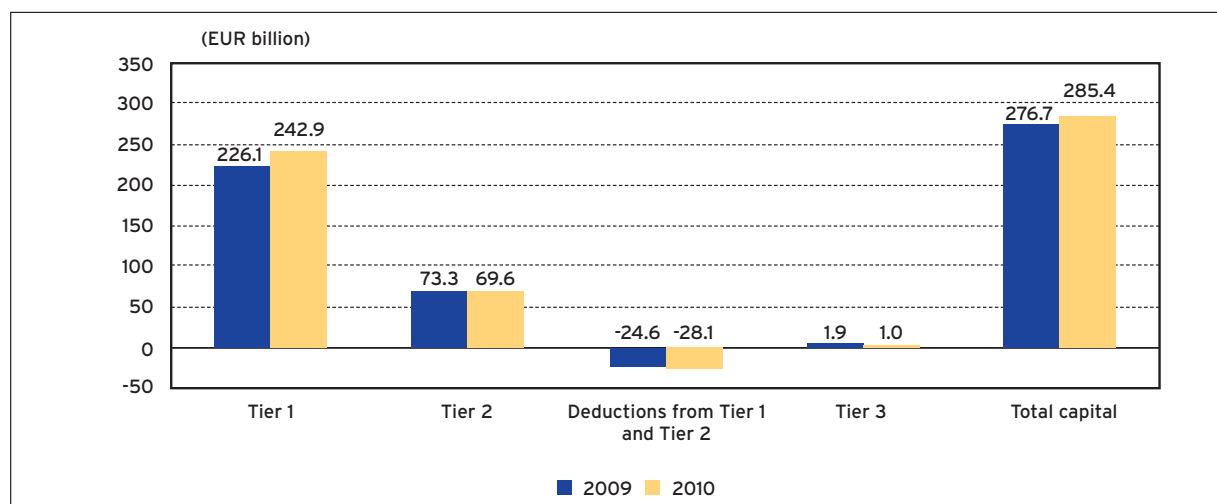
### 3.1 Capital continues to increase

Banks allocated a large proportion of their profits to reserves and this, coupled with managed growth in risk-weighted assets, took solvency ratios to historically high levels. In Q1 2011, banks repaid all the remaining support provided by the government in 2009 to bolster their equity.

Banks prepared actively for the transition to the new banking regulations set out in Basel 3. The new Capital Accord is designed among other things to enhance the level and quality of banks' capital. The increase in capital was therefore concentrated in Core or Tier One capital, which comprises the "purest" components of capital.

All the charts in this section cover France's seven main banking groups.

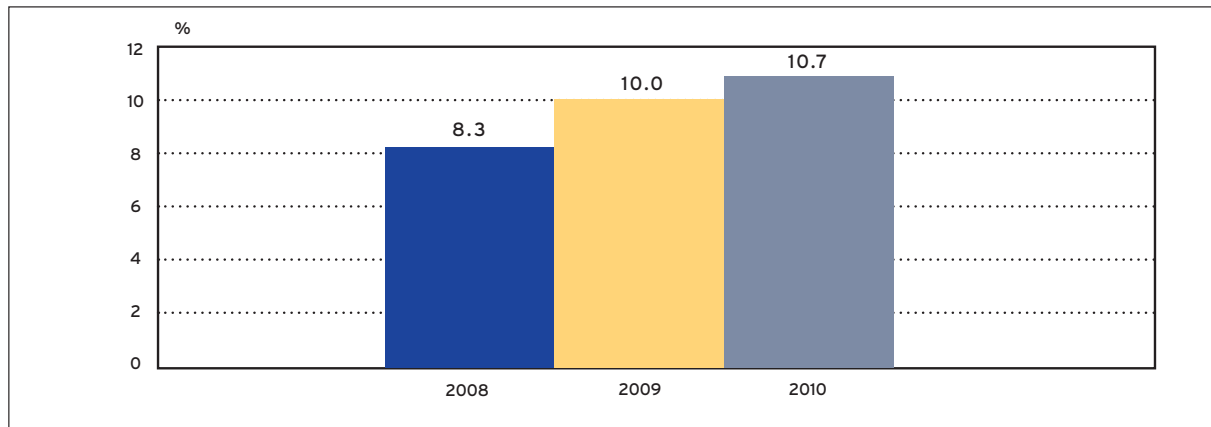
#### Total capital and its components



Source: General Secretariat of the ACP

The average Tier One ratio continued to increase, reaching an all-time high of 10.7%.

### Tier One Ratio

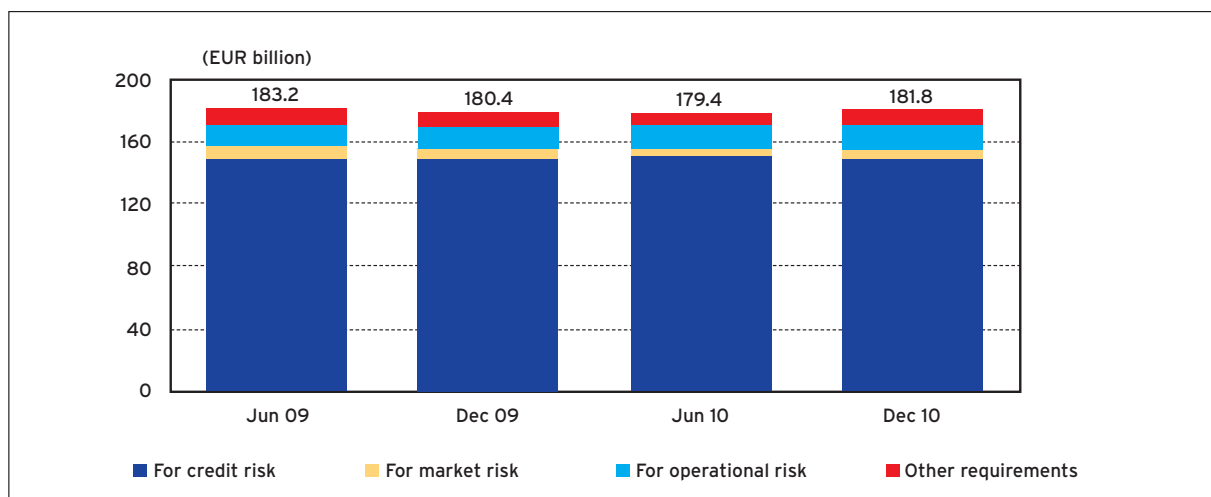


Source: General Secretariat of the ACP

## 3.2 Capital requirements kept in check

Capital requirements stayed more or less the same, in a sign that risks remained under control.

### Capital requirements

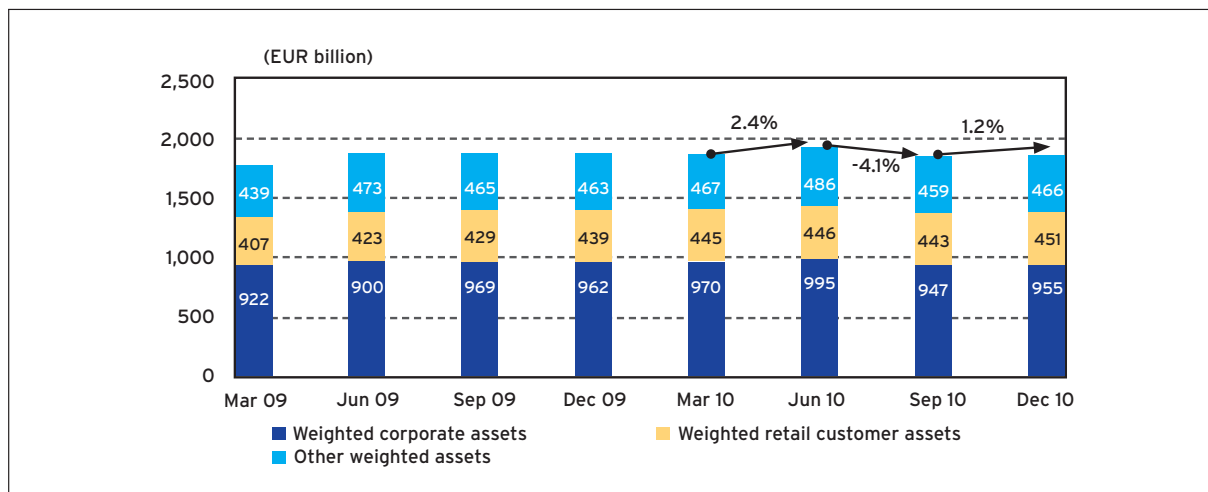


Source: General Secretariat of the ACP

### 3.2.1 Credit risk

The share of capital requirements for credit risk was stable at 82.4%. Risk-weighted assets increased by just 0.4% year-on-year, as the decline in weighted corporate assets offset the increase in weighted retail assets.

#### Credit risk-weighted assets

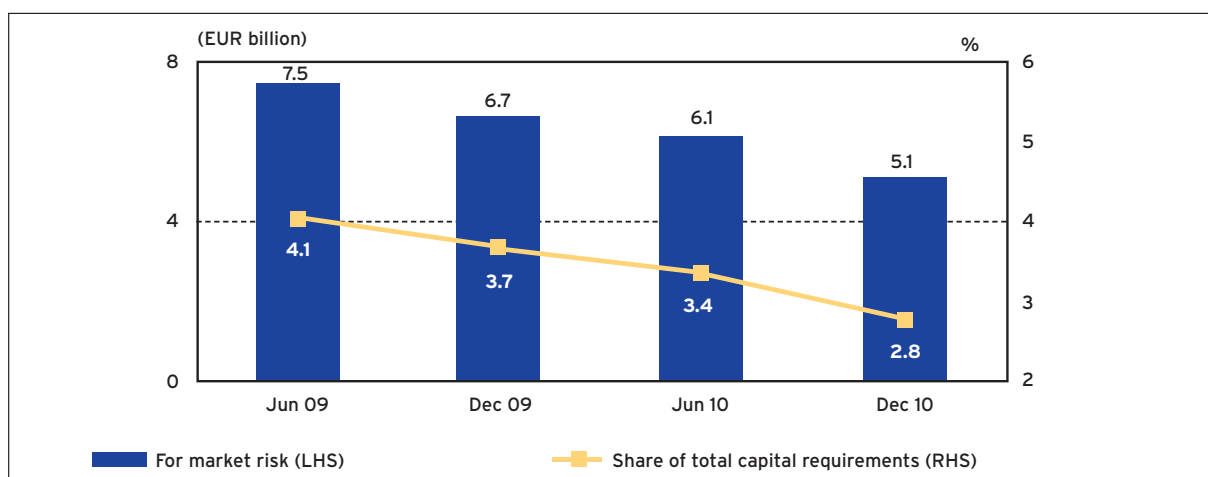


Source: General Secretariat of the ACP

### 3.2.2 Market risk

Capital requirements for market risk continued to decline in absolute terms and as a percentage of total capital requirements. Value at Risk (VaR) was steady at a lower level than that recorded in 2008. However, there was greater volatility in the first half of 2011 owing to concerns generated by the sovereign debt crisis.

#### Capital requirements for market risk

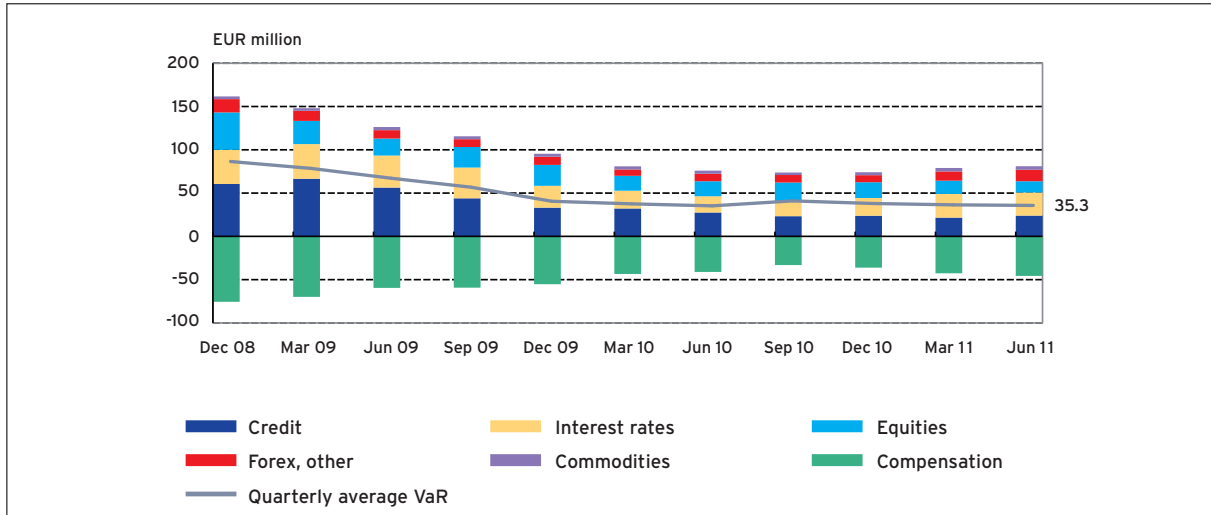


Source: General Secretariat of the ACP

**BRIEFING**

Value at Risk (VaR) is the maximum potential loss that an institution could incur in the value of an asset or a portfolio of financial assets in the event of adverse developments under normal market conditions over a prescribed holding period at a given confidence interval.

**1-day VaR and average quarterly VaR**

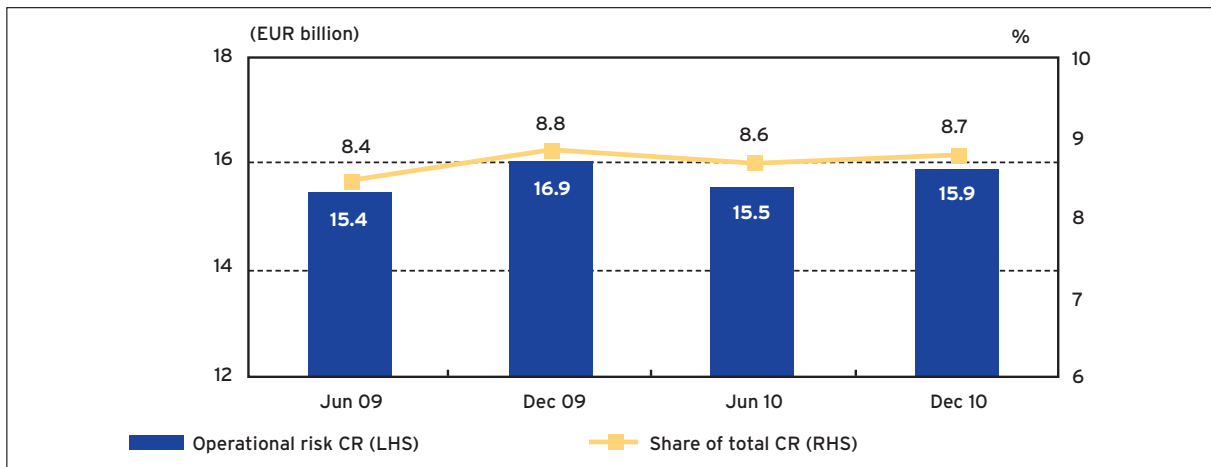


Source: Banks (BNPP, SG and CASA)

**3.2.3 Operational risk**

After surging by 15% between 2008 and 2009 capital requirements for operational risk stabilised in 2010, remaining below 9% of total requirements.

**Capital requirements for operational risk**



Source: General Secretariat of the ACP



## 4. Refocusing on customer business

### 4.1 Major groups' balance sheets

---

After contracting in 2009, total assets increased slightly in 2010, as the downturn in available-for-sale financial assets and financial assets at fair value through profit or loss was more than offset by the increase in customer loans and receivables.

The same was true on the liabilities side, with amounts owed to customers increasing even faster (5%) than on the assets side and making up for the strong contraction in other items, such as amounts owed to credit institutions and financial liabilities at fair value through profit or loss.

Efforts to refocus on customer business, which were noted in 2009, continued in 2010, with the result that customers now account for around one-half of assets and one-third of liabilities. As part of this, the ratio of customer loans and receivables to amounts owed to customers fell below 150%.

Banks appeared to take a prudent approach, with strong growth in hedging transactions on both sides of the balance sheet and a 4% increase in the book value of capital.

## Aggregated consolidated balance sheet of the seven leading banking groups

(EUR billion)	2008	2009	2010	2010/2009 change
<b>ASSETS</b>				
Financial assets at fair value through profit or loss	68.5	68.9	61.2	-11
Derivative hedging instruments	46.5	52.9	59.6	13
Available-for-sale financial assets	346.4	441.1	424.1	-4
Financial assets held for trading	2,550.5	1,812.6	1,813.3	0
Loans and advances to credit institutions	524.6	495.1	489.3	-1
Customer loans and receivables	2,791.8	3,025.9	3,145.3	4
Held-to-maturity financial assets	21.9	20.7	18.4	-11
Other	475.9	505.6	475.1	-6
<b>LIABILITIES</b>				
Financial liabilities held for trading	2,220.8	1,545.0	1,582.7	2
Financial liabilities at fair value through profit or loss	165.0	170.8	152.1	-11
Derivative hedging instruments	78.2	73.6	87.2	19
Amounts owed to institutions	778.7	693.1	614.7	-11
Amounts owed to customers	1,840.7	2,125.5	2,231.1	5
Debt evidenced by a certificate	1,013.2	1,075.9	1,103.2	3
Provisions	19.5	26.1	25.0	-4
Subordinated debt	100.7	102.8	101.3	-1
Consolidated shareholders' equity	216.1	266.3	277.2	4
Other	393.2	343.7	311.7	-9
<b>TOTAL</b>	<b>6,826.1</b>	<b>6,422.8</b>	<b>6,486.2</b>	<b>1</b>

Source: General Secretariat of the ACP

## 4.2 Structure of the French banking system

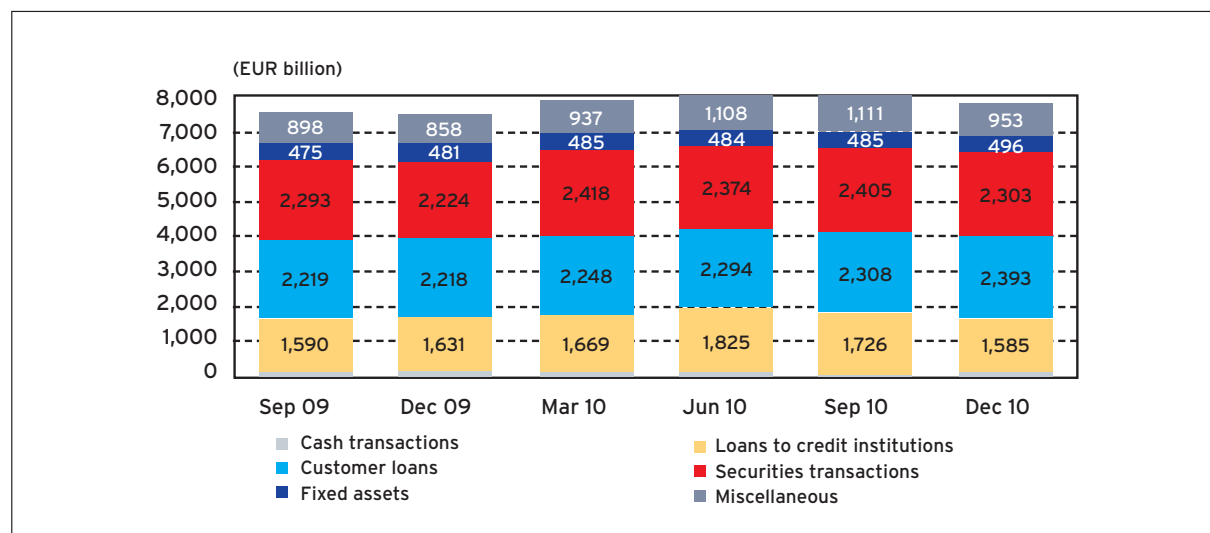
### BRIEFING

The analysis in the previous section consolidates the earnings and activity of a sample of the seven leading banking groups, in both accounting and prudential terms. It therefore includes all transactions, including those carried out by subsidiaries in other countries. The following analysis looks at aggregated parent-company data, which provide more detailed information about all credit institutions and investment firms. The discrepancies between these two complementary views stem from differences in consolidation structure, consolidation methods and accounting standards.

## 4.2.1 Assets

### Asset components

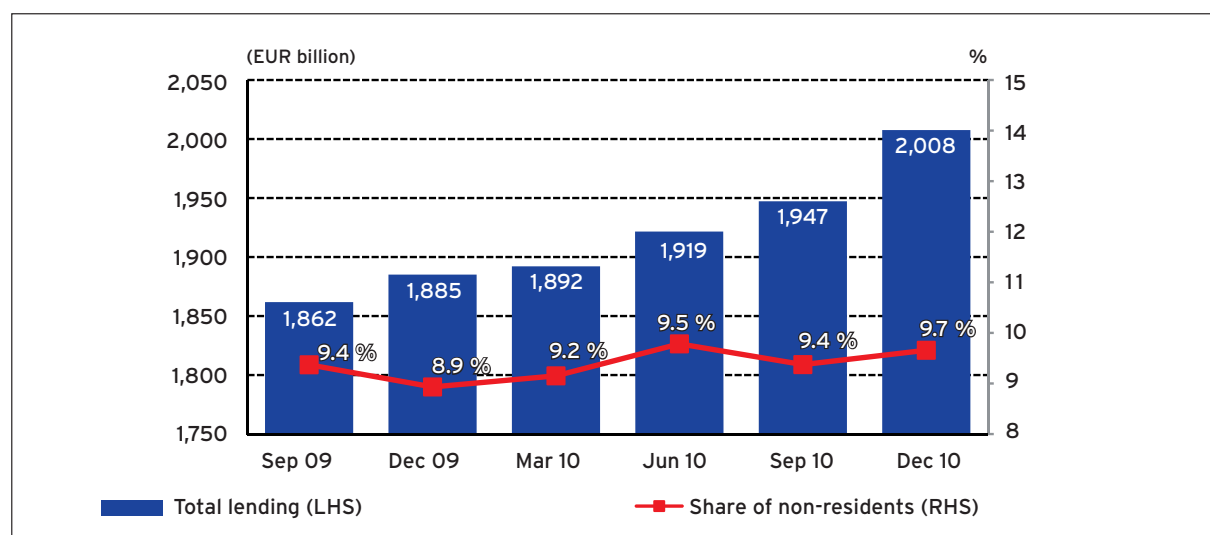
(Aggregated parent-company data)



Source: General Secretariat of the ACP

Sustained levels of business were responsible for the renewed growth in total assets. Outstanding customer loans, which account for 31% of total assets, grew strongly in all quarters.

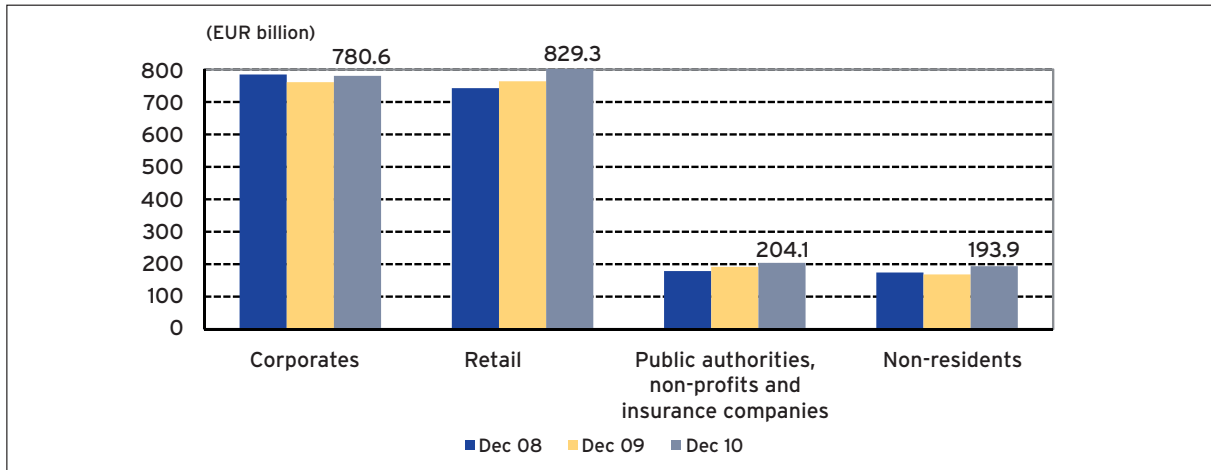
### Lending to the economy provided by the French banking system (Aggregated parent-company data, business in metropolitan France)



Source: General Secretariat of the ACP

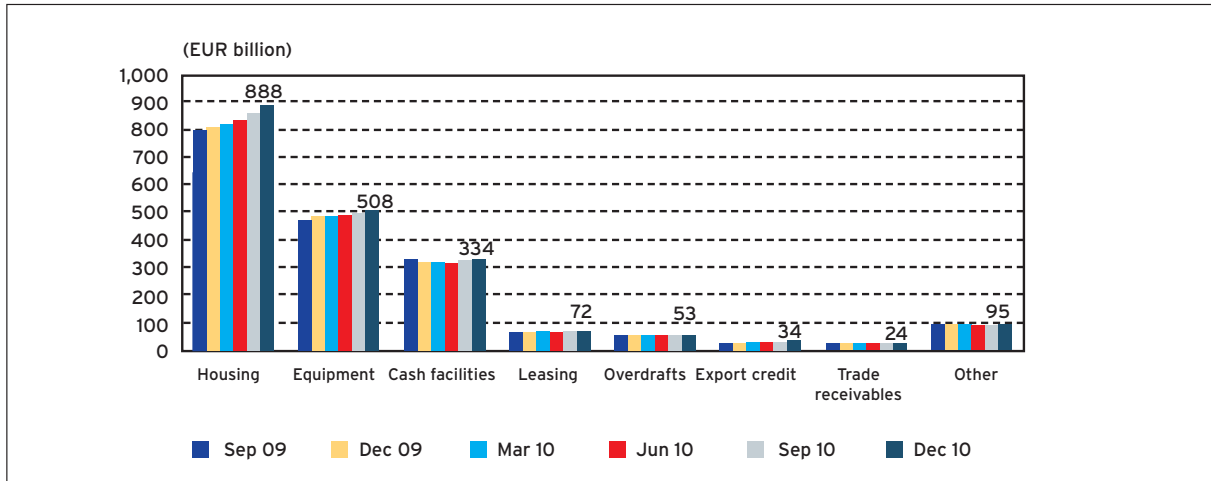
Lending to customers grew quickly in all categories, especially retail customers. Business in housing loans was brisk, supported by the level of interest rates and the determination of retail customers to take advantage of various tax breaks before they were amended.

**Lending to the economy by category of agent  
(Aggregated parent-company data)**



Source: General Secretariat of the ACP

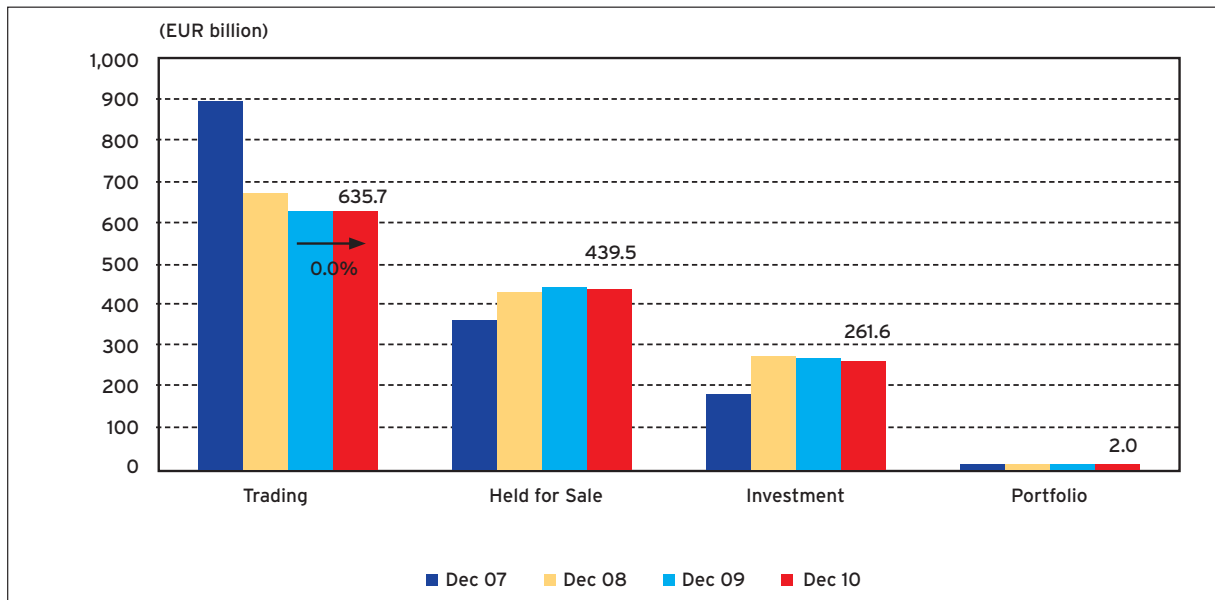
**Lending to the economy by loan type  
(Business in metropolitan France - aggregated parent-company data)**



Source: General Secretariat of the ACP

Overall, securities portfolios were unchanged, reflecting banks' wait-and-see strategy. Securities transactions appeared to rebound, but the increase was solely due to securities received under repurchase agreements, which rose 18%.

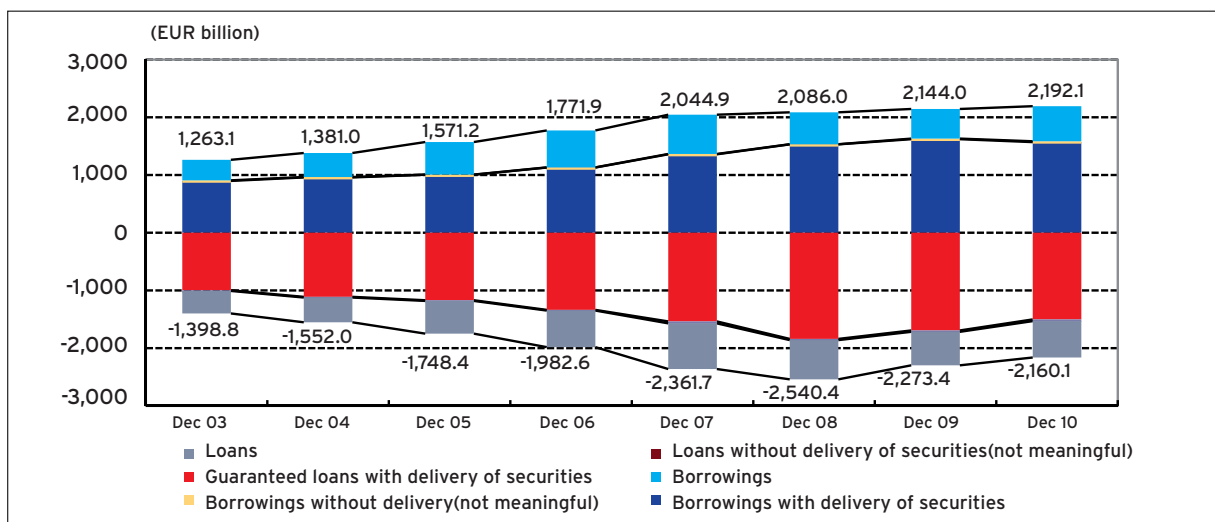
**Credit institutions' securities portfolios**  
(Aggregated parent-company data)



Source: General Secretariat of the ACP

On the assets side, interbank transactions increased solely as a result of repos.

**Interbank transactions**  
(Aggregated parent-company data)



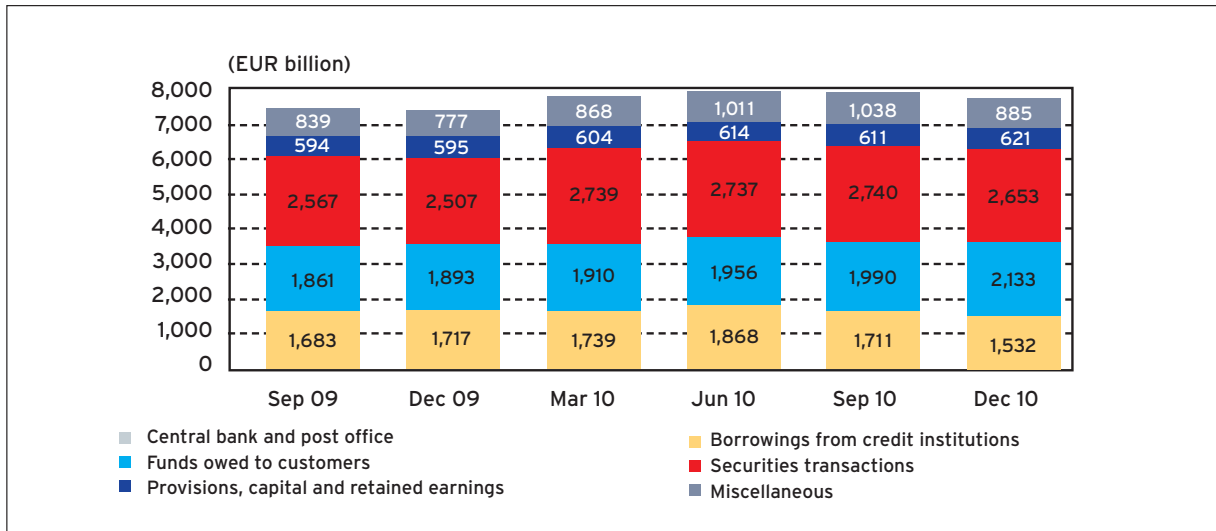
Source: General Secretariat of the ACP

On the liabilities side, interbank transactions contracted, reflecting the effect of measures to refocus on certain types of funding.

## 4.2.2 Liability components

Funds owed to customers now account for over one-quarter of liabilities.

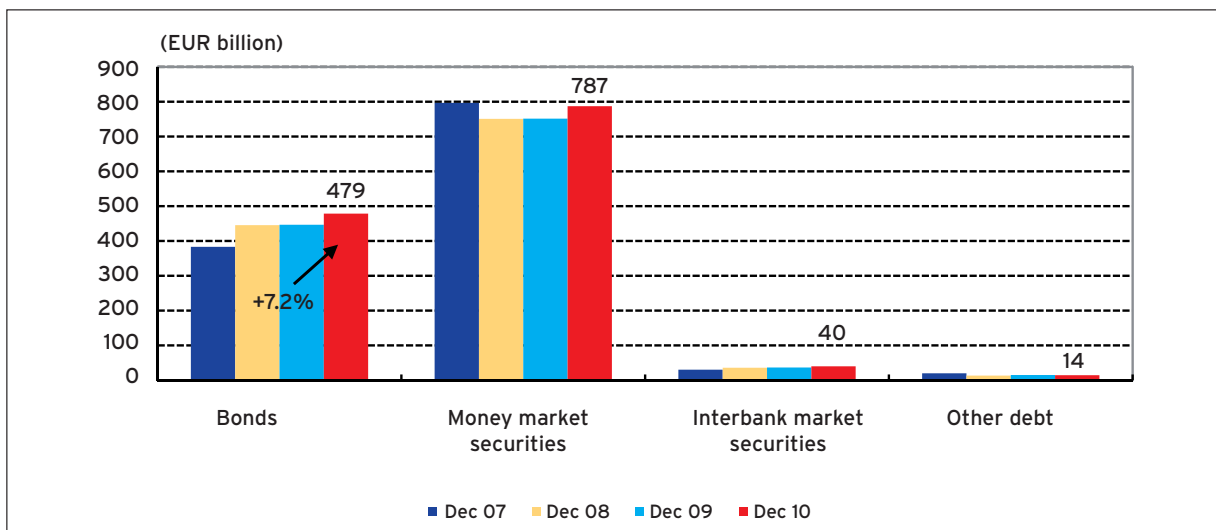
### Liability components (Aggregated parent-company data)



Source: General Secretariat of the ACP

However, securities issuance remained strong, especially in bonds, and in particular in covered bonds.

### Debt evidenced by a certificate (Business in metropolitan France - aggregated parent-company data)

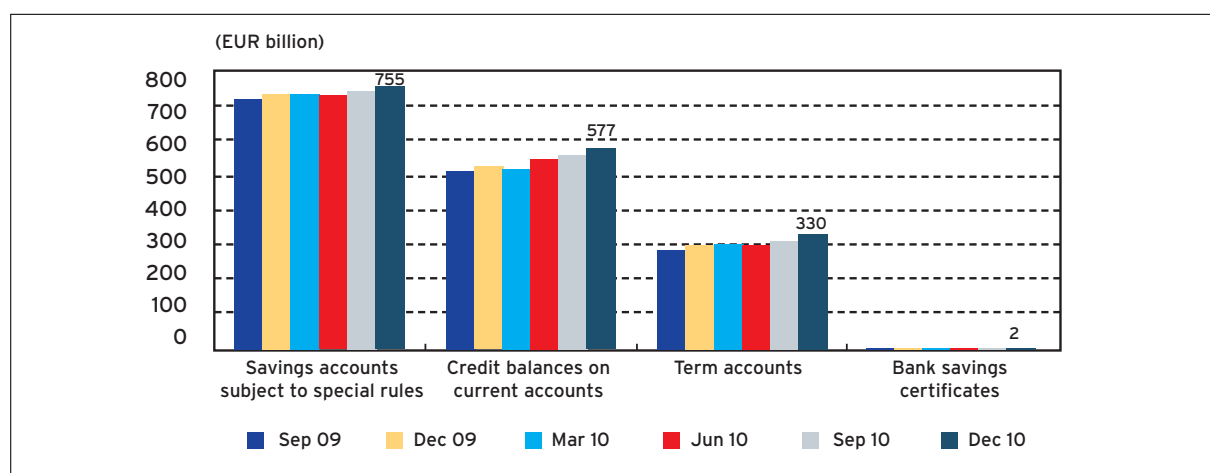


Source: General Secretariat of the ACP

The inflow of new deposits was the most important factor in the increase in liabilities. This growth stemmed from a 47% year-on-year surge in transactions with financial customers and from growth in the total deposits of non-financial customers. Several factors may have contributed to these outcomes:

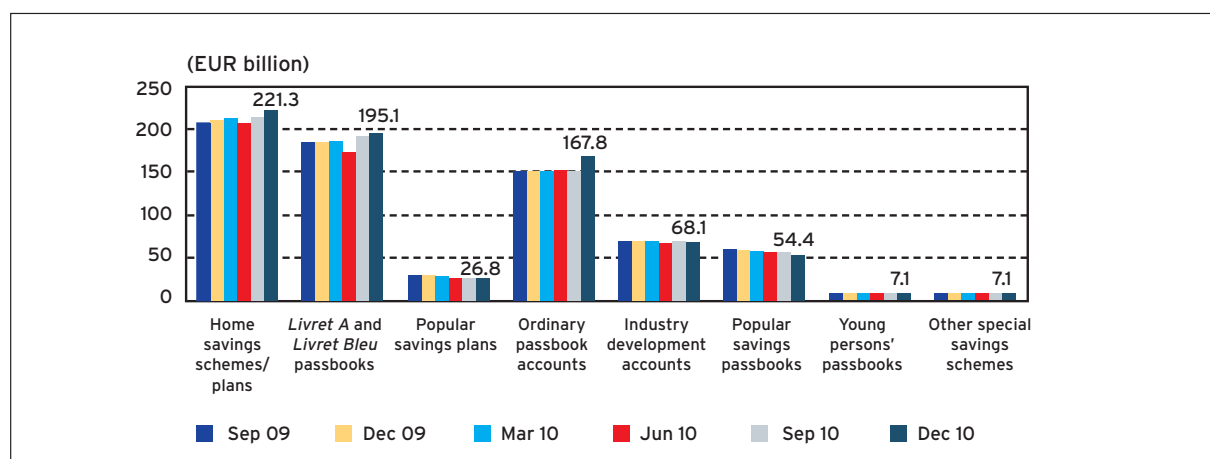
- low returns on money market investments may have prompted customers to keep a larger proportion of their funds in ordinary accounts in credit;
- the appeal of savings accounts subject to special rules, and particularly Livret A accounts, was enhanced by the increase in their return and the security that they offer;
- banks pursued strategies to make term accounts and passbooks more attractive.

### Customer deposits (Aggregated parent-company data)



Source: General Secretariat of the ACP

### Savings accounts subject to special rules (Aggregated parent-company data - business in metropolitan France)



Source: General Secretariat of the ACP

In an uncertain environment, liquidity remains a key issue for banks.



## 5. Risks identified and managed

French banks continued to report sound earnings in a challenging economic environment, relying on careful risk management and a universal banking model based on a diversified array of businesses.

However, banks will have to strengthen risk management further still by pursuing appropriate risk tolerance policies and maintaining sufficient levels of investment in information systems, because they will be obliged to perform detailed exposure analyses and conduct strict, ongoing controls of appropriate risk limits amid difficult economic conditions.

### 5.1 Liquidity

Credit institutions must ready themselves to comply with two liquidity ratios under Basel 3: the Net Stable Funding Ratio (NSFR) and the Liquidity Coverage Ratio (LCR). Effective implementation of the ratios will require changes to French banks' financing strategies. (Implementation is scheduled for 2015 for the LCR and 2018 for the NSFR to accommodate the need for observation phases to verify – and if necessary modify – the ratios' methodological underpinnings.)

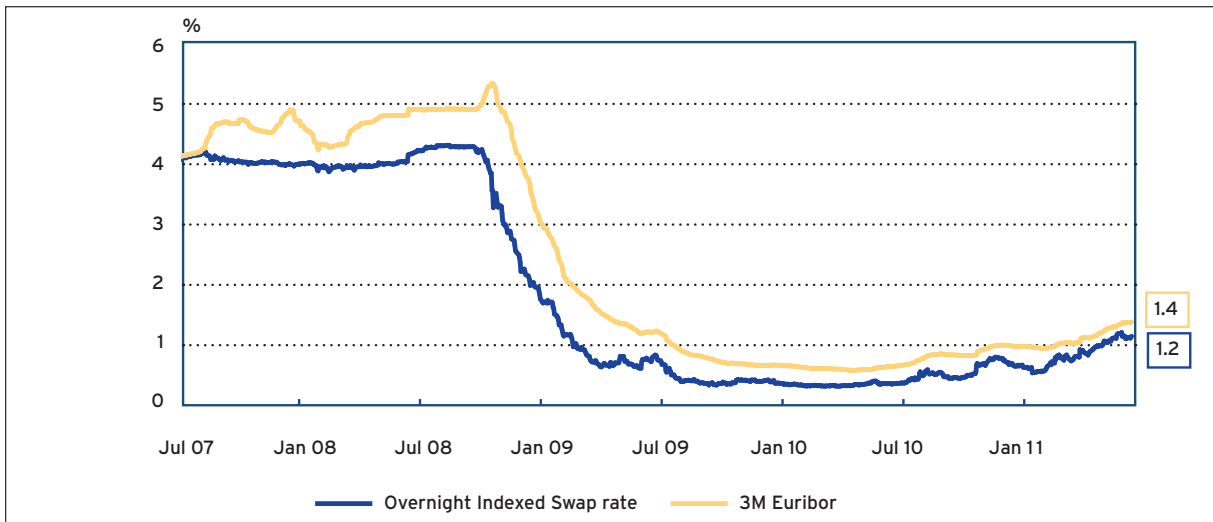
#### BRIEFING

The Liquidity Coverage Ratio (LCR) is a short-term ratio that measures a liquidity situation on a 30-day horizon. The LCR is designed to ensure that the reporting institution can cope with a sudden liquidity shock, such as an unforeseen increase in outgoing payments, by drawing on assets that are considered to be liquid (i.e. that can be converted to cash, including when market liquidity is stressed). The stock of liquid assets (the ratio's numerator), which are subject to a restrictive definition, must equal the amount that the institution would have to finance in a liquidity stress scenario (the denominator).

The Net Stable Funding Ratio (NSFR) is a more structural ratio measuring total funding on a one-year horizon. It is intended to control the maturity mismatching (i.e. provision of long-term financing using short-term resources) inherent to the banking business. Funding that is considered to be stable (numerator) must be at least equal to the required amount of stable funding (denominator).

Banks often have to contend with higher refinancing costs, although these are still down on their peaks of 2008.

### 3-month and overnight rates on the European interbank market



Source: Bloomberg

#### BRIEFING

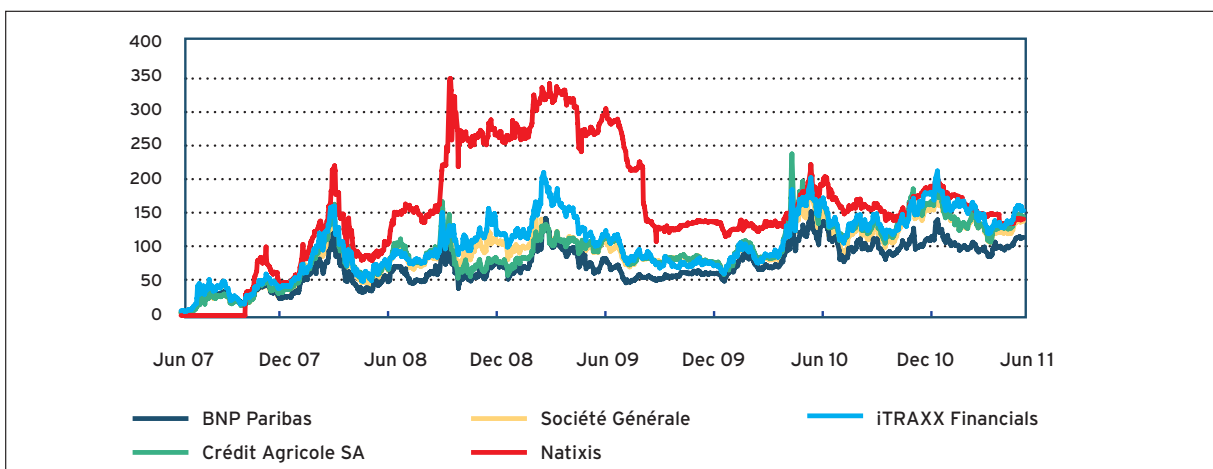
The Overnight Indexed Swap rate (OIS) is the overnight financing rate on the interbank market, whereas the 3-month Euribor is the rate for uncollateralised financing up to three months. The spread between the two rates is commonly used to show a loss of confidence on the interbank market.

In addition, credit default swap (CDS) spreads on French banks have remained at high levels since June 2010 and influence banks' refinancing costs.

#### BRIEFING

Credit Default Swap (CDS): a contract allowing an economic agent to obtain protection against the risk of non-repayment of a loan. The agent pays a third party a regular premium and will receive in exchange a pre-agreed sum if the borrower defaults.

### CDS premiums - senior debt, 5-year contracts Index base 100



Source : Bloomberg

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## 5.2 Sovereign risk

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Market uncertainty over the ability of governments to meet debt repayments exposed banks' balance sheet exposure to sovereigns. However, data published as part of the stress testing exercise conducted under the supervision of the European Banking Authority (EBA) demonstrated that total exposure to sovereigns viewed as sensitive by the markets was sizeable but manageable. Compared with the total portfolios of sensitive assets identified during the 2008 financial crisis, this sovereign exposure is similar in size but of higher quality. Banks are therefore capable of managing it.

## 5.3 Property risk

---

Given the dominant share of housing loans in outstanding loans (44% of credit granted by all banks in 2010 – metropolitan France), the risk of a sharp correction to housing prices is a potential source of vulnerability for the banking system. While lending policies in France do not depend on property values, this metric is still a major component of collateral.

Furthermore, sustained demand for housing loans and the high level of prices are linked to housing supply/demand mismatches but also to the low level of lending rates – another factor that might change.



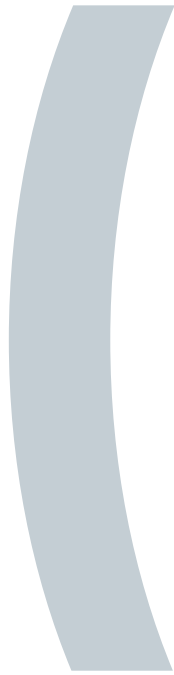
## Annexes

Sound banking system,  
uncertain environment

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## Annexes

Sound banking system,  
uncertain environment

## Annex 1

### Business data

(EUR billion)	2008	2009	2010	2010/2009 change in %
<b>TOTAL ASSETS</b>	<b>7,662</b>	<b>7,508</b>	<b>7,830</b>	<b>4.3</b>
Customer loans	2,288	2,218	2,393	7.9
Securities portfolio	1,387	1,348	1,339	-0.7
o/w trading securities	675	636	636	0.0
Customer deposits	1,785	1,893	2,133	12.7
o/w sight deposits	520	524	579	10.5
o/w savings accounts subject to special rules	646	729	755	3.7
Positions on financial futures (1)	83,034	83,284	91,293	9.6

\*Ces encours notionnels constituent un indicateur du volume d'activité sur ces marchés, sans toutefois refléter les risques encourus.

Source: General Secretariat of the ACP

## Annex 2

### Earnings data

(EUR billion)	2008	2009	2010	2010/2009 change in %
Net banking income	79.2	113.3	106.8	-5.7
Structural expenses	66.8	68.3	68.9	0.9
Gross operating income	12.4	45.1	38.0	-15.7
Net allocations to provisions and loan losses	10.0	14.5	8.9	-38.4
Operating income	-2.4	28.0	28.0	0.1
Ordinary pre-tax income	-4.2	25.5	25.5	0.2
<b>NET INCOME</b>	<b>-3.2</b>	<b>20.3</b>	<b>25.3</b>	<b>24.4</b>

Source: General Secretariat of the ACP

## Annex 3

### Summary of the main ratios relating to business and earnings

%	2008	2009	2010
Average cost of customer funds	3.26	1.95	1.34
Average return on customer loans	5.68	4.65	3.55
Overall banking margin	0.92	1.18	1.03
Cost-to-income ratio	84.4	60.2	64.4
Return on equity	-1.0	6.0	7.1

N.B.: The data are for metropolitan France only. All ratios, except cost-to-income, are calculated on the basis of average capital.

Source: General Secretariat of the ACP

## Annex 4

### Aggregate financial position of credit institutions

(Aggregated parent-company data)

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change 2010/2009	
				Amount	%
<b>ASSETS</b>					
CASH IN HAND, BALANCES WITH CENTRAL BANKS AND POST OFFICE BANKS	121,505	95,788	99,222	3,434	3.6
LOANS TO CREDIT INSTITUTIONS	1,533,282	1,630,723	1,585,159	-45,564	-2.8
. current accounts	233,165	241,428	213,296	-28,133	-11.7
. deposits and loans	1,060,481	1,123,842	1,088,651	-35,192	-3.1
. securities bought under repurchase agreements	2,678	10,234	14,619	4,386	42.9
. other loans	236,958	255,219	268,594	13,375	5.2
CUSTOMER LOANS	2,288,525	2,218,186	2,393,239	175,053	7.9
. loans to non-financial customers	1,992,992	1,968,715	2,075,907	107,192	5.4
. loans to financial customers	178,257	132,302	182,996	50,694	38.3
. securities bought under repurchase agreements	296	216	200	-17	-7.7
. overdrafts	72,396	65,201	81,122	15,921	24.4
. non-performing loans	26,374	36,999	38,594	1,595	4.3
. other credits	18,210	14,752	14,420	-332	-2.3
SECURITIES TRANSACTIONS	2,509,390	2,223,978	2,303,085	79,106	3.6
. securities bought under repurchase agreements	552,559	513,234	607,791	94,557	18.4
. trading securities	674,832	635,725	635,679	-46	0.0
. securities held for sale	432,790	444,536	439,547	-4,989	-1.1
. portfolio securities	2,321	2,324	2,019	-306	-13.1
. investment securities	277,007	265,346	261,628	-3,718	-1.4
. other transactions	569,881	362,813	356,421	-6,392	-1.8
CAPITAL ASSETS	457,490	481,375	495,752	14,377	3.0
. subordinated loans	42,575	44,009	44,742	733	1.7
. shares in affiliated entities	295,211	317,306	331,970	14,664	4.6
. fixed assets	28,484	28,558	29,016	458	1.6
. financial and operating leases	88,731	88,393	87,473	-920	-1.0
. other assets	2,489	3,107	2,550	-557	-17.9
MISCELLANEOUS	752,129	858,047	953,487	95,439	11.1
<b>TOTAL ASSETS</b>	<b>7,662,321</b>	<b>7,508,096</b>	<b>7,829,943</b>	<b>321,846</b>	<b>4.3</b>

Source: General Secretariat of the ACP

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change 2010/2009	
				Amount	%
<b>LIABILITIES</b>					
CENTRAL BANKS AND POST OFFICE BANKS	38,265	18,755	5,915	-12,840	-68.5
BORROWING FROM CREDIT INSTITUTIONS	1,860,451	1,717,180	1,531,701	-185,479	-10.8
. credit balances on current accounts	103,155	100,621	103,098	2,477	2.5
. due to banks	1,498,561	1,320,994	1,126,638	-194,356	-14.7
. securities sold under repurchase agreements	20,743	24,069	29,635	5,566	23.1
. other borrowing	237,992	271,495	272,330	834	0.3
FUNDS OWED TO CUSTOMERS	1,785,351	1,893,415	2,133,499	240,084	12.7
. borrowing from financial customers	244,489	307,359	433,537	126,177	41.1
. securities sold under repurchase agreements	410	1,320	2,889	1,569	118.9
. credit balances on current accounts	520,040	523,500	578,535	55,035	10.5
. savings accounts subject to special rules	645,884	728,557	755,334	26,777	3.7
. credit balances on term accounts	337,719	302,378	332,081	29,703	9.8
. certificates of deposit and savings certificates	1,938	1,886	2,206	319	16.9
. other liabilities	34,872	28,415	28,917	502	1.8
SECURITIES TRANSACTIONS	2,777,493	2,506,655	2,652,559	145,904	5.8
. securities sold under repurchase agreements	679,987	580,278	630,343	50,065	8.6
. debts evidenced by a certificate	1,245,348	1,249,434	1,320,046	70,613	5.7
o/w: . money market securities	750,778	751,386	787,142	35,756	4.8
. bonds	445,435	446,573	478,561	31,988	7.2
. other transactions	852,157	676,944	702,170	25,226	3.7
PROVISIONS, SHAREHOLDERS' EQUITY	577,814	562,691	583,504	20,813	3.7
. grants and public funding	4,322	4,810	6,334	1,524	31.7
. sundry provisions and mutual guarantee deposits	110,060	72,326	83,782	11,456	15.8
. subordinated debt	179,258	176,819	172,140	-4,679	-2.6
. equity capital, reserves and fund for general banking risks	284,173	308,736	321,248	12,512	4.1
RETAINED EARNINGS/LOSSES	35,608	32,145	37,350	5,205	16.2
MISCELLANEOUS	587,340	777,255	885,414	108,159	13.9
<b>TOTAL LIABILITIES</b>	<b>7,662,321</b>	<b>7,508,096</b>	<b>7,829,943</b>	<b>321,846</b>	<b>4.3</b>

Source: General Secretariat of the ACP

## Annex 5

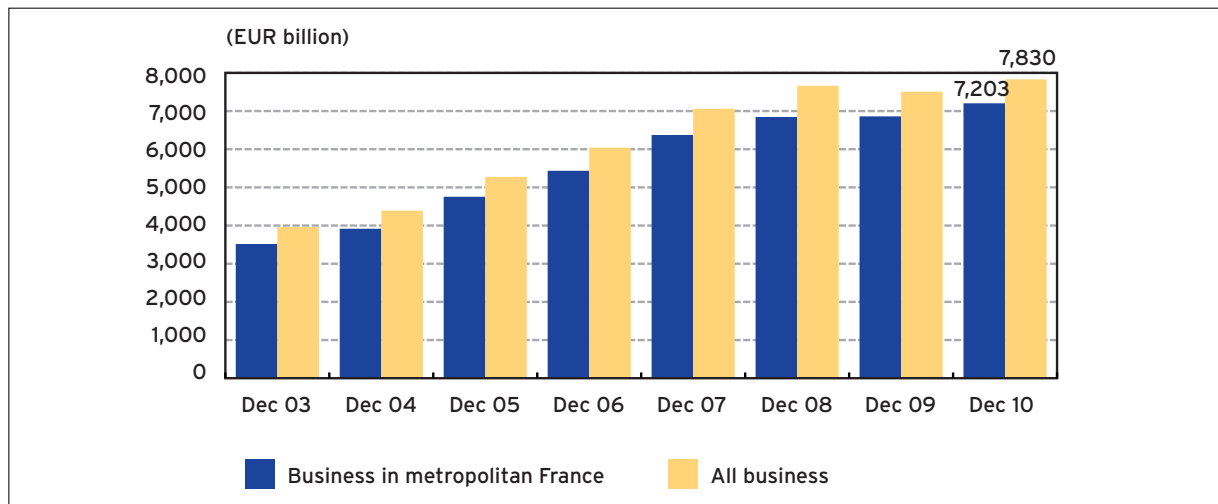
### Off-balance sheet commitments of credit institutions (Aggregated parent-company data)

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change 2010/2009	
				Amount	%
<b>FINANCING COMMITMENTS</b>					
Given:					
- to credit institutions	127,441	158,990	189,471	30,481	19.2
- to customers	757,388	770,089	849,289	79,200	10.3
Received:					
- from credit institutions	332,771	395,838	482,992	87,154	22.0
- from customers	37,123	32,073	56,701	24,628	76.8
<b>GUARANTEE COMMITMENTS</b>					
Given:					
- to credit institutions	373,193	379,253	412,066	32,813	8.7
- to customers	606,924	616,800	663,270	46,470	7.5
Received:					
- from credit institutions	459,036	462,689	471,864	9,175	2.0
- from customers	515,616	531,252	589,213	57,961	10.9
<b>COMMITMENTS ON SECURITIES</b>					
Securities to be received	174,240	190,584	220,269	29,685	15.6
o/w securities sold with a repurchase option	0	0	0	0	-
Securities to be delivered	183,163	192,271	220,414	28,143	14.6
o/w securities bought with a repurchase option	1,330	100	120	20	20.5
<b>CURRENCY TRANSACTIONS</b>					
Currencies to be received	4,399,623	5,094,748	5,844,344	749,596	14.7
Currencies to be delivered	4,408,950	4,539,089	5,852,637	1,313,548	28.9
<b>COMMITMENTS IN RESPECT OF FORWARD FINANCIAL INSTRUMENTS</b>					
o/w:					
Transactions in interest rate instruments	69,328,774	73,172,833	80,214,560	7,041,727	9.6
Transactions in currency instruments	3,154,686	2,404,701	3,087,026	682,325	28.4
Transactions in other instruments	10,550,401	7,706,221	7,991,143	284,922	3.7

Source: General Secretariat of the ACP

## Annex 6

### Change in aggregate financial position



Source: General Secretariat of the ACP

## Annex 7

### Lending to the economy

#### (Non-financial customers - aggregated parent-company data - business in metropolitan France)

(EUR million)

Dec 2010	Residents						Non-residents	Total	Annual % change
	Non-financial corporations	Sole proprietors	Individuals	Insurance companies	General government	Private non-profit entities			
Trade receivables	13,005	125	1	1	1,116	130	9,361	23,739	1.1
Export credits	3,693	5	0	0	21	0	30,685	34,404	29.6
Cash loans	113,805	9,161	128,931	1,762	11,956	376	68,268	334,259	1.6
Equipment loans	265,981	35,636	0	862	157,510	9,779	38,209	507,977	3.5
Housing loans	97,832	81,955	685,642	195	1,962	1,617	19,154	888,357	8.4
Other credits	58,469	1,070	2,509	678	5,803	318	17,358	86,205	0.5
Overdrafts	32,196	1,806	7,402	1,349	2,053	968	6,742	52,516	4.1
Consumer leases and similar operations	59,425	3,033	4,864	98	2,034	768	3,313	73,535	2.8
Subordinated loans	4,119	10	0	3,501	0	2	829	8,461	-6.8
<b>Grand total</b>	<b>648,525</b>	<b>132,801</b>	<b>829,349</b>	<b>8,446</b>	<b>182,455</b>	<b>13,958</b>	<b>193,919</b>	<b>2,009,453</b>	<b>5.4</b>
Relative shares of economic agents (%)	32.3	6.6	41.3	0.4	9.1	0.7	9.7	100.0	
Annual change (%)	0.8	4.1	7.2	-1.2	6.2	8.9	15.2	5.4	

Source: General Secretariat of the ACP

## Annex 8

### Funds owed to customers

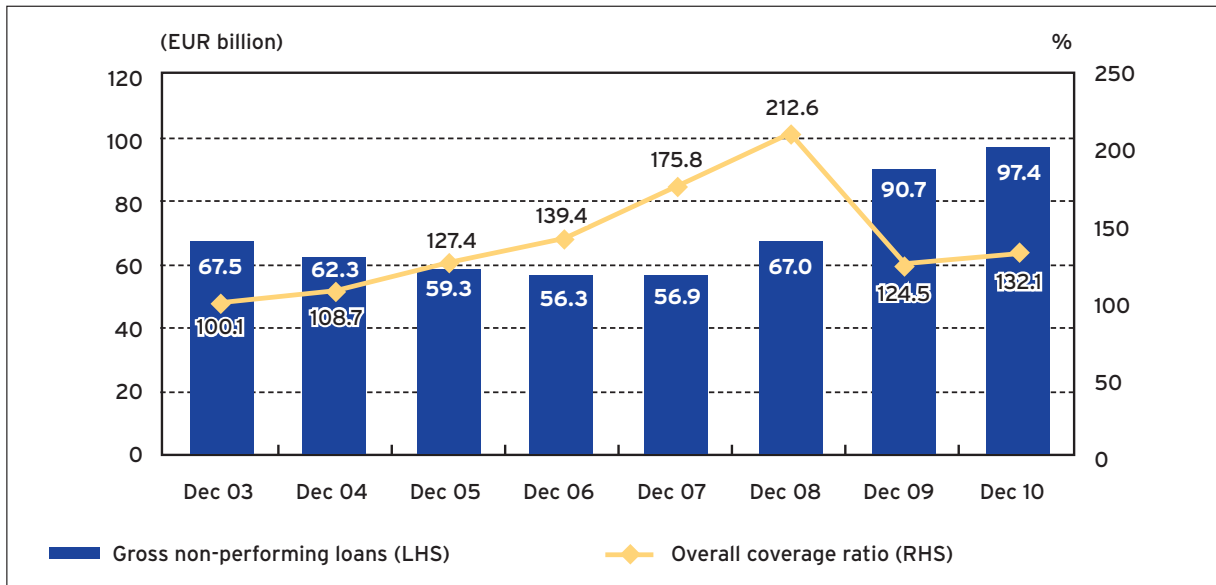
(Aggregated parent-company data - business in metropolitan France)

(EUR million)	Dec 2009				Dec 2010				Annual % change
	Residents	Non residents	Total	% of structure	Residents	Non residents	Total	% of structure	
Borrowing from financial customers	137,417	94,125	231,542	14.1	164,866	175,610	340,476	18.4	47.0
Securities sold under repurchase agreements	35	0	35	0.0	174	0	174	0.0	397.1
Credit balances on current accounts	440,289	35,862	476,151	29.0	479,464	36,361	515,825	27.9	8.3
Factoring accounts	6,560	740	7,300	0.4	7,297	756	8,053	0.4	10.3
Collateral deposits	4,984	4,056	9,040	0.6	4,750	3,350	8,100	0.4	-10.4
Savings accounts subject to special rules	711,082	10,164	721,246	43.9	736,755	11,057	747,812	40.5	3.7
O/w: - ordinary passbooks	146,542	5,872	152,414	9.3	161,082	6,483	167,565	9.1	9.9
- Livret a and livret bleu passbooks	183,429	1,159	184,588	11.2	193,657	1,388	195,045	10.6	5.7
- Young persons' passbooks	7,229	11	7,240	0.4	7,048	10	7,058	0.4	-2.5
- People's savings passbooks	58,291	24	58,315	3.5	54,339	19	54,358	2.9	-6.8
- Sustainable development passbooks	69,132	122	69,254	4.2	67,945	123	68,068	3.7	-1.7
- Home savings schemes/ accounts	210,344	2,558	212,902	13.0	218,277	2,777	221,054	12.0	3.8
- Popular savings schemes	29,000	249	29,249	1.8	26,304	239	26,543	1.4	-9.3
- Other savings accounts subject to special rules	7,095	4	7,099	0.4	7,094	8	7,102	0.4	0.0
Term deposit accounts	136,310	48,910	185,220	11.3	157,332	55,769	213,101	11.5	15.1
Interest bearing notes and savings certificates	1,826	1	1,827	0.1	2,164	1	2,165	0.1	18.5
Other amounts due	4,500	189	4,689	0.3	4,787	230	5,017	0.3	7.0
Accrued interest payable	5,477	403	5,880	0.4	5,656	758	6,414	0.3	9.1
<b>TOTAL</b>	<b>1,448,479</b>	<b>194,450</b>	<b>1,642,929</b>	<b>100.0</b>	<b>1,563,245</b>	<b>283,892</b>	<b>1,847,137</b>	<b>100.0</b>	<b>12.4</b>

Source: General Secretariat of the ACP

## Annex 9

### Overall non-performing loan coverage ratio



N.B.: The overall coverage ratio includes specific and general provisions.

Source: General Secretariat of the ACP

## Annex 10

### Aggregate income statement of credit institutions

(Aggregated parent-company data)

(EUR million)	METROPOLITAN FRANCE ONLY				AGGREGATE ACTIVITY			
	2008	2009	2010	Change 2010/2009 %	2008	2009	2010	Change 2010/2009 %
<b>NET BANK OPERATING INCOME (1)</b>	<b>70,881</b>	<b>94,577</b>	<b>89,066</b>	<b>- 5.8</b>	<b>74,945</b>	<b>109,449</b>	<b>103,123</b>	<b>-5.8</b>
. money market and interbank transactions	-3,084	4,177	3,183	-23.8	-3,841	5,714	3,898	-31.8
. customer transactions	68,294	59,459	61,195	2.9	76,704	66,617	66,947	0.5
. securities transactions (2)	-69,776	21,558	8,943	-58.5	-86,284	26,245	10,750	-59.0
o/w repurchase agreements	-3,725	-847	-1,460	-72.4	-4,776	-1,116	-1,693	-51.7
. leasing transactions	5,067	4,063	3,712	-8.6	5,369	4,349	4,120	-5.3
. off-balance sheet transactions	42,826	-26,228	-13,931	46.9	53,875	-28,550	-13,626	52.3
. financial services	15,572	14,738	14,963	1.5	16,249	15,786	15,924	0.9
. other operating revenue	11,983	16,811	11,001	-34.6	12,873	19,289	15,111	-21.7
<b>NET ANCILLARY AND MISCELLANEOUS INCOME</b>	<b>3,816</b>	<b>3,645</b>	<b>3,616</b>	<b>-0.8</b>	<b>4,218</b>	<b>3,894</b>	<b>3,726</b>	<b>-4.3</b>
<b>NET BANKING INCOME (1)</b>	<b>74,697</b>	<b>98,222</b>	<b>92,681</b>	<b>-5.6</b>	<b>79,163</b>	<b>113,344</b>	<b>106,849</b>	<b>-5.7</b>
<b>OVERHEADS</b>	<b>56,594</b>	<b>58,042</b>	<b>58,542</b>	<b>0.9</b>	<b>62,934</b>	<b>65,034</b>	<b>65,778</b>	<b>1.1</b>
. personnel	30,661	32,706	32,914	0.6	34,451	37,356	37,509	0.4
. other overheads	25,933	25,336	25,628	1.2	28,483	27,678	28,269	2.1
Depreciation and provisions for tangible and intangible fixed assets	3,558	2,935	2,788	-5.0	3,846	3,229	3,074	-4.8
<b>GROSS OPERATING INCOME</b>	<b>14,545</b>	<b>37,245</b>	<b>31,352</b>	<b>-15.8</b>	<b>12,383</b>	<b>45,081</b>	<b>37,996</b>	<b>-15.7</b>
Net allocations to provisions and bad loan write-offs (3)	6,949	11,296	7,664	-32.2	10,035	14,530	8,945	-38.4
Net allocations to provisions for risks and liabilities	2,710	2,178	1,193	-45.2	4,762	2,583	1,050	-59.4
<b>OPERATING INCOME</b>	<b>4,886</b>	<b>23,771</b>	<b>22,495</b>	<b>-5.4</b>	<b>-2,413</b>	<b>27,968</b>	<b>28,001</b>	<b>0.1</b>
Net capital gains on fixed assets	-1,755	-4,166	-2,232	46.4	-1,753	-2,464	-2,454	0.4
<b>ORDINARY PRETAX INCOME</b>	<b>3,131</b>	<b>19,605</b>	<b>20,263</b>	<b>3.4</b>	<b>-4,167</b>	<b>25,504</b>	<b>25,547</b>	<b>0.2</b>
<b>NET INCOME</b>	<b>2,707</b>	<b>15,868</b>	<b>21,247</b>	<b>33.9</b>	<b>-3,185</b>	<b>20,332</b>	<b>25,289</b>	<b>24.4</b>

(1) Excluding interest on non-performing loans.

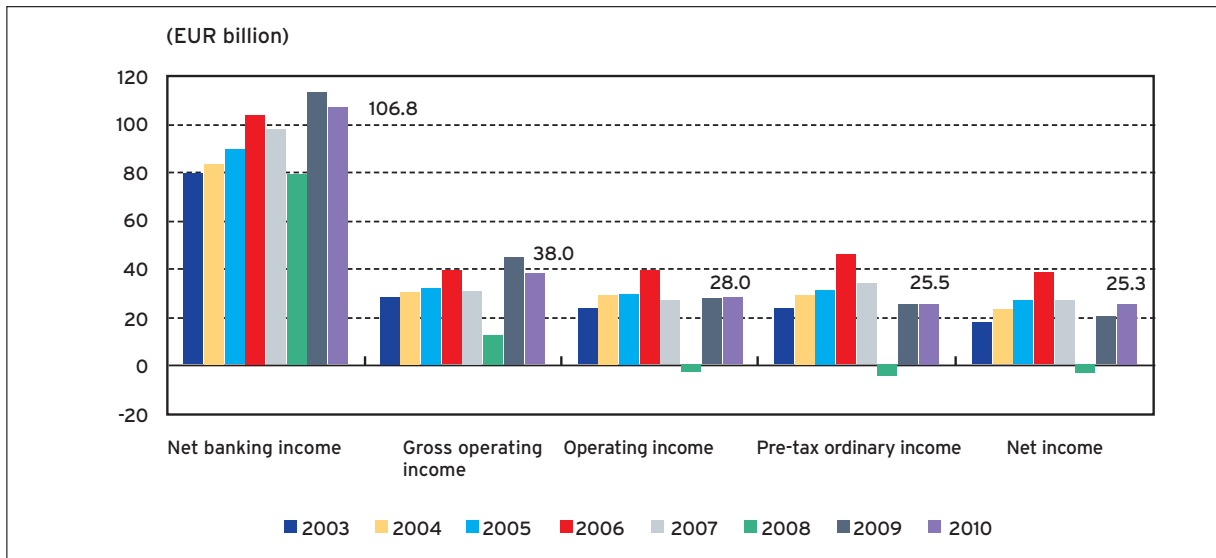
(2) Including allocations to provisions for impairment of securities held for sale and portfolio securities.

(3) Including interest on non-performing loans.

Source: General Secretariat of the ACP

## Annex 11

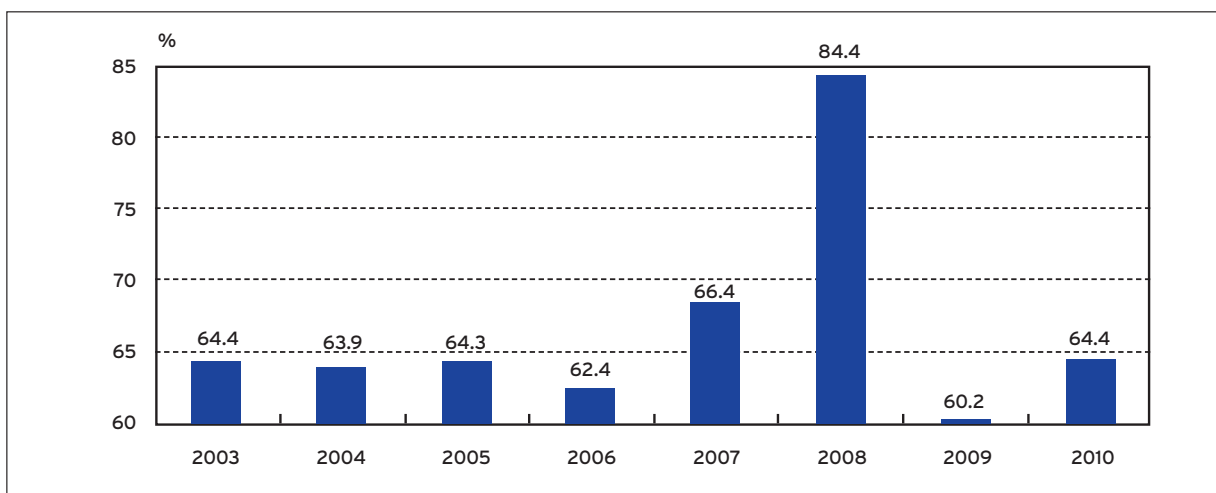
### Intermediate operating totals



Source: General Secretariat of the ACP

## Annex 12

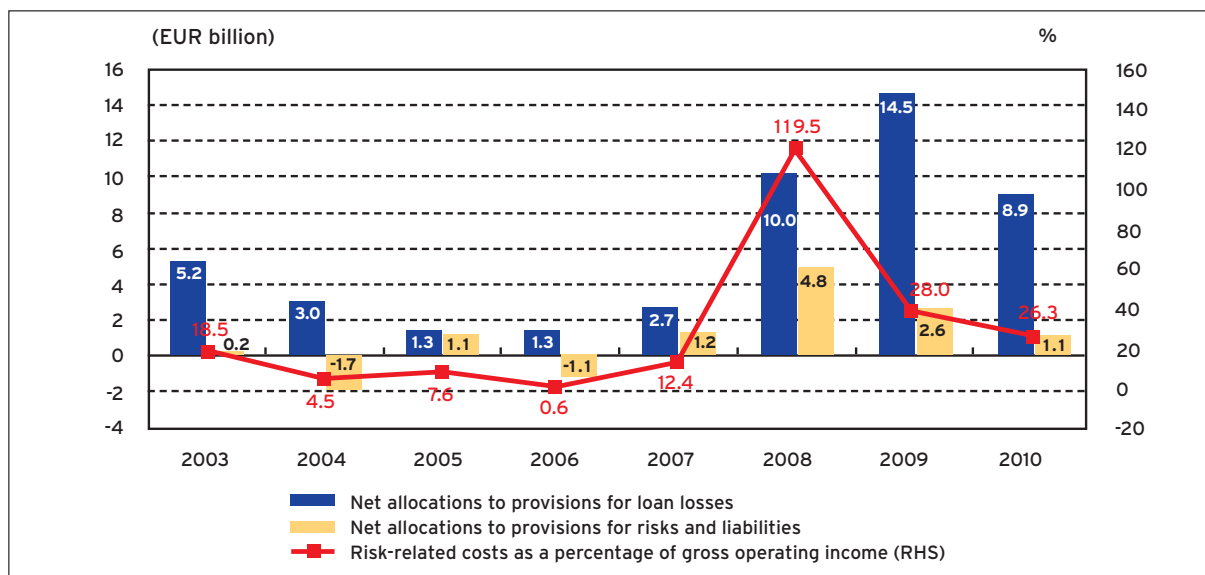
### Cost-to-income ratio



Source: General Secretariat of the ACP

## Annex 13

### Provisions compared to gross operating income



Source: General Secretariat of the ACP

## Annex 14

### Average costs and returns

(%)	2008	2009	2010
<b>1. Customer transactions</b>			
Average cost of borrowing (including money market securities)	3.26	1.95	1.34
Average return on loans	5.68	4.65	3.55
<b>2. Securities transactions</b>			
Debt securities (other than money market securities)	2.62	3.14	1.75
Subordinated debt	5.01	4.63	3.62
Return on securities portfolio	-0.62	5.42	3.15
<b>3. Money market transactions</b>			
Average cost of borrowing	5.28	2.76	1.58
Average return on loans	5.66	3.19	1.68
<b>4. Overall banking margin</b>			
	0.92	1.18	1.03

Source: General Secretariat of the ACP

NB: Data are for metropolitan data

## Annex 15

### Aggregate financial position of investment firms

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change in %
<b>ASSETS</b>				
MONEY MARKET AND INTERBANK MARKET TRANSACTIONS	59,527	50,060	57,596	15.1
CUSTOMER TRANSACTIONS	1,253	400	530	32.3
SECURITIES AND OTHER TRANSACTIONS	424,976	288,498	290,928	0.8
. Trading securities	116,116	103,680	124,808	20.4
. Options bought	181,054	93,460	77,006	-17.6
. Securities held for sale and portfolio securities	25,652	19,289	19,904	3.2
. investment securities	21	21	0	-
. Securities bought under repurchase agreements	10,285	7,259	7,446	2.6
. Trading and settlement accounts	4,811	4,342	4,271	-1.6
. Sundry debtors	21,790	13,663	8,626	-36.9
. Accruals and deferred income	62,593	44,702	47,401	6.0
. Non-performing assets and accruals	2,654	2,083	1,464	-29.7
CAPITAL ASSETS	575	580	609	4.9
. Subordinated loans	7	7	7	7.8
. Shares in affiliated entities	269	274	279	2.1
. Net fixed assets	295	295	318	7.9
. Non-performing assets and accruals	3	5	4	-24.8
SHAREHOLDERS AND PARTNERS	76	3	1	-72.8
<b>TOTAL ASSETS</b>	<b>486,407</b>	<b>339,542</b>	<b>349,664</b>	<b>3.0</b>
<b>LIABILITIES</b>				
MONEY MARKET AND INTERBANK MARKET TRANSACTIONS	109,101	83,549	103,850	24.3
CREDIT BALANCES ON CUSTOMER ACCOUNTS	1,166	1,913	1,458	-23.8
SECURITIES AND OTHER TRANSACTIONS	366,261	243,592	232,032	-4.7
. Securities transactions	33,041	33,195	28,877	-13.0
. Options sold	228,810	124,098	111,640	-10.0
. Debts evidenced by a certificate	15,156	14,902	17,979	20.7
o/w: . money market securities	10,339	12,279	16,113	31.2
. bonds	4,811	2,621	1,863	-28.9
. Trading and settlement accounts	6,758	5,443	3,999	-26.5
. Securities sold under repurchase agreements	30,536	31,517	28,817	-8.6
. Sundry creditors	14,908	4,240	4,492	5.9
. Accruals and deferred expenses	36,815	30,086	36,117	20.0
. Accrued interest payable	239	111	110	-0.7
PROVISIONS, SHAREHOLDERS' EQUITY	9,533	9,800	11,149	13.8
. Subordinated debt	311	295	265	-10.3
. Provisions	7,529	7,683	9,344	21.6
. Premiums related to capital stock and reserves	607	605	526	-13.1
. Capital	1,085	1,216	1,014	-16.6
RETAINED EARNINGS/LOSSES(+/-)	519	244	606	148.7
EXCESS OF INCOME/LOSS OVER CHARGES (+/-)	-174	443	568	28.0
<b>TOTAL LIABILITIES</b>	<b>486,407</b>	<b>339,542</b>	<b>349,664</b>	<b>3.0</b>

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change in %
<b>OFF-BALANCE SHEET</b>				
<b>FINANCING COMMITMENTS</b>				
Given	4,671	1,636	2,462	50.5
Received	11,789	13,444	14,789	10.0
<b>GUARANTEE COMMITMENTS</b>				
Given	4,697	4,274	2,146	-49.8
Received	6,262	6,385	5,733	-10.2
<b>COMMITMENTS ON SECURITIES</b>				
Securities to be received	33,374	5,383	4,251	-21.0
Securities to be delivered	4,114	5,153	4,931	-4.3
<b>CURRENCY TRANSACTIONS</b>				
Currencies to be received	15,055	18,211	44,370	143.6
Currencies to be delivered	8,377	13,773	31,794	130.8
<b>COMMITMENTS IN RESPECT OF FORWARD FINANCIAL INSTRUMENTS</b>	4,163,298	2,629,480	2,692,660	2.4
<b>OTHER OFF-BALANCE SHEET COMMITMENTS</b>	10,505	10,455	12,011	14.9

Source: General Secretariat of the ACP

## Annex 16

### Aggregate income statement of investment firms

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change in %
<b>MONEY MARKET AND INTERBANK TRANSACTIONS</b>	<b>1,570.6</b>	<b>-367.2</b>	<b>360.0</b>	<b>-</b>
. interest expense	5,549.3	3,824.8	1,663.5	-56.5
. interest revenue	7,119.9	3,457.7	2,023.5	-41.5
<b>SECURITIES TRANSACTIONS (PROPRIETY TRADING)</b>	<b>-74,876.9</b>	<b>-9,974.4</b>	<b>-245.3</b>	<b>97.5</b>
. expenses	77,442.6	16,017.4	4,003.7	-75.0
o/w repurchase agreements	1,551.0	234.1	144.3	-38.4
o/w bond interest	31.5	12.2	14.6	20.0
. revenues	2,565.7	6,043.0	3,758.4	-37.8
o/w repurchase agreements	642.2	116.0	50.1	-56.8
<b>TRANSACTIONS in FORWARD FINANCIAL INSTRUMENTS (PROPRIETY TRADING)</b>	<b>76,537.8</b>	<b>12,429.0</b>	<b>1,840.3</b>	<b>-85.2</b>
. expenses	875,549.8	613,630.3	444,775.8	-27.5
. revenues	952,087.3	626,059.2	446,616.1	-28.7
<b>FINANCIAL SERVICES/EXPENSES</b>	<b>2,043.4</b>	<b>1,000.7</b>	<b>1,036.7</b>	<b>3.6</b>
. interbank transactions	11.4	15.6	5.2	-66.6
. customer transactions	13.2	12.7	8.4	-33.5
. securities transactions	546.2	389.5	389.4	0
. foreign exchange transactions	636.6	0.9	0.0	-98.9
. commitments on securities	0.0	0.0	0.0	-
. forward financial instrument transactions	491.3	297.8	276.4	-7.2
. provision of financial services	344.7	284.2	357.3	25.8
<b>FINANCIAL SERVICES/INCOME</b>	<b>1,828.8</b>	<b>1,534.8</b>	<b>1,638.7</b>	<b>6.8</b>
. interbank transactions	15.4	11.7	12.6	8.1
. customer transactions	15.5	16.4	14.4	-11.8
. securities transactions	259.0	188.5	123.5	-34.5
. foreign exchange transactions	1.9	2.1	1.8	-14.6
. commitments on securities	4.2	5.3	2.9	-45.4
. forward financial instrument transactions	189.2	106.8	95.4	-10.7
. provision of financial services	1,343.7	1,204.3	1,388.1	15.3
<b>FOREIGN EXCHANGE TRANSACTIONS</b>	<b>-682.9</b>	<b>179.2</b>	<b>-66.8</b>	<b>-</b>
. expenses (losses)	1,904.0	2,563.2	1,292.5	-49.6
. income (gains)	1,221.1	2,742.3	1,225.8	-55.3
<b>INCOME FROM EQUITY INTERESTS AND SUBORDINATED DEBT</b>	<b>93.5</b>	<b>79.3</b>	<b>115.5</b>	<b>45.8</b>
EXPENSES ON SUBORDINATED LOANS	15.3	8.1	6.3	-22.0
OTHER BANK OPERATING INCOME	110.1	152.2	58.9	-61.3
OTHER BANK OPERATING EXPENSES	252.5	95.7	88.3	-7.8
NET ANCILLARY AND MISCELLANEOUS INCOME	215.2	-45.8	62.5	-
<b>NET BANKING INCOME</b>	<b>2,485.1</b>	<b>2,882.8</b>	<b>2,632.5</b>	<b>-8.7</b>

(EUR million)	Dec 2008	Dec 2009	Dec 2010	Change in %
<b>OVERHEADS</b>	1,812.0	1,893.0	1,868.3	-1.3
. personnel	1,054.5	1,078.5	1,003.6	-6.9
. taxes	66.7	63.7	45.9	-28.0
. external services	971.1	1,008.4	1,014.2	0.6
. other operating expenses (rebilled expenses)	-280.3	-257.5	-195.4	24.1
Depreciation and provisions for tangible and intangible fixed assets	72.0	80.9	83.2	2.9
<b>GROSS OPERATING INCOME</b>	<b>600.9</b>	<b>908.9</b>	<b>681.0</b>	<b>-25.1</b>
Net allocations to provisions and loan losses	420.9	45.5	30.5	-32.9
Net allocations to provisions for risks and liabilities	2.1	78.7	-100.4	-
<b>OPERATING INCOME</b>	<b>177.8</b>	<b>784.8</b>	<b>750.8</b>	<b>-4.3</b>
Net capital gains on fixed assets	-10.9	12.6	25.6	102.5
<b>ORDINARY PRETAX INCOME</b>	<b>167.0</b>	<b>797.4</b>	<b>776.4</b>	<b>-2.6</b>
EXCEPTIONAL INCOME	14.8	5.2	5.2	0.4
EXCEPTIONAL EXPENSES	116.6	13.6	7.6	-44.0
<b>NET ALLOCATION TO RESERVE FOR GENERAL BANKING RISKS</b>	<b>-73.0</b>	<b>5.2</b>	<b>2.8</b>	<b>-47.0</b>
. Allocations to reserve for general banking risks	0.0	5.2	2.8	-47.0
. Writebacks from reserve for general banking risks	73.0	0.0	0.0	-
<b>NET ALLOCATIONS TO REGULATORY PROVISIONS</b>	<b>0.2</b>	<b>0.2</b>	<b>0.3</b>	<b>88.9</b>
CORPORATE INCOME TAX	305.2	339.5	156.2	-54.0
<b>NET INCOME</b>	<b>-167.4</b>	<b>443.9</b>	<b>616.6</b>	<b>38.9</b>

Source: General Secretariat of the ACP



## Contents

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54	1. Continued concentration in the insurance market
55	2. Use of the European passport by insurance entities
59	3. Broadly positive financial data in 2010
65	4. Areas for attention

## Scope of the study

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The figures presented in this section are taken from data that insurance entities under the prudential supervision of the Autorité de contrôle prudentiel (ACP) are required to file annually. The study does not include the activity of European insurance companies that have been conducting business in France since 1995 under the freedom of establishment or the freedom to provide services. These companies are subject to the supervisory authorities of their home countries under the European passport. However, such companies account for less than 2% of the activity in France.

# **A robust insurance sector**

# 1. Continued concentration in the insurance market

Concentration in the insurance market, which started in the mid-1990s, continued in 2010. The total number of authorised insurance entities fell from 1,268 in 2009 to 1,129 in 2010. The decline in numbers primarily concerned mutual insurers governed by the Mutual Insurance Code.

## BRIEFING

Insurance is regulated by a set of European directives. Insurance entities in France are subject to three separate sets of regulations: the Insurance Code, the Mutual Insurance Code and the Social Security Code. The three codes are similar with regard to prudential regulations; and a single supervisory authority, the ACP, is responsible for enforcing their provisions.

In 2010 around 140 insurance entities<sup>5</sup>, most of them mutual insurers, disappeared as a result of the recent wave of concentration in the sector. This movement stems mainly from competition between insurers and the increasing complexity of supplementary health insurance, which has prompted many insurers to adjust their strategies and seek critical mass for their long-term development.

## Insurance entities

Number of insurance entities	At 31/12/2009	At 31/12/2010
Life insurers and composite insurers	103	102
Non-life insurers	244	235
<b>Total, insurers</b>	<b>347</b>	<b>337</b>
Reinsurers	21	20
<b>Insurance Code</b>	<b>368</b>	<b>357</b>
Provident institutions	56	53
<b>Social Security Code</b>	<b>56</b>	<b>53</b>
Mutual Insurers Book II	844	719
o/w substitute mutual insurers	-	237
<b>Mutual Insurance Code</b>	<b>844</b>	<b>719</b>
<b>Total authorised entities and entities not requiring authorisation</b>	<b>1,268</b>	<b>1,129</b>

Source: General Secretariat of the ACP

5. The 2009 statistics presented here may differ from those published previously for the same period by the Comité des entreprises d'assurance (CEA) and the Autorité de contrôle des assurances et des mutuelles (ACAM). This is because they take account of the changes made when the ACP was created in terms of responsibility for approving insurance entities, particularly mutual insurers, and exclude entities that are still supervised but that are no longer authorised to issue policies.

## 2. Use of the European passport by insurance entities

### 2.1 Access to the French market

#### Freedom of establishment

The number of EU companies authorised to do business in France under the freedom of establishment did not change markedly between 31 December 2005 and 31 December 2010. There was however a slight increase between the end of 2005 (105 branches) and the end of 2008 (110), then a steep decline from that date onwards (95 at 31 December 2010).

Non-life insurers dominate throughout the period, accounting for 86 branches at end-2005 and 77 at end-2010. The European countries with the greatest representation on French territory are the United Kingdom, Germany, Belgium and Ireland with, respectively, 38, 14, 9 and 8 branches established in France. Many Member States from Eastern Europe have no branches in France.

#### Branches established in France by EEA insurance companies at 31 December 2010

Country	Branches established in France					
	Notifications from insurers authorised in another EEA country					
	2005	2006	2007	2008	2009	2010
Germany	17	18	17	16	15	14
Belgium	12	12	12	12	10	9
Denmark	1	1	1	0	0	0
Spain	4	4	4	4	4	3
Finland	1	1	1	1	1	1
Greece	1	1	1	1	1	0
Ireland	7	5	5	7	8	8
Italy	4	5	5	5	4	4
Luxembourg	6	7	7	7	7	6
Norway	1	1	1	1	1	1
Netherlands	5	6	7	7	7	6
Portugal	3	3	3	3	3	3
United Kingdom	41	39	41	44	41	38
Sweden	2	2	2	2	2	2
<b>TOTAL</b>	<b>105</b>	<b>105</b>	<b>107</b>	<b>110</b>	<b>104</b>	<b>95</b>

Source: General Secretariat of the ACP

## Freedom to provide services

Freedom to provide services is the other way of using the EEA passport to do business in another EEA country without having a permanent establishment there. In contrast with notifications under the freedom of establishment, passporting requests under the freedom to provide services have risen steadily and significantly since 2005, climbing from 827 notifications to 1,046 in 2010. The United Kingdom is the source of around one-quarter of these notifications, Ireland is responsible for a further 13%, while other countries are less represented.

### Notifications under the freedom to provide services in France by EEA insurers and branches of insurers at 31 December 2010

Country	Free provision of services in France					
	Notifications from insurers authorised in another EEA country and from branches of insurers authorised to do business in the EEA under the freedom to provide services					
	2005	2006	2007	2008	2009	2010
Germany	76	78	76	78	84	90
Austria	18	22	24	24	27	27
Belgium	50	51	53	56	56	59
Bulgaria	0	0	1	2	2	4
Cyprus	0	0	0	0	0	0
Denmark	17	19	20	23	23	25
Spain	31	31	32	38	44	48
Estonia	2	2	3	3	4	5
Finland	11	11	11	11	13	15
Gibraltar	9	10	14	16	18	21
Greece	4	3	3	4	4	5
Hungary	5	8	9	10	10	13
Ireland	117	123	127	133	133	135
Iceland	2	3	3	3	3	2
Italy	53	55	54	57	59	60
Latvia	1	1	1	4	4	4
Liechtenstein	15	19	21	24	25	22
Lithuania	2	3	4	5	4	3
Luxembourg	62	63	64	68	66	65
Malta	1	3	6	11	17	20
Norway	13	13	15	16	19	20
Netherlands	60	62	69	70	67	66
Poland	3	8	9	10	11	12
Portugal	12	13	15	15	16	17
Czech Republic	6	6	8	10	9	10
Romania	0	0	1	1	1	1
United Kingdom	225	231	236	224	227	247
Slovakia	1	1	1	2	3	4
Slovenia	2	3	4	5	4	4
Sweden	29	32	36	38	39	42
<b>TOTAL</b>	<b>827</b>	<b>874</b>	<b>920</b>	<b>961</b>	<b>992</b>	<b>1,046</b>

Source: General Secretariat of the ACP

## 2.2 Passporting by French companies

### Freedom of establishment

French insurers had opened 109 branches in EEA countries at 31 December 2010. As with the French branches of EEA insurers, non-life insurance is the main business of these branches. The main countries targeted by French insurers are Italy (16 branches), Spain (15 branches) and Germany (11 branches). No French insurer has opened branches in Cyprus, Estonia, Iceland, Lithuania, Malta or Slovenia. Some branches in EEA countries also do business elsewhere in the European Union under the freedom to provide services.

### Branches established in the EEA by French insurers at 31 December 2010

Country	Branches established in the EEA	
	Notifications from insurers authorised in France	
	2010	
Germany		11
Austria		4
Belgium		9
Bulgaria		5
Denmark		1
Spain		15
Finland		2
Greece		3
Hungary		3
Ireland		2
Italy		16
Latvia		1
Liechtenstein		1
Luxembourg		4
Norway		1
Netherlands		4
Poland		5
Portugal		8
Czech Republic		2
Romania		3
United Kingdom		7
Slovakia		1
Sweden		1
<b>TOTAL</b>		<b>109</b>

Source: General Secretariat of the ACP

## Freedom to provide services

At 31 December 2010, French insurers had made 1,743 notifications under the freedom to provide services in other EEA countries. The countries most favoured by French institutions are, in order, Belgium (111 notifications), Luxembourg and Germany (92 notifications each), Italy and Spain (84 notifications each).

### Notifications under the freedom to provide services in the EEA by French insurers and branches of French insurers at 31 December 2010

Country	Free provision of services in the EEA
	Notifications from insurers authorised in France and from branches of French insurers based in the EEA
	2010
Germany	92
Austria	66
Belgium	111
Bulgaria	43
Cyprus	45
Denmark	63
Spain	84
Estonia	40
Finland	58
Gibraltar	1
Greece	64
Hungary	54
Ireland	68
Iceland	34
Italy	84
Latvia	45
Liechtenstein	29
Lithuania	41
Luxembourg	92
Malta	47
Norway	46
Netherlands	68
Poland	57
Portugal	76
Czech Republic	54
Romania	49
United Kingdom	74
Slovakia	52
Slovenia	47
Sweden	59
<b>TOTAL</b>	<b>1,743</b>

Source: General Secretariat of the ACP



## 3. Broadly positive financial data in 2010

### 3.1 Further growth in total assets

At end-2010, the aggregate total assets of all insurance and reinsurance entities under ACP supervision stood at EUR 1,953 billion at book value, corresponding to EUR 2,023 billion at market value, i.e. including unrealised gains. The book value of total insurance assets continued to grow in 2010 compared with the previous year, with a 7.2% increase to EUR 132 billion.

#### Aggregate summary balance sheet

(EUR billion)

Assets	2008	2009	2010
Reinsurers	73.7	77.6	83.0
Investments (excl. unit-linked)	1,331.3	1,421.1	1,530.8
Unit-linked investments	183.4	209.1	222.5
Other assets	114.7	113.9	117.1
<b>Total assets</b>	<b>1,703.1</b>	<b>1,821.7</b>	<b>1,953.4</b>
Liabilities			
Equity	130.1	135.3	141.7
Provisions (excl. unit-linked)	1,244.9	1,337.8	1,439.5
Unit-linked provisions	184.5	210.6	223.8
Other liabilities	143.6	138.0	148.4
<b>Total liabilities</b>	<b>1,703.1</b>	<b>1,821.7</b>	<b>1,953.4</b>
Unrealised gains	5.6	79.2	69.5
<b>Total assets at market value</b>	<b>1,708.7</b>	<b>1,900.9</b>	<b>2,022.9</b>

Source: General Secretariat of the ACP

This overall movement conceals contrasting trends in different balance sheet components. Unit-linked policies, where the policyholder bears the risk of a loss of asset value, were up 6.4%, or slightly less than total assets, which rose 7.2%. On the other side of the balance sheet, equity increased by 4.8% whereas provisions grew by more than 7.6%.

## BRIEFING

The “provisions” item in the insurance sector represents insurers’ commitments to policyholders. It provides an assessment of the future cost of the claims and benefits to be paid to policyholders. For the purposes of analysis, the balance sheet is often expressed as a percentage of this estimated item, as shown below.

### Summary balance sheet as a percentage of provisions

%

Assets	2008	2009	2010
Reinsurers	5.9	5.8	5.8
Investments(excl. unit-linked)	106.9	106.2	106.3
Unit-linked investments	14.7	15.6	15.5
Other assets	9.2	8.5	8.1
<b>Total assets</b>	<b>136.8</b>	<b>136.2</b>	<b>135.7</b>
Liabilities			
Equity	10.5	10.1	9.8
Provisions(excl. unit-linked)	100.0	100.0	100.0
Unit-linked provisions	14.8	15.7	15.5
Other liabilities	11.5	10.3	10.3
<b>Total liabilities</b>	<b>136.8</b>	<b>136.2</b>	<b>135.7</b>
Unrealised gains	0.4	5.9	4.8
Total assets at market value	137.3	142.1	140.5

Source: General Secretariat of the ACP

The structure of the balance sheet, expressed as a proportion of provisions in euros, shows no significant change from the previous year.

## 3.2 Shares of different categories of insurers in the aggregate balance sheet of the insurance sector

## BRIEFING

A single set of European Insurance Directives governs the insurance entities under ACP supervision, but these entities have different business profiles that stem from their history and legal structure, as well as from different insurance specialisations.

### Analysis by category of insurers’ shares of the main balance sheet components of the insurance sector

%

Share of balance sheet component	Life insurers and composite insurers	Provident institutions	Mutual insurers (Mutual Insurance Code)	Non-life insurers	Reinsurers
Equity	40.2	8.9	11.8	31.4	7.6
Provisions(excl. unit-linked)	83.2	2.3	2.7	9.2	2.6
Unit-linked provisions	99.9	0.0	0.1	0.0	0.0
Total assets	80.9	2.5	3.1	10.6	2.8
Unrealised gains (losses)	40.3	2.7	6.3	36.6	14.0

Source: General Secretariat of the ACP

- Owing to their commitments under savings policies, life and composite insurers hold a large share of the assets in the sector. As at end-2010, they recorded unrealised gains overall, thus making a positive contribution to the differential between the book value and the market value of assets. In contrast, life and composite insurers' share of sector equity is 40.2%, which, though significant, is smaller than their share of total assets (80.9%), as life insurance requires less capital than other, riskier, lines.
- Under the specialisation principle, non-life insurers do not cover risks linked to the human lifespan; they cover only personal risks, such as incapacity, disability and health. Furthermore, non-life insurers are the only insurers authorised to cover third-party liability and most property and casualty risks. In 2010, their equity accounted for 31.4% of all equity in the sector.
- Provident institutions operating in the field of employee insurance schemes offer both long-term coverage, such as retirement, disability and incapacity benefits, which are capital consuming, and short-term coverage, such as group health insurance.
- Many of the mutual insurers governed by the Mutual Insurance Code offer individual health coverage. Rapid settlement of claims means that they are not required to hold substantial investments. By contrast, some mutual insurers specialising in life insurance hold large volumes of assets.
- Reinsurers are allowed to accept all types of risks from insurers. Their balance sheets therefore combine the whole spectrum of risks covered by the insurance sector.

#### THE FRENCH SUPPLEMENTARY HEALTH INSURANCE MARKET

In France, three categories of insurance entities are entitled to offer supplementary health insurance (i.e. supplementing mandatory sickness insurance under the social security system): provident institutions, mutual health insurers and insurers.

At 31 December 2010, the ACP recorded 574 entities offering supplementary health insurance: 106 insurers, 29 provident institutions and 439 mutual insurers. The share of health-related business varies considerably from category to category: mutual insurers generate over 89% of total turnover from this segment of their business, compared with 48% for provident institutions and just 14% for non-life insurers and 6% among life and composite insurers.

In 2010, the net income of entities providing supplementary health insurance, expressed as a percentage of premiums, came to 2.3% for mutual insurers, 2.7% for life and composite insurers, 3.9% for non-life insurers and 4% for provident institutions. Furthermore, the loss ratio and combined ratio (claims and management expenses/contributions) are high, reflecting the fierce competition and thin margins that characterise the business.

While the financial position of entities providing supplementary health insurance deteriorated slightly relative to the previous year, it nevertheless remained solid. As at end-2010, the solvency margin coverage ratio was more than 112% for life and composite insurance companies, 346% for non-life insurers, 386% for mutual insurers and 433% for provident institutions. These ratios should be used with caution, however, since the current solvency margin requirement does not include insurance and investment risks, in contrast with the forthcoming Solvency 2 regime.

### 3.3 Coverage ratios for prudential requirements above the regulatory minimum but down in some cases

At end-2010, the average coverage ratio for regulated commitments in the insurance sector as a whole was between 104% and 127% depending on the category of insurers. Overall, insurers' assets exceeded the regulatory requirements.

#### Coverage ratios for regulated commitments (available eligible assets / regulated commitments)

%	2010	25th percentile in 2010	Median in 2010	75th percentile in 2010	2009	2008
Life and composite insurers	103.9	103.1	104.5	112.2	103.5	104.2
Non-life insurers	111.4	103.0	116.6	157.7	111.7	113.7
Mutual insurers	125.2	192.0	378.5	715.6	127.6	106.6
Provident institutions	126.8	104.1	116.4	134.8	124.8	124.8

Source: General Secretariat of the ACP

Compared with 2009, the coverage of commitments to policyholders declined slightly for non-life and mutual insurers but still exceeded the minimum requirements. Conversely, the ratio increased among life insurers, composite insurers and provident institutions.

At end-2010, the coverage ratio for the minimum solvency margin requirement was 125.6% for life insurers and 464.8% for provident institutions, excluding unrealised gains. It should be noted, however, that some of the components of the coverage ratio are prone to major volatility, hence the need to maintain a safety margin. Accordingly, relative to 2009, coverage of the minimum solvency margin requirement was down<sup>6</sup> in each category of insurer. The fall was even more dramatic in the case of the ratios with unrealised gains, which were down at end-2010 in all categories except mutual insurers.

#### Balance sheet margin coverage ratio, without and with unrealised gains (Equity adjusted for unrealised gains (losses)/ regulatory margin requirement)

%	2010	25th percentile in 2010	Median in 2010	75th percentile in 2010	2009	2008
Life and composite insurers	125.6	117.2	165.2	256.9	129.0	127.9
plus unrealised gains	178.9	150.0	199.3	366.6	199.5	146.9
Non-life insurers	401.8	119.5	282.4	681.1	407.5	320.3
plus unrealised gains	576.7	128.6	343.2	782.3	610.7	448.6
Mutual insurers	337.1	195.6	341.9	575.7	345.6	340.0
plus unrealised gains	426.7	194.9	355.7	610.9	374.7	340.0
Provident institutions	464.8	172.4	318.5	710.7	522.6	446.0
plus unrealised gains	535.0	178.6	403.6	754.8	602.7	463.1

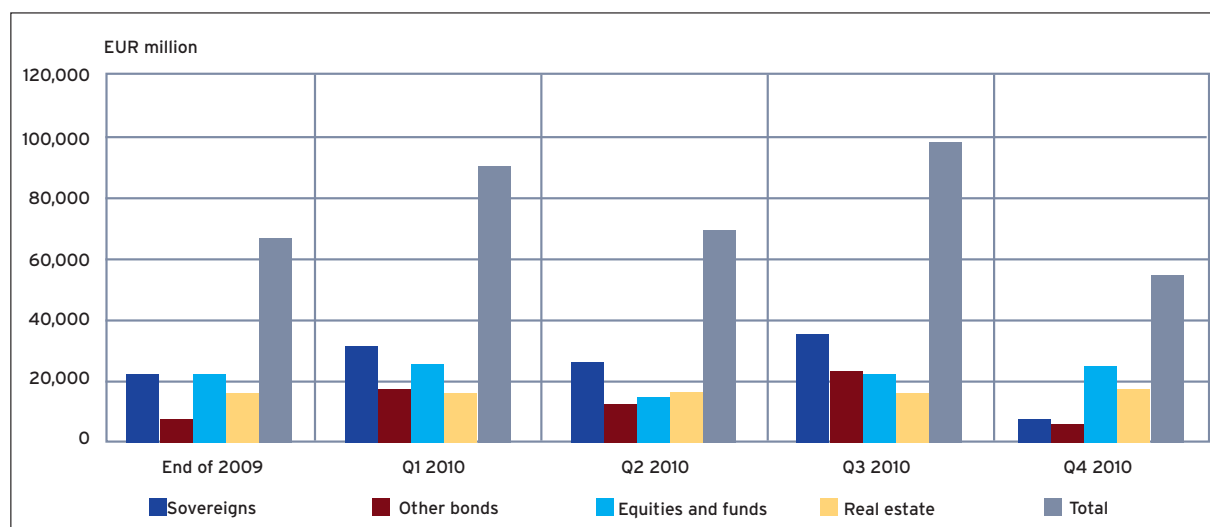
Source: General Secretariat of the ACP

6. Coverage of commitments and coverage of the solvency margin may move in opposite directions because of the varying influence of their components.

In terms of prudential requirements, work continued on preparing the technical measures required to implement the Solvency 2 Directive. As in the banking sector, a decisive shift is underway aimed at improving capital adequacy relative to risks, the measurement of which is to be substantially refined, including through the option of using internal models.

### 3.4 Fall in unrealised gains

#### Unrealised gains and losses on different asset classes in 2010, insurance sector



Source: General Secretariat of the ACP

#### BRIEFING

Unrealised gains measure the difference between the book value of investments and their market value.

Unrealised gains in the insurance sector decreased between end-2009 and end-2010, falling from EUR 90 billion to around EUR 55 billion.

The largest declines involved government securities and, to a lesser extent, non-sovereign debt securities (these two categories of assets were down approximately EUR 35 billion over the year). As a whole, however, asset classes continued to generate unrealised gains at end-2010.

## 3.5 Improved results in 2010

Turnover in the insurance sector rose by around 8% in 2010, owing to life and non-life business, which gained 5% and 13% respectively on the previous year.

### BRIEFING

Underwriting income and net income: to make certain that insurers' financial statements are comparable, insurance accounting regulations call for underwriting income to be reported separately. This means that investments of own funds, non-recurring income and expenses and income tax charges have an impact on net income only. Furthermore, the regulations break down underwriting income into two components: life and non-life.

In 2010, life underwriting income increased by 11% compared with 2009 to EUR 5.1 billion, while non-life underwriting income rose by 14% to EUR 3.6 billion. Growth in investment income in non-life insurance (11%) offset the increase in claim payouts owing to the year's high loss experience (one-off weather events, Atlantic Storm Xynthia, flooding in the Var region, severe winter conditions, etc.). Claim payouts and investment income in life insurance were higher than in 2008 but down slightly on 2009. After counting capitalised investment income, non-recurring items and tax expenses recorded in the non-underwriting income statement, net income for the sector stood at EUR 9.4 billion in 2010, compared with EUR 8.2 billion in 2009.

In 2010, the margin rate for the sector as a whole, i.e. net income as a percentage of premiums, increased from 3.1% in 2009 to 3.3%.

### Summary income statement in EUR billion

(EUR billion)	Vie			Non vie			Total		
	2008	2009	2010	2008	2009	2010	2008	2009	2010
Premiums	140.6	158.8	166.1	103.1	105.5	119.1	243.7	264.3	285.2
Benefits and claims paid * (-)	114.7	213.0	208.6	77.0	82.6	93.0	191.7	295.6	301.6
Investment income	-9.5	70.9	60.1	5.5	5.2	5.8	-4.0	76.2	65.9
o/w adjustments for unit-linked life insurance **	-54.1	25.0	10.3				-54.1	25.0	10.3
Administration expenses (-)	12.6	12.8	13.4	21.1	22.5	25.7	33.7	35.3	39.1
Reinsurance (-)	0.7	-0.7	-0.9	3.2	2.5	2.6	3.9	1.9	1.7
<b>Underwriting income</b>	<b>2.7</b>	<b>4.6</b>	<b>5.1</b>	<b>7.3</b>	<b>3.2</b>	<b>3.6</b>	<b>9.4</b>	<b>7.8</b>	<b>8.7</b>
				Investment income (non-underwriting)			3.8	4.5	4.6
				Other non-underwriting income or loss			-1.8	-4.0	-3.9
				<b>Net income</b>			<b>11.8</b>	<b>8.2</b>	<b>9.4</b>

\* Claims+Expenses+Profit-sharing +/- Adjustments for unit-linked life insurance \*\*

\*\*Adjustment to eliminate the income statement impact of losses or gains on unit-linked policies

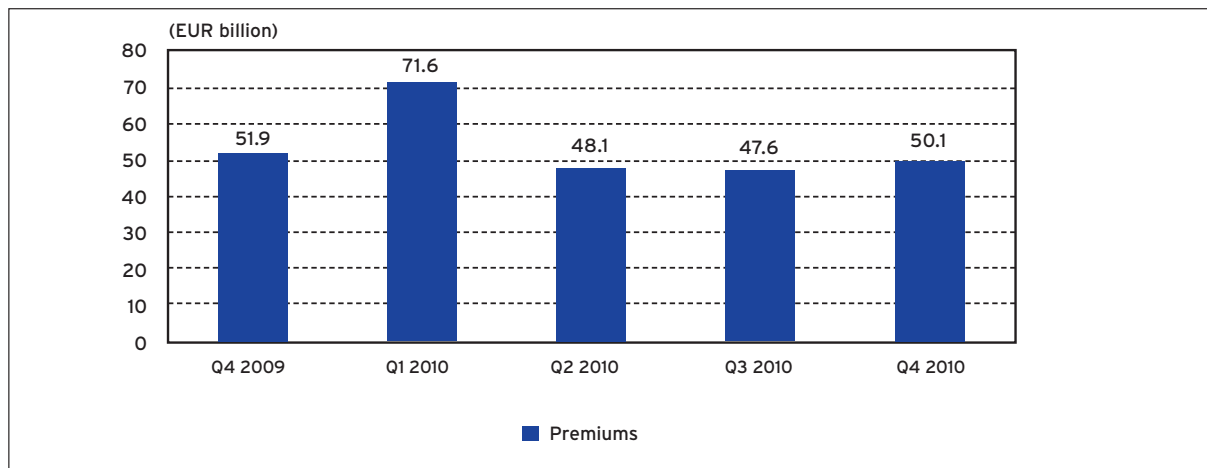
Source: General Secretariat of the ACP

## 4. Areas for attention

### 4.1 Inflows of new funds to life insurance

Totalling EUR 217.3 billion over 2010 as a whole, gross inflows of new funds to the insurance sector remain positive, although they were down 1% on 2009.

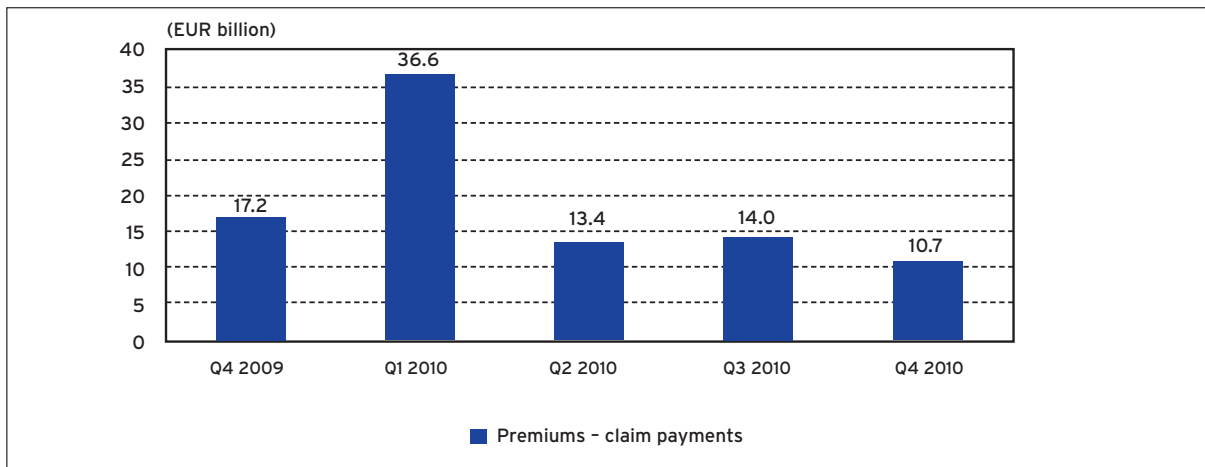
#### Gross inflows (France) - insurance sector



Source: General Secretariat of the ACP

The decline was accompanied by a 3% increase in claim payments, resulting in net inflows of EUR 74.6 billion in 2010, a decline of 9% compared with 2009.

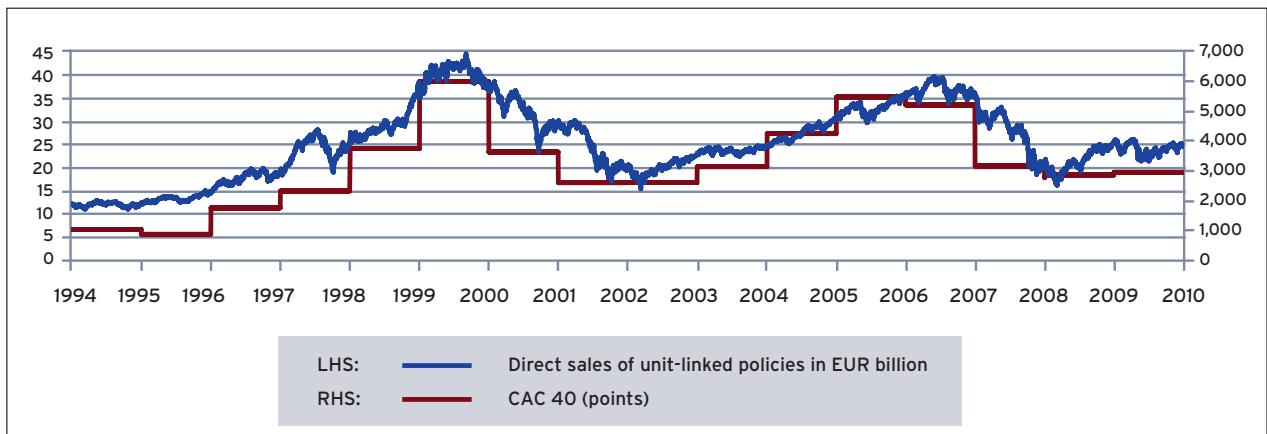
### Premiums - claim payments (France) - insurance sector



Source: General Secretariat of the ACP

An analysis by category shows a slight upturn in new subscriptions to unit-linked policies in 2010, which rose by 3% from 2008 to EUR 19 billion. In the past, sales of this type of policy have always been heavily dependent on stock market index performances.

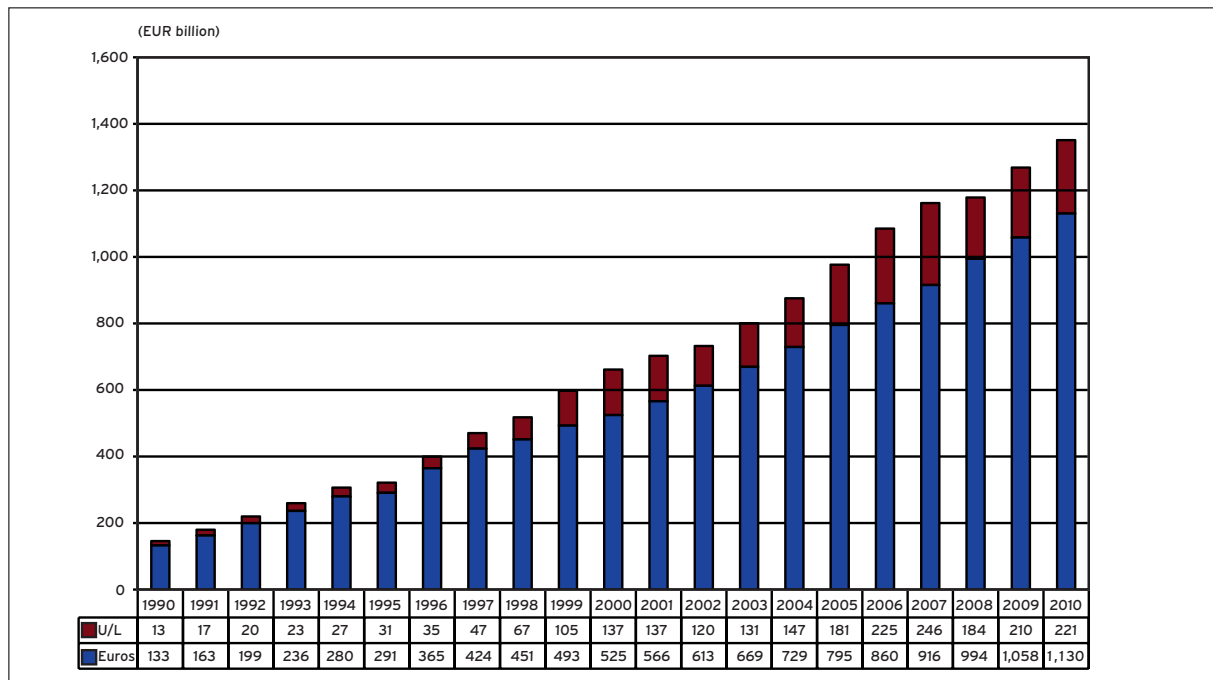
### New subscriptions to unit-linked policies (direct sales) and CAC 40 index



Source: General Secretariat of the ACP

The pattern of redemptions reflected in the decline in actuarial reserves for unit-linked policies in 2008 was not repeated.

## Actuarial reserves for life insurance policies



Source: General Secretariat of the ACP

## 4.2 Sovereign risk

French insurers hold EUR 509 billion in sovereign debt, half of which in French government securities. Aside from the loss of value of sovereign debt, the increased volatility on financial markets could affect the earnings of large insurance groups. Faced with these challenges, insurance entities must continue to rigorously manage their risks.

## 4.3 Property investment

Property makes up a small proportion of insurers' portfolios. In 2010, insurance companies devoted 3.6% of their investments to property, the same as in 2009. Property risk therefore appears to be small.



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## A robust insurance sector

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# Annexes

## A robust insurance sector

## Annex 1

### Life and capital redemption insurance

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	3,816	100.0	5,993	100.0	8,247	100.0	9,096	100.0
Investment income (underwriting)	1,228	32.2	994	16.6	848	10.3	1,224	13.5
Reinsurers' share of expenses	1,176	30.8	1,151	19.2	1,397	16.9	1,640	18.0
<b>Total resources</b>	<b>6,220</b>	<b>163.0</b>	<b>8,138</b>	<b>135.8</b>	<b>10,492</b>	<b>127.2</b>	<b>11,960</b>	<b>131.5</b>
<b>EXPENSES</b>								
Claims paid	5,061	132.6	6,368	106.3	4,994	60.5	4,580	50.3
Change in insurance reserves	-1,522	-39.9	34	0.6	3,387	41.1	4,218	46.4
Administrative and acquisition costs	170	4.5	189	3.2	187	2.3	242	2.7
Profit sharing	866	22.7	758	12.6	1,071	13.0	1,211	13.3
Premiums passed on to reinsurers	1,144	30.0	1,107	18.5	1,319	16.0	1,544	17.0
<b>Total expenses</b>	<b>5,719</b>	<b>149.9</b>	<b>8,456</b>	<b>141.1</b>	<b>10,958</b>	<b>132.9</b>	<b>11,795</b>	<b>129.7</b>
Net transfers between categories	-97	-2.5	254	4.2	278	3.4	142	1.6
<b>UNDERWRITING INCOME</b>	<b>404</b>	<b>10.6</b>	<b>-64</b>	<b>-1.1</b>	<b>-188</b>	<b>-2.3</b>	<b>225</b>	<b>2.5</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	23	29	21	17	0.2	6.4
Acquisition expenses	71	92	113	150	1.6	57.9
Administrative costs and other net underwriting expenses	100	98	73	92	1.0	35.7
<b>TOTAL</b>	<b>194</b>	<b>219</b>	<b>208</b>	<b>258</b>	<b>2.8</b>	<b>100.0</b>

Source: General Secretariat of the ACP

EUR million	2007	2008	2009	2010
Life insurance provisions at closing date	30,281	31,741	36,757	42,555

Source: General Secretariat of the ACP

Changes in guaranteed capital	(EUR million)		Change in %
	Start of year	End of year	
2007	34,437	34,287	-0.4
2008	34,232	35,153	2.7
2009	34,870	39,395	13.0
2010	39,155	45,317	15.7

Source: General Secretariat of the ACP

Contract surrender (EUR million)	2007	2008	2009	2010	% of capital
Termination	10	5	4	4	0.0
Redemption	4,569	3,397	4,370	3,887	9.9
Reductions	18	13	10	22	0.1

Source: General Secretariat of the ACP

## Annex 2

### Euro or foreign currency individual and group insurance contracts

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	86,079	100,0	83,142	100,0	97,638	100,0	102,998	100,0
Investment income (underwriting)	29,011	33,7	25,608	30,8	26,119	26,8	28,410	27,6
Reinsurers' share of expenses	4,851	5,6	4,967	6,0	3,532	3,6	4,760	4,6
<b>Total resources</b>	<b>119,941</b>	<b>139,3</b>	<b>113,717</b>	<b>136,8</b>	<b>127,290</b>	<b>130,4</b>	<b>136,169</b>	<b>132,2</b>
<b>EXPENSES</b>								
Claims paid	61,886	71,9	66,029	79,4	65,145	66,7	69,326	67,3
Change in insurance reserves	25,117	29,2	24,266	29,2	28,660	29,4	30,632	29,7
Administrative and acquisition costs	6,115	7,1	6,222	7,5	6,647	6,8	6,977	6,8
Profit sharing	23,311	27,1	18,960	22,8	25,771	26,4	26,037	25,3
Premiums passed on to reinsurers	4,682	5,4	4,661	5,6	3,320	3,4	4,508	4,4
<b>Total expenses</b>	<b>121,111</b>	<b>140,7</b>	<b>120,138</b>	<b>144,5</b>	<b>129,543</b>	<b>132,7</b>	<b>137,479</b>	<b>133,5</b>
Net transfers between categories	3,617	4,2	7,249	8,7	3,724	3,8	2,572	2,5
<b>UNDERWRITING INCOME</b>	<b>2,447</b>	<b>2,8</b>	<b>828</b>	<b>1,0</b>	<b>1,470</b>	<b>1,5</b>	<b>1,261</b>	<b>1,2</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	275	273	320	301	0.3	4.1
Acquisition expenses	3,677	3,092	3,229	3,337	3.2	45.8
Administrative costs and other net underwriting expenses	2,445	3,144	3,424	3,645	3.5	50.0
<b>TOTAL</b>	<b>6,397</b>	<b>6,509</b>	<b>6,973</b>	<b>7,283</b>	<b>7.1</b>	<b>100.0</b>

Source: General Secretariat of the ACP

EUR million	2007	2008	2009	2010
Life insurance provisions at closing date	769,072	824,445	891,064	956,273

Source: General Secretariat of the ACP

Changes in guaranteed capital	(EUR million)		Change in %
	Start of year	End of year	
2007	985,127	1,037,258	5.3
2008	1,037,044	1,112,184	7.2
2009	1,080,657	1,160,429	7.4
2010	1,155,409	1,246,121	7.9

Source: General Secretariat of the ACP

Contract surrender (EUR million)	2007	2008	2009	2010	% of capital
Termination	36,322	32,420	20,519	20,799	1.8
Redemption	48,997	42,369	39,434	39,082	3.4
Reductions	874	2,004	592	508	0.0

Source: General Secretariat of the ACP

## Annex 3

### Whole life and term life group insurance

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	11,359	100.0	10,992	100.0	12,351	100.0	10,853	100.0
Investment income (underwriting)	2,425	21.3	1,740	15.8	1,543	12.5	1,955	18.0
Reinsurers' share of expenses	823	7.2	1,493	13.6	2,042	16.5	1,474	13.6
<b>Total resources</b>	<b>14,607</b>	<b>128.6</b>	<b>14,225</b>	<b>129.4</b>	<b>15,936</b>	<b>129.0</b>	<b>14,282</b>	<b>131.6</b>
<b>EXPENSES</b>								
Claims paid	6,226	54.8	6,389	58.1	6,828	55.3	6,805	62.7
Change in insurance reserves	2,055	18.1	1,333	12.1	1,628	13.2	213	2.0
Administrative and acquisition costs	2,454	21.6	2,383	21.7	2,774	22.5	2,940	27.1
Profit sharing	1,749	15.4	1,252	11.4	1,921	15.6	1,470	13.5
Premiums passed on to reinsurers	985	8.7	1,768	16.1	2,340	18.9	1,643	15.1
<b>Total expenses</b>	<b>13,469</b>	<b>118.6</b>	<b>13,125</b>	<b>119.4</b>	<b>15,493</b>	<b>125.4</b>	<b>13,070</b>	<b>120.4</b>
Net transfers between categories	82	0.7	-315	-2.9	411	3.3	226	2.1
<b>UNDERWRITING INCOME</b>	<b>1,220</b>	<b>10.7</b>	<b>785</b>	<b>7.1</b>	<b>898</b>	<b>7.3</b>	<b>1,437</b>	<b>13.2</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	136	129	145	176	1.6	5.6
Acquisition expenses	2,057	2,122	2,279	2,414	22.2	77.0
Administrative costs and other net underwriting expenses	418	287	515	544	5.0	17.4
<b>TOTAL</b>	<b>2,611</b>	<b>2,538</b>	<b>2,939</b>	<b>3,134</b>	<b>28.9</b>	<b>100.0</b>

Source: General Secretariat of the ACP

EUR million	2007	2008	2009	2010
Life insurance provisions at closing date	63,677	67,219	72,985	75,396

Source: General Secretariat of the ACP

Changes in guaranteed capital	(EUR million)		Change in %
	Start of year	End of year	
2007	1,521,433	1,692,033	11.2
2008	1,751,121	1,840,887	4.8
2009	1,793,983	1,811,552	1.0
2010	1,802,799	1,675,789	-7.0

Source: General Secretariat of the ACP

Contract surrender (EUR million)	2007	2008	2009	2010	% of capital
Termination	6,561	49,533	29,734	34,381	1.9
Redemption	385	385	371	293	0.0
Reductions	2003	697	740	321	0.0

Source: General Secretariat of the ACP

## Annex 4

### Unit-linked life insurance

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	33,523	100.0	20,182	100.0	17,829	100.0	19,045	100.0
Investment income (underwriting)	1,848	5.5	1,341	6.6	1,479	8.3	1,520	8.0
Reinsurers' share of expenses	3,232	9.6	-270	-1.3	802	4.5	594	3.1
<b>Total resources</b>	<b>38,603</b>	<b>115.2</b>	<b>21,253</b>	<b>105.3</b>	<b>20,111</b>	<b>112.8</b>	<b>21,158</b>	<b>111.1</b>
<b>EXPENSES</b>								
Claims paid	9,973	29.7	15,749	78.0	10,587	59.4	11,938	62.7
Change in insurance reserves	17,978	53.6	-4,933	-24.4	1,398	7.8	2,855	15.0
Administrative and acquisition costs	2,022	6.0	1,908	9.5	1,231	6.9	1,437	7.5
Profit sharing	544	1.6	789	3.9	643	3.6	487	2.6
Premiums passed on to reinsurers	3,174	9.5	781	3.9	336	1.9	345	1.8
<b>Total expenses</b>	<b>33,691</b>	<b>100.5</b>	<b>14,294</b>	<b>70.8</b>	<b>14,194</b>	<b>79.6</b>	<b>17,063</b>	<b>89.6</b>
Net transfers between categories	-3,603	-10.7	-7,139	-35.4	-4,415	-24.8	-2,959	-15.5
<b>UNDERWRITING INCOME</b>	<b>1,309</b>	<b>3.9</b>	<b>-180</b>	<b>-0.9</b>	<b>1,502</b>	<b>8.4</b>	<b>1,137</b>	<b>6.0</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	61	89	88	76	0.4	5.0
Acquisition expenses	1,146	799	596	625	3.3	41.3
Administrative costs and other net underwriting expenses	876	1,102	634	812	4.3	53.7
<b>TOTAL</b>	<b>2,083</b>	<b>1,990</b>	<b>1,319</b>	<b>1,513</b>	<b>7.9</b>	<b>100.0</b>

Source: General Secretariat of the ACP

EUR million	2007	2008	2009	2010
Life insurance provisions at closing date	243,862	182,797	207,269	219,360

Source: General Secretariat of the ACP

## Annex 5

### Occupational retirement insurance (class 26 and PERP)

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	1,745	100.0	1,836	100.0	1,842	100.0	1,872	100.0
Investment income (underwriting)	560	32.1	509	27.7	508	27.6	810	43.3
Reinsurers' share of expenses	501	28.7	414	22.5	573	31.1	976	52.2
<b>Total resources</b>	<b>2,806</b>	<b>160.8</b>	<b>2,759</b>	<b>150.3</b>	<b>2,922</b>	<b>158.6</b>	<b>3,658</b>	<b>195.4</b>
<b>EXPENSES</b>								
Claims paid	420	24.1	-35	-1.9	587	31.9	655	35.0
Change in insurance reserves	1,272	72.9	1,950	106.2	1,176	63.9	1,543	82.5
Administrative and acquisition costs	91	5.2	109	5.9	97	5.3	148	7.9
Profit sharing	716	41.0	502	27.3	768	41.7	1,022	54.6
Premiums passed on to reinsurers	291	16.7	295	16.1	288	15.6	274	14.6
<b>Total expenses</b>	<b>2,790</b>	<b>159.9</b>	<b>2,821</b>	<b>153.6</b>	<b>2,916</b>	<b>158.3</b>	<b>3,642</b>	<b>194.6</b>
Net transfers between categories	0	0.0	1	0.1	0	0.0	0	0.0
<b>UNDERWRITING INCOME</b>	<b>16</b>	<b>0.9</b>	<b>-61</b>	<b>-3.3</b>	<b>7</b>	<b>0.4</b>	<b>16</b>	<b>0.9</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	3	4	4	5	0.3	3.2
Acquisition expenses	68	74	79	78	4.2	49.7
Administrative costs and other net underwriting expenses	27	39	22	74	3.9	47.0
<b>TOTAL</b>	<b>98</b>	<b>117</b>	<b>105</b>	<b>157</b>	<b>8.4</b>	<b>100.0</b>

Source: General Secretariat of the ACP

EUR million	2007	2008	2009	2010
Life insurance provisions at closing date	18,035	20,004	21,843	24,564

Source: General Secretariat of the ACP

## Annex 6

### Motor insurance

#### Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	17,687	100.0	17,846	100.0	17,805	100.0	18,274	100.0
Investment income (underwriting)	1,493	8.4	1,119	6.3	1,095	6.2	1,062	5.8
Reinsurers' share of expenses	1,978	11.2	1,966	11.0	1,270	7.1	1,296	7.1
<b>Total resources</b>	<b>21,158</b>	<b>119.6</b>	<b>20,931</b>	<b>117.3</b>	<b>20,171</b>	<b>113.3</b>	<b>20,632</b>	<b>112.9</b>
<b>EXPENSES</b>								
Claims paid	13,020	73.6	13,523	75.8	14,141	79.4	13,216	72.3
Change in insurance reserves	1,417	8.0	947	5.3	1,543	8.7	820	4.5
Administrative and acquisition costs	3,550	20.1	3,726	20.9	3,781	21.2	3,338	18.3
Profit sharing	8	0.0	16	0.1	4	0.0	3	0.0
Premiums passed on to reinsurers	2,189	12.4	2,134	12.0	1,199	6.7	1,379	7.5
<b>Total expenses</b>	<b>20,184</b>	<b>114.1</b>	<b>20,346</b>	<b>114.0</b>	<b>20,667</b>	<b>116.1</b>	<b>18,755</b>	<b>102.6</b>
<b>UNDERWRITING INCOME</b>	<b>974</b>	<b>5.5</b>	<b>585</b>	<b>3.3</b>	<b>-496</b>	<b>-2.8</b>	<b>47</b>	<b>0.3</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	1,622	1,656	1,654	1,523	8.3	31.3
Acquisition expenses	2,358	2,409	2,510	2,209	12.1	45.4
Administrative costs and other net underwriting expenses	1,200	1,319	1,274	1,132	6.2	23.3
<b>TOTAL</b>	<b>5,180</b>	<b>5,384</b>	<b>5,438</b>	<b>4,863</b>	<b>26.6</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>29.3</b>	<b>30.2</b>	<b>30.5</b>	<b>26.6</b>		

Source: General Secretariat of the ACP

#### Change in claims ratio (claims/premiums, including claims processing expense)

Year of claim events (%)	2006	2007	2008	2009	2010
Claims ratio					
At the end of the first year	84.0	86.1	85.5	91.3	90.2
At the end of the second year	83.5	85.4	85.4	90.3	-
At the end of the third year	81.1	83.5	83.0	-	-
At the end of the fourth year	80.4	82.4	-	-	-
At the end of the fifth year	79.6	-	-	-	-

Source: General Secretariat of the ACP

## Annex 7

### Property insurance

#### Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	12,875	100.0	13,376	100.0	13,747	100.0	14,166	100.0
Investment income (underwriting)	729	5.7	579	4.3	508	3.7	496	3.5
Reinsurers' share of expenses	1,168	9.1	1,112	8.3	2,172	15.8	1,319	9.3
<b>Total resources</b>	<b>14,772</b>	<b>114.7</b>	<b>15,067</b>	<b>112.6</b>	<b>16,428</b>	<b>119.5</b>	<b>15,982</b>	<b>112.8</b>
<b>EXPENSES</b>								
Claims paid	7,722	60.0	7,972	59.6	10,308	75.0	8,241	58.2
Change in insurance reserves	713	5.5	596	4.5	452	3.3	410	2.9
Administrative and acquisition costs	3,204	24.9	3,440	25.7	3,507	25.5	3,171	22.4
Profit sharing	80	0.6	88	0.7	81	0.6	71	0.5
Premiums passed on to reinsurers	2,294	17.8	2,265	16.9	2,412	17.5	2,145	15.1
<b>Total expenses</b>	<b>14,013</b>	<b>108.8</b>	<b>14,361</b>	<b>107.4</b>	<b>16,760</b>	<b>121.9</b>	<b>14,038</b>	<b>99.1</b>
<b>UNDERWRITING INCOME</b>	<b>759</b>	<b>5.9</b>	<b>706</b>	<b>5.3</b>	<b>-332</b>	<b>-2.4</b>	<b>361</b>	<b>2.5</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	1,078	1,109	1,194	1,031	7.3	24.5
Acquisition expenses	2,188	2,348	2,382	2,193	15.5	52.2
Administrative costs and other net underwriting expenses	1,022	1,094	1,127	981	6.9	23.3
<b>TOTAL</b>	<b>4,288</b>	<b>4,551</b>	<b>4,704</b>	<b>4,205</b>	<b>29.7</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>33.3</b>	<b>34.0</b>	<b>34.2</b>	<b>29.7</b>		

Source: General Secretariat of the ACP

#### Change in claims ratio (claims/premiums, including claims processing expense)

Year of claim events (%)	2006	2007	2008	2009	2010
Claims ratio					
At the end of the first year	71.9	72.2	71.9	88.6	77.5
At the end of the second year	69.9	69.7	70.9	85.6	-
At the end of the third year	67.5	67.5	69.1	-	-
At the end of the fourth year	66.4	66.5	-	-	-
At the end of the fifth year	65.7	-	-	-	-

Source: General Secretariat of the ACP

## Annex 8

### General liability insurance Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	2,959	100.0	3,037	100.0	3,069	100.0	3,000	100.0
Investment income (underwriting)	679	22.9	600	19.8	480	15.6	479	16.0
Reinsurers' share of expenses	572	19.3	428	14.1	422	13.7	491	16.4
<b>Total resources</b>	<b>4,210</b>	<b>142.3</b>	<b>4,065</b>	<b>133.8</b>	<b>3,970</b>	<b>129.4</b>	<b>3,970</b>	<b>132.3</b>
<b>EXPENSES</b>								
Claims paid	1,401	47.3	1,573	51.8	1,531	49.9	1,401	46.7
Change in insurance reserves	848	28.7	379	12.5	449	14.6	727	24.2
Administrative and acquisition costs	583	19.7	624	20.5	633	20.6	561	18.7
Profit sharing	3	0.1	2	0.1	3	0.1	4	0.1
Premiums passed on to reinsurers	580	19.6	541	17.8	545	17.8	557	18.6
<b>Total expenses</b>	<b>3,415</b>	<b>115.4</b>	<b>3,119</b>	<b>102.7</b>	<b>3,161</b>	<b>103.0</b>	<b>3,249</b>	<b>108.3</b>
<b>UNDERWRITING INCOME</b>	<b>795</b>	<b>26.9</b>	<b>946</b>	<b>31.1</b>	<b>809</b>	<b>26.4</b>	<b>411</b>	<b>13.7</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	187	194	189	166	5.5	22.9
Acquisition expenses	389	410	422	363	12.1	49.9
Administrative costs and other net underwriting expenses	194	215	212	198	6.6	27.2
<b>TOTAL</b>	<b>769</b>	<b>818</b>	<b>822</b>	<b>727</b>	<b>24.2</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>26.0</b>	<b>26.9</b>	<b>26.8</b>	<b>24.2</b>		

Source: General Secretariat of the ACP

#### Change in claims ratio (claims/premiums, including claims processing expense)

Year of claim events (%)	2006	2007	2008	2009	2010
Claims ratio					
At the end of the first year	80.3	85.3	83.6	81.0	79.8
At the end of the second year	80.9	83.0	84.4	81.6	-
At the end of the third year	76.1	83.2	83.7	-	-
At the end of the fourth year	73.5	82.3	-	-	-
At the end of the fifth year	72.8	-	-	-	-

Source: General Secretariat of the ACP

## Annex 9

### Natural disaster insurance Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	1,270	100.0	1,293	100.0	1,282	100.0	1,300	100.0
Investment income (underwriting)	88	6.9	76	5.9	57	4.5	57	4.4
Reinsurers' share of expenses	390	30.7	336	26.0	288	22.5	720	55.4
<b>Total resources</b>	<b>1,748</b>	<b>137.6</b>	<b>1,705</b>	<b>131.9</b>	<b>1,627</b>	<b>127.0</b>	<b>2,077</b>	<b>159.8</b>
<b>EXPENSES</b>								
Claims paid	593	46.7	648	50.1	677	52.8	1,219	93.8
Change in insurance reserves	62	4.9	18	1.4	-124	-9.7	20	1.6
Administrative and acquisition costs	198	15.6	223	17.2	217	16.9	195	15.0
Profit sharing	9	0.7	10	0.8	9	0.7	8	0.6
Premiums passed on to reinsurers	759	59.8	751	58.1	752	58.7	636	49.0
<b>Total expenses</b>	<b>1,621</b>	<b>127.6</b>	<b>1,650</b>	<b>127.6</b>	<b>1,531</b>	<b>119.5</b>	<b>2,079</b>	<b>160.0</b>
<b>UNDERWRITING INCOME</b>	<b>127</b>	<b>10.0</b>	<b>55</b>	<b>4.3</b>	<b>96</b>	<b>7.5</b>	<b>-157</b>	<b>-12.1</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	68	74	68	89	6.8	31.2
Acquisition expenses	135	141	141	122	9.4	43.0
Administrative costs and other net underwriting expenses	63	82	76	73	5.7	25.9
<b>TOTAL</b>	<b>266</b>	<b>297</b>	<b>285</b>	<b>284</b>	<b>21.9</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>20.9</b>	<b>23.0</b>	<b>22.2</b>	<b>21.9</b>		

Source: General Secretariat of the ACP

## Annex 10

### Other insurance

#### Simplified income statement

“Other insurance” includes assistance, legal expenses and sundry financial losses.

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	3,114	100.0	3,287	100.0	3,467	100.0	3,653	100.0
Investment income (underwriting)	122	3.9	85	2.6	91	2.6	92	2.5
Reinsurers' share of expenses	374	12.0	396	12.0	492	14.2	506	13.9
<b>Total resources</b>	<b>3,610</b>	<b>115.9</b>	<b>3,768</b>	<b>114.6</b>	<b>4,050</b>	<b>116.8</b>	<b>4,251</b>	<b>116.4</b>
<b>EXPENSES</b>								
Claims paid	1,436	46.1	1,485	45.2	1,660	47.9	1,774	48.6
Change in insurance reserves	158	5.1	142	4.3	204	5.9	21	0.6
Administrative and acquisition costs	1,234	39.6	1,314	40.0	1,339	38.6	1,316	36.0
Profit sharing	98	3.1	73	2.2	39	1.1	54	1.5
Premiums passed on to reinsurers	496	15.9	573	17.4	599	17.3	576	15.8
<b>Total expenses</b>	<b>3,422</b>	<b>109.9</b>	<b>3,587</b>	<b>109.1</b>	<b>3,841</b>	<b>110.8</b>	<b>3,741</b>	<b>102.4</b>
<b>UNDERWRITING INCOME</b>	<b>188</b>	<b>6.0</b>	<b>181</b>	<b>5.5</b>	<b>209</b>	<b>6.0</b>	<b>329</b>	<b>9.0</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	288	305	321	347	9.5	20.6
Acquisition expenses	962	1,010	1,059	1,067	29.2	63.5
Administrative costs and other net underwriting expenses	272	305	280	267	7.3	15.9
<b>TOTAL</b>	<b>1,522</b>	<b>1,619</b>	<b>1,660</b>	<b>1,681</b>	<b>46.0</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>48.9</b>	<b>49.3</b>	<b>47.9</b>	<b>46.0</b>		

Source: General Secretariat of the ACP

Change in claims ratio (claims/premiums, including claims processing expense)

Year of claim events (%)	2006	2007	2008	2009	2010
Claims ratio					
At the end of the first year	55.5	53.9	52.4	54.8	54.5
At the end of the second year	50.7	51.1	52.0	52.7	-
At the end of the third year	50.3	50.6	49.1	-	-
At the end of the fourth year	49.1	49.8	-	-	-
At the end of the fifth year	48.7	-	-	-	-

Source: General Secretariat of the ACP

## Annex 11

### Transport insurance

#### Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	968	100.0	1018	100.0	964	100.0	936	100.0
Investment income (underwriting)	94	9.7	109	10.7	52	5.3	58	6.2
Reinsurers' share of expenses	149	15.4	202	19.8	251	26.0	147	15.7
<b>Total resources</b>	<b>1,211</b>	<b>125.1</b>	<b>1,329</b>	<b>130.6</b>	<b>1,267</b>	<b>131.4</b>	<b>1,141</b>	<b>121.9</b>
<b>EXPENSES</b>								
Claims paid	601	62.1	628	61.7	615	63.8	731	78.1
Change in insurance reserves	-53	-5.5	-76	-7.5	-2	-0.2	-243	-26.0
Administrative and acquisition costs	240	24.8	250	24.6	238	24.6	240	25.7
Profit sharing	-1	-0.1	-1	-0.1	1	0.1	0	0.0
Premiums passed on to reinsurers	282	29.1	341	33.5	295	30.6	250	26.8
<b>Total expenses</b>	<b>1,069</b>	<b>110.4</b>	<b>1,142</b>	<b>112.2</b>	<b>1,146</b>	<b>118.8</b>	<b>979</b>	<b>104.6</b>
<b>UNDERWRITING INCOME</b>	<b>142</b>	<b>14.7</b>	<b>187</b>	<b>18.4</b>	<b>121</b>	<b>12.5</b>	<b>133</b>	<b>14.2</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	40	43	43	35	3.7	12.7
Acquisition expenses	139	142	151	140	15.0	50.9
Administrative costs and other net underwriting expenses	100	108	86	100	10.7	36.4
<b>TOTAL</b>	<b>280</b>	<b>293</b>	<b>281</b>	<b>275</b>	<b>29.4</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>28.9</b>	<b>28.8</b>	<b>29.1</b>	<b>29.4</b>		

Source: General Secretariat of the ACP

## Annex 12

### Construction insurance

#### Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	2,460	100.0	2,463	100.0	2,313	100.0	2,254	100.0
Investment income (underwriting)	742	30.2	622	25.3	543	23.5	547	24.3
Reinsurers' share of expenses	303	12.3	289	11.7	351	15.2	342	15.2
<b>Total resources</b>	<b>3,505</b>	<b>142.5</b>	<b>3,374</b>	<b>137.0</b>	<b>3,207</b>	<b>138.7</b>	<b>3,143</b>	<b>139.5</b>
<b>EXPENSES</b>								
Claims paid	970	39.4	1,082	43.9	1,128	48.8	1,006	44.6
Change in insurance reserves	1,384	56.3	1,157	47.0	859	37.2	702	31.1
Administrative and acquisition costs	365	14.8	385	15.6	371	16.1	315	14.0
Profit sharing	0	0.0	0	0.0	2	0.1	2	0.1
Premiums passed on to reinsurers	411	16.7	426	17.3	403	17.4	388	17.2
<b>Total expenses</b>	<b>3,130</b>	<b>127.2</b>	<b>3,050</b>	<b>123.8</b>	<b>2,764</b>	<b>119.5</b>	<b>2,412</b>	<b>107.0</b>
<b>UNDERWRITING INCOME</b>	<b>375</b>	<b>15.2</b>	<b>324</b>	<b>13.2</b>	<b>443</b>	<b>19.2</b>	<b>440</b>	<b>19.5</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	142	145	145	119	5.3	27.4
Acquisition expenses	247	262	245	211	9.4	48.7
Administrative costs and other net underwriting expenses	119	123	127	103	4.6	23.8
<b>TOTAL</b>	<b>508</b>	<b>530</b>	<b>517</b>	<b>434</b>	<b>19.3</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>20.7</b>	<b>21.5</b>	<b>22.3</b>	<b>19.3</b>		

Source: General Secretariat of the ACP

## Annex 13

### Credit insurance and surety bonding

#### Simplified income statement

EUR million	2007		2008		2009		2010	
	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums	Amount	% of premiums
<b>RESOURCES</b>								
Premiums	878	100.0	882	100.0	796	100.0	928	100.0
Investment income (underwriting)	97	11.0	84	9.5	104	13.1	71	7.6
Reinsurers' share of expenses	139	15.8	87	9.9	111	13.9	183	19.7
<b>Total resources</b>	<b>1,114</b>	<b>126.9</b>	<b>1,053</b>	<b>119.4</b>	<b>1,011</b>	<b>127.0</b>	<b>1,182</b>	<b>127.3</b>
<b>EXPENSES</b>								
Claims paid	315	35.9	369	41.8	599	75.3	304	32.7
Change in insurance reserves	85	9.7	-47	-5.3	-50	-6.3	95	10.2
Administrative and acquisition costs	232	26.4	224	25.4	230	28.9	274	29.5
Profit sharing	12	1.4	21	2.4	14	1.7	27	2.9
Premiums passed on to reinsurers	163	18.6	175	19.8	139	17.4	237	25.6
<b>Total expenses</b>	<b>807</b>	<b>91.9</b>	<b>742</b>	<b>84.1</b>	<b>932</b>	<b>117.1</b>	<b>937</b>	<b>101.0</b>
<b>UNDERWRITING INCOME</b>	<b>307</b>	<b>35.0</b>	<b>311</b>	<b>35.3</b>	<b>79</b>	<b>9.9</b>	<b>241</b>	<b>26.0</b>

Source: General Secretariat of the ACP

Operating expenses (EUR million)	2007	2008	2009	2010	% of premiums	% of total
Claims processing expenses	56	47	37	0	0.0	0.0
Acquisition expenses	174	174	181	184	19.9	67.3
Administrative costs and other net underwriting expenses	58	50	49	90	9.7	32.7
<b>TOTAL</b>	<b>288</b>	<b>271</b>	<b>268</b>	<b>274</b>	<b>29.5</b>	<b>100.0</b>
<b>Total as a % of premiums</b>	<b>32.8</b>	<b>30.7</b>	<b>33.6</b>	<b>29.5</b>		

Source: General Secretariat of the ACP



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# Recent compensation policies and practices at major banks in France and in countries where G-SIFIs<sup>7</sup> are headquartered

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<sup>7</sup> G-SIFIs: Global Systemically Important Financial Institutions.



Recent compensation policies and practices at major banks in France and in countries where G-SIFIs are headquartered

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## Summary

In 2009, the Financial Stability Board (FSB) issued a set of principles and standards for compensation at financial institutions. The G20 called for these principles and standards to be implemented before the end of 2010.

In France, the Banking and Financial Regulations Act of 22 October 2010 requires “the ACP to review compensation policies and practices applied in connection with employees who are financial market professionals and whose compensation could have a material impact on the risk exposure of the firm, in order to assess compliance with current legal and regulatory provisions”.

This report provides an initial review of the progress made in implementing the FSB’s principles and standards in France and in the main countries where G-SIFIs<sup>8</sup> are headquartered, both in terms of regulatory developments and banks’ compensation practices.

### 1. Regulatory developments

#### 1.1 France

France incorporated the FSB’s key principles and standards, including the ones on disclosure, into its regulations in late 2009, and then rounded off the process by transposing Europe’s Third Capital Requirements Directive (CRD3)<sup>9</sup> of 24 November 2010. As a result, Regulation 97-02 is now in line with all the principles and standards. France has not introduced an application threshold for the measures, which therefore apply to all banks and financial institutions covered by CRD3.

#### 1.2 European Union (United Kingdom and Germany)

The UK’s Financial Services Authority (FSA) and Germany’s Bundesanstalt für Finanzdienstleistungsaufsicht (BaFin) introduced new regulations **in the second half of 2009** aimed at reforming compensation practices in financial services by aligning with FSB principles and standards. However, both authorities introduced principles of proportionality based on firm size and compensation thresholds for affected populations. The FSA estimates that its new rules affect 26 or so major financial institutions, while BaFin has said that its most demanding provisions do not apply to the majority of institutions covered by the regulations. Neither the FSA nor BaFin set disclosure obligations.

**In the second half of 2010**, the United Kingdom and Germany, like France, transposed CRD3, and their regulations are now in line with all of the FSB’s principles and standards. However, they have maintained proportionality approaches in terms of:

- the institutions subject to the most demanding requirements, based on size and activities;
- the scope of populations of “risk-takers”, whose definition leaves plenty of room for interpretation.

#### 1.3 Switzerland

FINMA, the Swiss regulator, published a circular in late 2009 applicable from 1 January 2011, except as regards disclosure requirements, which apply to compensation paid in respect of 2010.

8. G-SIFIs: Global Systemically Important Financial Institutions.

9. CRD3 adopts the FSB’s principles and standards on compensation in the financial sector.

However:

- FINMA did not transpose all of the FSB's principles and standards; and
- the regulator introduced a principle of proportionality effectively limiting application to six banks and five insurance companies; the rules act as non-binding guidance for other institutions.

#### 1.4 United States

In 2008, the United States passed the TARP Act, which provided refinancing to financial institutions. This aid came with severe restrictions on compensation for senior executives, providing an incentive to exit the programme as quickly as possible.

At end-2009:

- the Federal Reserve Board (Fed) organised a consultation on proposed guidance based on the FSB's principles and standards. This guidance did not set a minimum threshold for the portions of variable compensation paid on a deferred basis and/or in shares. The Fed also reviewed the compensation practices of major US banks and foreign banks operating in the United States;
- the Securities and Exchange Commission (SEC) amended its regulations on the disclosure of executive compensation. However, the changes were not consistent with the FSB's principles and standards and were not specific to the financial sector.

In 2010, several federal regulatory agencies, including the Fed and the FDIC<sup>10</sup>, issued final guidance for the whole of the banking and insurance sector. This document was very similar to the proposed guidance

issued by the Fed in 2009. The highlight of 2010 was the passing of the Dodd Frank Act on 21 July, which amended the regulatory framework for the delivery of financial services in the United States and which is designed to coordinate the activities of the different federal regulators.

Implementing legislation for Dodd Frank is being written in 2011. As part of this process, the guidance of June 2010 is to be replaced by a new and largely similar document that, like the earlier version, will not transpose exactly all of the FSB's principles and standards.

## 2. Banks' compensation practices

### 2.1 International

Disclosures by major banks in the main countries reveal the following broad trends:

- general talk about introducing compensation schemes that discourage excessive risk-taking, coupled with a determination to retain the freedom to set compensation on a highly competitive employment market;
- determination in the United States to refrain from disclosing information about risk-takers, on competitive grounds; likewise, in Germany and the United Kingdom, there is a clear desire to restrict this regulated population;
- as a result, banks are applying the concept of "risk-takers" in two different ways: one for their in-house practices, and another for their disclosures.

### 2.2 France

Overall, the FSB's principles and standards, as written into Regulation

10. FDIC: Federal Deposit Insurance Corporation.

97-02, have been implemented in a satisfactory manner in France, although there are marked differences between institutions, depending on the size of their corporate and investment banking (CIB) business and depending on whether they are French or tied to foreign banks.

The fact that the regulations do not contain precise rules on applying the proportionality principle has certainly promoted proper implementation.

Disclosures by French banks are more open and extensive than those of banks in the other countries analysed; this is a positive point in terms of reporting, but needs to be considered against the less stringent practices of foreign banks in a highly competitive job market.

By and large, French banks have applied FSB standards 6 to 9 effectively (40-60% of variable compensation deferred over a period of three years or more, 50% of variable compensation awarded in shares or equivalent instruments, introduction of malus provisions). Non-EU banks have not necessarily applied these standards, and banks within the EU may have restricted this approach to certain population categories. Once again, this amounts to effective application of the standards, but it is also a competitive weakness.

Meanwhile, even in France, the shares of fixed and variable portions of compensation vary considerably from one institution to another depending on their lines of business, and the differences are even greater at higher management levels. Banks with smaller CIB businesses have a higher proportion of fixed compensation than other banks.

The report also highlights a number

of shortcomings in terms of the portions paid in shares, malus provisions and guaranteed bonuses.

### 3. Conclusion

**The FSB's principles and standards provided an opportunity for all parties – regulators and banks alike – to reflect on the dangers posed by compensation policies that do not discourage excessive risk-taking and that fail to emphasise long-term performance.** Beyond the principles themselves, however, the goal of convergence, which is necessary to ensure effectiveness, and the discussions required to achieve that goal are far from complete. In particular:

- the notion of material risk-takers is not defined in the FSB's principles and standards, which is giving rise to overly diverse interpretations both within and between countries;
- requisite disclosure levels are too dissimilar, with those following less stringent approaches openly seeking to shield themselves from competition on the job market;
- the quantitative standards (6 to 9) are pitting those countries that are applying them as standards against those that view them merely as guidance;
- some countries say that the FSB's principles and standards are incompatible with domestic legislation, particularly labour laws.

All these questions need uniform responses to prevent cross-country competitive distortions, which would be detrimental to the implementation of the FSB's principles and standards, and to ensure the effective emergence of sound compensation policies at international level.

## Compensation policies and practices at major banks in France and in countries where G-SIFIs are headquartered<sup>11</sup>

Noting that excessive variable compensation practices at banks and other financial institutions played a part in the uncontrolled risks that underpinned the sub-prime crisis in 2007 and the wider problems in 2008, on 2 April 2009, the Financial Stability Forum (FSF) issued a set of Principles for Sound Compensation Practices, which were rounded out on 25 September 2009 with Principles for Sound Compensation Practices – Implementation Standards issued by the FSF's successor, the Financial Stability Board<sup>12</sup> (FSB). The heads of state and government of the G20 member states endorsed most of the principles at the summit meeting held in Pittsburgh on 24 and 25 September 2009. Then, meeting in Toronto on 26 and 27 June 2010, the G20 heads of state and government called for all the FSB's principles and standards<sup>13</sup> to be implemented before the end of 2010.

In view of the international and competitive nature of the banking sector – particularly in the capital markets, which, as the 2007-2008 crisis demonstrated, are highly sensitive to potential systemic risk – it was felt that a review was needed of the measures taken by France and the other main FSB member states where the largest global banks are headquartered to align themselves with the FSB principles. Accordingly, a study was made of regulatory developments in France, two other EU countries (United Kingdom and Germany), Switzerland and the United States, and of the compensation practices followed by their main banking institutions. That study is

the subject of this report.

To review regulatory developments, the study looked directly at the laws and regulations issued by the governments and regulators of the abovementioned countries. To analyse banking practices in France, the study looked at the questionnaires<sup>14</sup> sent by the ACP to eight major French- or foreign-owned banking institutions, all representative of the general and mutual banking sectors. A sample of 12 foreign banks was selected that encompassed the major systemically important banks mentioned in a Basel Committee study of 22 November 2010<sup>15</sup>. The analysis of compensation practices was conducted by reviewing disclosures in 2009 and 2010 annual reports and in other published documents<sup>16</sup>, as well as, more generally, on the basis of information provided on banks' websites.

The list of French and foreign laws and regulations examined during the course of the study is provided in Annex 2, while Annex 3 lists the French and foreign banks included in the review.

### 1. Compensation regulations and policies

#### 1.1 Transposition of FSB principles into French regulations

France was quick to bring its banking and financial regulations in line with the FSB's recommendations. The Order of 3 November 2009 “on the compensation of employees whose

11. G-SIFIs: Globally Systemically Important Financial Institutions.

12. The Financial Stability Forum (FSF) was replaced by the Financial Stability Board (FSB) at the G20 summit held in London on 2 April 2009.

13. Cf. synopsis of the FSB's principles and standards in Annex 1.

14. One qualitative and one statistical.

15. Basel Committee on Banking Supervision: “An assessment of methodology of systemic importance and a potential set of global systemically important banks” dated 22 November 2010. This study identifies 69 banks from around the world, by decreasing order of systemic importance. The 12 selected banks are in the list of the top 15 systemically important banks cited by the study (excluding French banks).

16. Including compensation reports, the charters of banks' internal committees and particularly the charters of compensation committees, proxy statements in the United States, which are voted on at general shareholders' meetings, and all other published documents.

activities could have an impact on the risk exposure of credit institutions and investment firms” amended Regulation 97-02 on the internal control of credit institutions and investment firms by introducing the FSB’s key principles and standards. The order, which was published in the Official Journal of 5 November 2009, was immediately applicable, so its provisions came into force in France at the end of 2009.

At that stage, France’s regulations were materially inconsistent with the FSB’s recommendations on just two points:

- Under Article 31-4, Regulation 97-02 covered senior executives and “employees who are financial market professionals”, whereas the FSB targets “senior executives as well as other employees whose actions have a material impact on the risk exposure of the firm”;
- Article 31-4.3 of Regulation 97-02 stated that “a significant fraction of compensation should be subject to performance requirements and paid on a deferred basis”, and Article 31-4.4 added that “a substantial portion of compensation may take the form of shares [...]”, whereas the FSB states that “a substantial portion of variable compensation, such as 40 to 60%, should be payable under deferral arrangements [...]” and “a substantial proportion, such as more than 50%, of variable compensation should be awarded in shares [...]”.

These differences were eliminated when European Directive 2010/76/EU of 24 November 2010 (CRD3)<sup>17</sup> was transposed into French law by an Order dated 13 December 2010, which further amended and clarified the obligations stipulated in

Regulation 97-02 in terms of compensation-related policies, controls and disclosures for employees whose actions may expose their institutions to material risk. In its most recent version<sup>18</sup>, Regulation 97-02 also introduced a principle of proportionality in Article 31-4, as provided for by CRD3<sup>19</sup> and in line with FSB principles taken up in the Supplemental Pillar 2 Guidance<sup>20</sup> issued by the Basel Committee in July 2009. Article 31-4 thus states that “[institutions should approach compensation policies] in a way and to the extent that is appropriate to their size, internal organisation and the nature, the scope and the complexity of their activities”. Thus far, this proportionality approach has not been translated into specific regulatory requirements in France.

## 1.2 Incorporation of FSB principles in foreign regulations

### 1.2.1 United Kingdom

In August 2009, the FSA<sup>21</sup> issued a new set of regulations designed to reform compensation practices in financial services. The new rules gave rise to a Remuneration Code, which was added to the FSA’s Handbook<sup>22</sup>. However, the UK’s proportionality approach meant that the new code applied only to 26 banks and other major financial institutions and, within those organisations, to about 4,300 individuals, i.e. directors, senior executives and top-paid managers and employees.

As far as the rest of the financial community was concerned, these provisions were intended as non-binding guidelines on sound practices. No disclosure requirements were set. Rather, the FSA stressed the overriding

17. Directive amending Directives 2006/48/EC and 2006/49/EC and adopting the FSB’s principles and standards as regards compensation in the financial sector.

18. Regulation 97-02 (amended), consolidated version as at 13 December 2010.

19. Cf. CRD3 Directive, Annex I.1.

20. Basel Committee on Banking Supervision: “Enhancements to the Basel II framework”, “Supplemental Pillar 2 Guidance”, IA6: “the detail and sophistication of a bank’s risk management programmes should be commensurate with the size and complexity of its business and the overall level of risk that the bank accepts. This guidance, therefore, should be applied to banks on a proportionate basis.”

21. Financial Services Authority.

22. The FSA’s Handbook sets out all the regulator’s rules and guidance.

importance of confidentiality as protection against competition.

When it transposed CRD3, the United Kingdom expanded and strengthened its own requirements, again using a mix of rules and guidance, but in a manner that ensured compliance with all the FSB's Principles for Sound Compensation Practices. The revision also provided an opportunity to introduce a requirement for affected institutions to disclose details of compensation policies. The United Kingdom maintained two principles of proportionality relating to:

- the scope of regulatory requirements, which is commensurate with the size and business of firms;
- the threshold below which the definition of "risk-taker"<sup>23</sup> does not apply (total compensation less than GBP 500,000 and variable compensation making up less than 33% of total compensation; any person above the threshold may therefore be assumed to be part of the population of risk-takers). The FSA estimates that around 2,500 firms are subject to its regulations, without specifying the number of firms subject to the most restrictive rules, or the number of individuals affected.

In February 2011, the UK government signed a formal agreement with the country's largest banks. Under the agreement, called Project Merlin, the government undertook to support the financial industry, in return for assurances from the sector that it would support the development of the domestic economy and reform variable compensation policies to make them more acceptable to public opinion.

## 1.2.2 Germany

In late 2009, Germany's regulator<sup>24</sup>, issued a circular laying the foundations for a regulatory framework designed to apply the FSB's Principles for Sound Compensation Practices – Implementation Standards. The circular also introduced a proportionality approach whereby the most restrictive rules on designing and disclosing variable compensation applied only to those firms that believed they were required to comply on the basis of a self-assessment.

Furthermore, eight major German banks undertook on 11 December 2009 to voluntarily comply forthwith with the G20 recommendations on variable compensation issued following the Pittsburgh summit. One of the eight published a narrative report lacking in detail about its 2009 compensation arrangements; but the other banks' annual reports showed that the new principles had indeed been taken into consideration, albeit to a degree that is hard to measure.

Germany then voted on new legislation in July 2010 and issued implementing decrees in October 2010, so achieving early transposition into German law of the CRD3 compensation provisions published in November 2010. The new legislation, which came into effect on the day following publication, incorporated most of BaFin's 2009 circular, which was repealed in parallel. As a result, Germany's regulations are now aligned with the FSB's compensation principles.

Germany maintained two principles of proportionality in its 2010 regulations. Banks and other financial institutions are subject merely to general principles of

23. This report uses the following terms interchangeably: risk-takers, controlled staff and Code Staff (the UK term).

24. BaFin: Bundesanstalt für Finanzdienstleistungsaufsicht.

restraint to ensure financial soundness. The more demanding provisions, such as the need to set up compensation committees, precise rules on awarding deferred and non-deferred variable compensation, and public disclosure requirements, apply only to:

- major institutions whose total assets exceed EUR 40 billion, or EUR 10 billion if the institution in question believes itself to be sufficiently major;
- within these institutions, only to senior managers and other risk-takers. The institution itself classifies employees in this regard, but must keep documentation about such classification.

### 1.2.3 Switzerland

In Switzerland, variable compensation in respect of 2009 and paid in 2010 was not subject to specific regulatory requirements, whether in terms of compensation policies or disclosure. Even so, the main Swiss banks said in their 2009 annual reports that they had brought their compensation policies into line with international standards as set out in the G20 Pittsburgh Summit Statement. One bank also published an annual report on compensation, which was mainly narrative in nature, with few statistics.

On 21 October 2009, FINMA, the Swiss regulator, published Circular 2010/1 on “Remuneration schemes: minimum standards for remuneration schemes of financial institutions” which was set to take effect on 1 January 2010. While all provisions had to be complied with by 1 January 2011, those concerning annual reporting on compensation policy applied to disclosures on compensation paid in 2011 in respect

of 2010. However, Switzerland did not transpose in full the FSB’s principles on the percentages of compensation that should be deferred and/or paid in shares (no minimum percentage required), on banning guaranteed deferred bonuses, and on the notion of “risk-takers”, which was mentioned but not clarified. Significantly, Circular 2010/1 introduced a principle of proportionality limiting the scope to institutions with equity capital of more than CHF 2 billion. As a result, just six banks and five insurers incorporated under Swiss law are affected. Unless otherwise required by FINMA, other institutions are asked to take the rules of Circular 2010/1 into account as best practice guidelines.

### 1.2.4 United States

Since the financial crisis of 2008, which followed on from the 2007 sub-prime crisis, the United States has been a forum for ongoing discussions about legal and regulatory changes, either to address emergency situations or to lay the groundwork for practices that are more commensurate with the risks taken by banks and other financial institutions.

As part of this, in 2008 the United States passed the TARP<sup>25</sup> Act, which provided financial support to banking and financial organisations. The law’s associated restrictions on senior executive compensation and disclosure requirements provided an incentive for institutions that received federal aid to exit the programme as quickly as possible.

From 2009 onwards, the Fed repeatedly made the point in proposed guidance, sometimes co-signed with other regulators, that

25. TARP – Troubled Asset Relief Program: Act passed on 3 October 2008 (also known as the Paulson Plan, after the then US Treasury Secretary Henry Paulson).

“banking organizations too often rewarded employees for increasing the firm’s short term revenue or profit without adequate recognition of the risks the employee’s activities posed for the firm. Importantly, problematic compensation practices were not limited to the most senior executives at financial firms. Compensation practices can incent employees at various levels of a banking organization, either individually or as a group, to undertake imprudent risks that can significantly and adversely affect the risk profile of the firm”<sup>26</sup>.

The Fed held a consultation in October 2009 on Proposed Guidance on Sound Incentive Compensation<sup>27</sup> Policies. The guidance, which was consistent with the FSB’s principles and standards, was based on three key principles for variable compensation, namely that such compensation should:

- not provide an incentive to take excessive risks;
- be compatible with effective controls and risk management;
- be supported by strong corporate governance.

However, the proposed guidance did not set minimum percentages for the portions of variable compensation paid on a deferred basis and/or in shares. Indeed, it went so far as to question the usefulness of such thresholds. At the same time, the Fed asked all banks to assess their variable compensation systems and promptly correct any deficiencies. In late 2009, it also began a review of compensation practices at large US banks and foreign banks operating in the United States. All this work led to the joint publication of final guidance<sup>28</sup> on 25 June 2010 by several federal

regulatory agencies with responsibility for the banking and insurance sectors. The final guidance, which is largely based on the proposed guidance issued eight months earlier, mentions that it is in line with the FSB’s Principles for Sound Compensation Practices and stresses its principle-based approach. It applies not only to senior executives but also to other employees who, either individually or as part of a group, have the ability to expose the banking organisation to material risk.

Against this backdrop, large US banks were vague in disclosures about their compensation policies in 2009. They all said that they had taken account of the FSB’s principles and standards. Annual reports and related documents indicate that US banks have certainly taken note of the changes in international standards on compensation. However, without quantitative data, it is impossible to measure the scope of people affected, the exact nature of the measures taken and the resulting changes.

The Dodd Frank Act, passed on 21 July, was the highlight of 2010. The result of a legislative process set in train immediately after the outbreak of the financial crisis, the act seeks to amend the regulatory framework for the delivery of financial services in the United States and coordinate the activities of the federal regulators in charge of supervising these services. The Act, which runs to about 900 pages, has around 1,000 sections, seven of which dealing specifically with compensation policies. As regards the sections requiring implementing measures, the SEC<sup>29</sup>, the Fed and other federal regulatory agencies are currently preparing the measures in

26. This phrase, or a version of it, appears several times in the 2009 proposed guidance, as well as in the final and supplementary guidance of 2010 and 2011.

27. In this report, the term “variable compensation” is synonymous with “incentive compensation” commonly used in US laws and regulations.

28. “Guidance on Sound Incentive Compensation Policies” published in the Federal Register on 25 June 2010.

their respective areas of jurisdiction. One of these<sup>30</sup>, which is co-signed by seven federal agencies, including the Fed, the FDIC<sup>31</sup> and the SEC, was put out to public consultation on 14 April 2011 for 45 days. Once it receives final approval, the new rule should replace the Guidance on Sound Incentive Compensation Policies of 25 June 2010. Like the Guidance of 25 June 2010, the new rule (it is a proposed rule rather than proposed guidance) does not cover all of the FSB's 2009 principles and standards. The most demanding obligations will apply to the largest institutions, and particularly to major banks with assets of over USD 50 billion<sup>32</sup>. At these institutions, the requirement to defer compensation applies only to senior executives, without specifics about proportions to be paid in shares or cash. On a more general note, there is no requirement to disclose quantitative information about risk-takers, the question of guaranteed bonuses is not tackled, and the principle of hedging variable compensation is not banned<sup>33</sup>. The proposed rule states explicitly that disclosure obligations are under the responsibility of the SEC, which has general jurisdiction in this area over listed companies, but not specifically over all financial institutions. The SEC is in the process of updating its regulations in this area to reflect the provisions of the Dodd Frank Act.

## **2. Banks' compensation practices**

### **2.1 Trends observed from 2010 compensation disclosures by foreign banks**

#### **2.1.1 United Kingdom**

UK banks have adjusted their

disclosures to meet the new regulations. Reporting on variable compensation policies, whether in annual reports or specific compensation reports, show that the policies apply to a broad population of managers, although it is not possible to measure the precise scope, since UK banks have opted to limit their regulated population or "Code Staff", i.e. the only people subject to disclosure requirements, to a small group of employees, selected essentially on the basis of their position in the chain of command. Thus, in the three banks included in the sample, Code Staff consisted of between 230 and 320 people out of total headcounts ranging from 147,000 to 295,000.

#### **2.1.2 Germany**

German banks, like their UK counterparts, have opted for a narrow definition of their regulated population. The compensation reports by banks included in the study reveal an obvious concern to ensure broad internal application of policies on deferred variable compensation paid partly in shares or equivalent instruments. However, again like UK banks, the regulated population subject to disclosure requirements is narrowed to some 200-300 people, when it is identified at all.

#### **2.1.3 Switzerland**

Since the Swiss regulator has not transposed all of the FSB's principles and standards, reporting by Switzerland's banks is incomplete with respect to the principles and standards, although it complies with domestic regulatory obligations. Still, a review of published statements reveals positive changes to variable

29. SEC: Securities and Exchange Commission.

30. A proposed rule, rather than guidance, on "Incentive-based Compensation Arrangements", co-signed by seven federal agencies, including the Fed and the FDIC (the insurance supervisor).

31. FDIC: Federal Deposit Insurance Corporation.

32. As regards banks under Fed supervision.

33. In the proposed rule, US regulators question the usefulness of reducing hedging options and ask for opinions in the consultation paper.

compensation policies, which clearly apply, once again, to a much wider internal population than the publicly identified group of “risk-takers”, which does not exceed 200 people and for which no quantitative information is provided on compensation or award and payment procedures.

Interestingly, one Swiss bank said in its compensation report that it had compared its regulated population with that determined by FSA rules. The bank found that under UK rules it had a population of just 100, compared with 200 under Swiss rules, and that the overlap between the two groups consisted of only 50 people.

#### 2.1.4 United States

US banks say they are committed to compensation policies that encourage growth in long-term revenue and profit and discourage imprudent risk-taking. It seems that the Fed’s monitoring of the compensation policies of large banking organisations since late 2009 has encouraged banks to bolster their corporate governance arrangements and introduce variable compensation policies that place considerable importance on deferral arrangements and on payment in shares and equivalent instruments. The term “risk-takers” is however nowhere to be found in the banks’ published documents, including the charters of their compensation committees, annual reports and proxy statements. US banks do not put out compensation reports, and the only quantitative information available relates to “named executive officers”, which consist of five or seven senior managers defined under SEC rules<sup>34</sup>. US banks stress that their first

concern is to attract and keep talent.

#### 2.1.5 Summary

An analysis of disclosures by banks in the other countries covered by the review points to the following broad trends.

Compensation policies got varying treatment in chairmen’s messages introducing banks’ annual reports. One-half of bank chairmen did not even mention the topic in their 2010 annual reports.

By contrast, there were repeated references to setting up compensation schemes that reward long-term performance, discourage imprudent risk-taking and preserve wage competitiveness.

Banks are effectively applying the regulations implemented as a result of CRD3 transposition in Europe. The same is true for Switzerland’s new regulations. However, reporting by American banks reflects the fact that US regulations lag behind in this area. US banks mainly report the bare minimum, and as far as disclosing quantitative data goes, they report solely on senior executive compensation, in keeping with their legal obligations.

In general, the term “risk-taker” does not appear in disclosures by banks in the sample, with the exception of Swiss banks and one US bank, although they do not provide quantitative data about “risk-takers” as they define them. UK banks prefer to use the term “Code Staff”<sup>35</sup> while German banks talk about “regulated employees”.

Similarly, all the banks in the sample restrict the regulated population to just 200-300 people, whereas they typically have total headcounts

34. SEC final rules on executive and director compensation disclosure issued on 11 August 2006 (<http://www.sec.gov/rules/final/2006/33-8732a.pdf>). Named executive officers are the principal executive officer, the principal financial officer, the three other most highly compensated executive officers and, where applicable, up to two senior managers who would have been on the list except for the fact that they were no longer serving as executive officers at the end of the fiscal year.

35. i.e. people that could incur material risk as defined by the Remuneration Code in the FSA Handbook.

ranging from 100,000 to around 300,000. In the United States, no quantitative data are available (except for one bank that reported that 470 people were subject to the same variable compensation arrangements).

In almost all banks in the sample, the concept of regulated population refers to a small group of top-level executives rather than “operational risk-takers”.

Statements made by banks concerning compensation policies also reveal that variable compensation and deferred bonuses paid in shares involve much wider groups than the regulated population alone. In other words, these two notions have become “uncorrelated”.

There are wide differences when it comes to defining “risk-takers”, whether or not this term is actually used (see comments on reporting by Swiss banks about the different effects of Swiss and UK regulations).

In all countries represented in the sample, banks that received public assistance demonstrated greater moderation in their senior executive compensation policies.

Fixed compensation percentages vary considerably from bank to bank<sup>36</sup>, though this information is not always available. In the United Kingdom, the fixed compensation of Code Staff at the large banks covered by the review ranged from 18 to 26% of total compensation, while the individual shares of executive committee members ranged from 2% to 45%. In Germany and Switzerland, where uniform information was available only for the compensation of the management board or executive committee, the

portion of fixed compensation ranged on average from 14% to 29%, with similar individual rates. In the United States, where banks reported only the individual compensation of named executive officers, the average portion of fixed compensation varied from 4.3% to 7% depending on the bank.

Variable compensation comes in different forms although the trend is towards deferred variable compensation in shares or equivalent instruments, with an effective vesting date that is different from the award date, and malus or clawback clauses.

A new form of variable compensation is emerging, namely Long Term Incentive Plans (LTIPs), whereby payment is deferred for three to five years and made conditional on achieving certain performance and return on equity (ROE) targets. Six out of the 12 banks in the sample have such plans, which they reserve for their most senior executives; final vesting is subject to certain requirements and malus or clawback provisions.

## 2.2 Compensation practices at French banks

French banks have clearly taken on-board the amendments to the regulations on compensation, as written into Regulation 97-02 amended by the Order of 13 December 2010 transposing CRD3.

Even so, France’s banks are not uniformly positioned in this area. Some disparities reflect cultural or size differences<sup>37</sup>; others stem from the fact that the six of the banks reviewed are French banks and are assessed as regards their global operations, whereas two of the banks

36. Except at banks that received financial aid from the government, where compensation is more restricted.

37. The statistical questionnaire asked about variable compensation in respect of 2009 and 2010. In practice, the detailed analysis covered only data pertaining to 2010, because the statistics for 2009 deal with a different population from that of 2010. At end-2009, the disclosure obligations of Regulation 97-02 (Article 43-1) applied to “financial market professionals whose activities have a material impact on the risk exposure of the firm” (banks typically reported all affected employees) whereas under the updated version of December 2010, the obligations apply to “persons whose professional activities have a material impact on the firm’s risk profile” (no reference to market professionals).

are subsidiaries of foreign-owned banks and are reviewed solely on the basis of their operations in France.

#### 2.2.1 Compensation as a percentage of net banking income

No clear trend emerges in this area.

The overall rate of compensation (fixed plus variable) ranged between 1.3 and 5.5% of net banking income, without a clear-cut trend by category.

Variable compensation accounted for less than 3% of net banking income at all banks in the sample.

For the most part, compensation's share and specifically variable compensation's share of net banking income does not look large enough to create problems for banks in terms of their ability to strengthen capital.

#### 2.2.2 Population of risk-takers

French banks have a broad vision of "persons whose activities could have an impact on the risk exposure of credit institutions and investment firms" (hereafter "risk-takers" or "regulated population"), as referred to both in Regulation 97-02 and in the FSB's 2009 principles and standards. France's major banks all identified about 3,500 people out of total headcounts of between 150,000 and 200,000. Risk-takers accounted for between 1% and 3.1% of the total headcount, except at one institution, which reported a lower rate. The firm in question is a subsidiary of a foreign bank and its lower rate is attributable to compliance with a group policy.

Employees receiving compensation of over EUR 1 million made up a small percentage of the regulated population, usually between 1.8% and 8.8%, with a wide spread of

rates within the range. The abovementioned institution was once again the exception, with a higher rate than the other banks (fewer risk-takers, but all at a more senior level or more highly compensated).

In comparison, major UK, Swiss and German banks identified 200 to 300 risk-takers, while US banks provided no data. In all these countries, published documents show that "risk-takers" are essentially top managers. By contrast, the review of compensation disclosures shows that French banks count people who may not have a material impact on risks individually, but who may contribute to a collective impact because of their involvement in a business deemed to be sensitive; these employees are said to be "regulated on a collective basis" by the banks.

Overall, French banks use a broad definition of "risk-takers", including in their disclosures, in contrast with major foreign banks, which offer far more narrow reporting on compensation policies.

#### 2.2.3 Distribution between fixed and variable compensation

2.2.3.1 Looking at controlled staff as a whole, the sample basically divided into three categories:

- institutions where the amount of variable compensation was lower than the amount of fixed compensation: the three firms in this category are primarily banks with a smaller corporate and investment banking (CIB) business or a separate CIB arm;
- institutions where the amount of variable compensation was between one and two times greater

than the amount of fixed compensation: the majority of banks in the sample (four) fell into this category;

- one institution (the exception previously mentioned above) where variable compensation was 4.5 times greater than fixed compensation, owing to the larger proportion of risk-takers earning over EUR 1 million.

#### 2.2.3.2 An analysis of sub-categories of the main population reveals more diverse patterns:

- executive committee<sup>38</sup>: the share of variable compensation in total compensation (fixed + variable) of the executive committee overall varies widely from bank to bank, ranging from 11.7% to 78.7%<sup>39</sup>, including six institutions in a range of 68% to 78.7%. Conversely, fixed compensation amounted to between 21.3% and 88.8% of total compensation, including six institutions in a range of 21.3% to 32%;
- the share of fixed compensation of individual senior executives was never lower than 22.5% and went as high as 64% (aside from the exception mentioned in footnote 39);
- front office: the share of variable compensation in total compensation (fixed + variable) paid to front office staff varied between 41.9% and 67% at six of the eight banks, of which four posted ratios in excess of 60%. The two remaining banks were at opposing ends of the scale: one reported a lower rate (smaller front office compared with the other banks), while the second had a higher rate (exception as mentioned above, for the same reasons).

In other words, banks are not all taking the same approach to

interpreting the “appropriate split between fixed and variable compensation” mentioned in Article 31-2 of Regulation 97-02. Not including the one exception, however, variable compensation paid to all categories in the regulated population<sup>40</sup> was always less than twice total fixed compensation. Put another way, on average, **fixed compensation at French banks makes up between one- and two-thirds of the total compensation of the regulated population.**

A comparison with the foreign banks considered in this study is complicated by the fact that their regulated populations are narrower than those reported by French banks and are chiefly made up of senior management. Even so, at the 12 foreign banks analysed, the fixed compensation of controlled staff, where data were available, ranged between 18 and 26% of total compensation (UK), whereas 33% marked the low end of the range in France. Average fixed compensation of members of management boards, executive and equivalent committees<sup>41</sup> varied between 4% and 29% depending on the bank and the country. By contrast, it was never lower than 21.3% in France. Furthermore, the individual fixed compensation of foreign senior executives was in a range of 2.3% to 44.4% whereas the individual fixed compensation of French senior executives was not lower than 22.5%.

#### 2.2.4 Malus and clawback<sup>42</sup> practices

All the banks in the sample say that they have introduced malus policies for situations where targets are not reached. Targets differ depending on the category of staff, with senior directors being assigned targets based on overall earnings (operating income, net income, ROE), and

38. Senior managers within the meaning of Article 4a of Regulation 97-02 (executive body) and other members of the executive committee.

39. With the exception of one bank that did not pay any variable compensation.

40. Executive committee, as well as front office, control and other staff.

41. “Named executive officers” in the United States.

42. A malus is a reduction in the amount paid, whereas a clawback is a request to return amounts already paid or non-payment of vested but as yet undistributed sums.

“operational risk-takers” being given targets based more closely on the results of their individual units. Except in the case of the largest banks, the responses were less precise on how banks treat capital and liquidity consumption and the effective cost of risks incurred when assessing employee performance. These aspects are however mentioned in broad terms as an integral part of compensation policies.

Overall, although malus clauses are duly applied in the event that targets are not met, it is important to ensure that the targets themselves are not set at levels that are too easily reached.

Clawbacks are applied only to new hires that leave the employer before completing a full year of work. It is unclear whether clawbacks are applied in cases of professional or ethical breaches, or whether only malus clauses are used.

#### 2.2.5 Deferred compensation as a percentage of total variable compensation

Aside from one institution with a small CIB business, the deferred share of variable compensation ranged between 41.3% and 57.6% at all banks, rising to 72.9% in one instance.

Overall, banks therefore complied with the regulatory minimum requirement, which is that 40% of variable compensation should be paid under deferral arrangements.

#### 2.2.6 Compensation in shares or equivalent instruments as a percentage of total variable compensation

There were three outliers in this area: at two banks, the percentage of compensation paid in shares relative to total variable compensation was between 28.9% and 34.7% while at

a third bank, the share was 71.4%. The first two banks said that they applied a special compensation policy to risk-takers whose variable compensation is lower than EUR 100,000. This compensation is paid exclusively in cash although it may be partly deferred and indexed to the share price. These staff are chiefly employees who incur risks as part of a group (see point 2.2.2 above). Other individual risk-takers receiving higher amounts of variable compensation are paid at least 50% of their variable compensation, whether deferred or not, in shares or equivalent financial instruments.

At all other banks, compensation paid in shares accounted for between 41.3% and 51.2% of variable compensation. **The overall percentage** of compensation paid in shares and equivalent instruments is probably pulled down by the banks’ broad definition of risk-takers, coupled with compensation policies similar to those reported by the two exceptions mentioned above.

In all, while most of the banks are close to the 50% regulatory threshold, only three institutions actually reached the target of having at least half their variable compensation paid in shares or equivalent instruments. However, this overall finding needs to be put in perspective, and it would be useful to break it down by staff category.

#### 2.2.7 Guaranteed bonuses

Employees who received guaranteed bonuses accounted for less than 2% of the population of risk-takers in five banks, and between 7.1% and 7.3% at the three other banks.

The latter group of banks attributed these high rates to a wave of resignations by high-ranking

employees, notably from their London, New York and Hong Kong operations, or in one specific market business line. These departures required recruitments in the same category, where the practice is to offer guaranteed bonuses. The three banks stressed, however, that these bonuses were only guaranteed in the first year and were subject to partial, index-linked, deferral arrangements.

As a percentage of total variable compensation, guaranteed bonuses accounted for less than 4.3% at all banks, aside from the three exceptions described above, where they were in a range of 10.8% to 14.9%. Given the size of the guaranteed bonuses at these three banks, further review should be conducted, over and above the brief supplementary explanations obtained from the institutions.

Be that as it may, it appears that the practice of paying guaranteed bonuses is linked to the location of banks' activities and may be an external constraint for businesses conducted in foreign financial centres that do not comply with the same obligations as those imposed in France.

#### 2.2.8 Senior executive compensation

A special review was conducted of the overall individual compensation awarded to senior executives. Out of the eight banks, and aside from a few instances of lower compensation, the compensation of senior executives ranged between EUR 0.7 million and EUR 3.8 million. These figures do not include deferred compensation awarded in early 2011, which is not included in reported compensation for 2010.

These amounts are well below the compensation paid to the senior

executives of the large foreign banks analysed in the context of this study, aside from those that ran into serious financial difficulties and received government support. Compensation of chief executive officers at these foreign banks ran from EUR 2.2 million to EUR 13.6 million (or equivalent in other currencies), although EUR 2.2 million was the exception, with compensation mostly in the EUR 7-10 million range.

#### 2.2.9 Summary

A review of the questionnaires completed by French banks reveals that:

- on the whole, French banks have taken proper account of the new regulations as set out in Regulation 97-02, which transposed all the FSB's principles and standards, including the quantitative criteria of standards 6 to 9, which many non-EU countries<sup>43</sup> prefer to treat as guidelines, rather than mandatory thresholds;
- although broader than in other countries studied, the definition of what constitutes a "risk-taker" still varies from bank to bank. At seven banks, i.e. with one exception, the regulated population makes up between 1% and 3% of total headcount;
- there is room for improvement in the following areas:
  - explanations for policies on ex ante risk measurement and ex post performance assessment for the award of variable compensation,
  - the share of variable compensation paid in shares or equivalent financial instruments,
  - malus practices,
  - compliance with restrictions on awards of guaranteed bonuses.

43. In the EU, the CRD3 makes it mandatory for "risk-takers" to comply with these criteria.

### 3. Conclusion

French banks' compensation policies cannot be analysed separately from those of banks in other major financial centres. All the banks considered in the study say in their disclosures that incentivising compensation policies and practices need to be put in place to discourage excessive risk-taking and reward long-term performance, while preserving competitiveness on a fiercely contested international and domestic job market. Foreign regulators stress the same points in the recitals of their regulations. Accordingly, there is a need for shared understanding of, and support for, implementation of the Principles for Sound Compensation Practices issued by the Financial Stability Board, which seek to address a root cause of the 2007-2008 financial crisis, as well as the scale of the associated problems. Otherwise, long-term competitive distortions could be created between major financial centres, which would inevitably reduce efficiency.

In a fast-changing global financial sector, nothing is permanent, and the principles and standards themselves may evolve. Even so, if they are to be effectively and smoothly implemented, the main countries need to reach clear agreement on four key ideas:

- the precise definition of “material risk-takers” “whose activities have a material impact on the risk exposure of the firm<sup>44</sup>”. The principles and standards are silent on this point, and regulators have given banks considerable latitude to come up with their own interpretations;
- countries differ considerably in terms of whether they view standards 6 to 9 (minimum thresholds for deferred compensation, payable or not in

shares over a minimum period of three years, malus and clawback clauses), as binding standards or mere guidelines, which is undermining the effective implementation of the FSB's principles and standards;

- the desired level of disclosure on compensation policies that comply with the FSB's principles and standards. Some countries are avoiding or dragging their heels in this regard, others are limiting the scope of reporting, while others still are calling for greater transparency. These differences put banks on an uneven footing and favour the protectionist stance of the least stringent countries;
- some countries are using other domestic legislation, notably labour laws, as an excuse for not implementing some of the FSB's principles and standards; a common response is needed to this situation.

Finally, the FSB's principles and standards say that banks should conduct ex ante analyses of all potential risks when determining their overall budgets for variable compensation, and ex post performance measurements when awarding this compensation. This is a complex subject that many banks have yet to tackle fully. Building on the Basel Committee's May 2011 report, “Range of methodologies for risk and performance alignment of compensation”, which provides tangible responses in this area, regulators and banks need to dialogue on this issue, which is a prerequisite for introducing sound compensation practices.

44. As mentioned in the implementation standards for the FSB principles.

## Annex 1

### Synopsis of FSB principles and standards

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#### Effective governance of compensation

**P1 Board of directors must actively oversee compensation systems**

**P2 Regular review by Board of directors**

S1 SIFI's should have a Board Remuneration Committee: competent and independent / risk committee / FSB P&S / annual review

**P3 Staff in control functions must be independent, endowed with authority and independent compensation**

S2 Employees in risk and compliance functions: adequate remuneration / performance based on the achievement of the objectives of their functions

#### Effective alignment of compensation with prudent risk-taking

**P4 *Ex ante* risk adjustment:** compensation must be adjusted for all types of risks

S3 Variable compensation consistent with sound capital base

S4 Variable compensation should take into account full range of risks, in particular capital and liquidity

**P5 Alignment of compensation with performance:** bonus pool linked to overall performance

S5 Negative financial performance should lead to contraction of compensation

**P6 Compensation structures and *ex post* performance adjustment:** time horizon of risks

S6 Remuneration mainly variable, individual based and deferred (40% to 60%)

S7 Deferral period  $\geq 3$  years and vesting no faster than on a pro rata basis

- P7 Compensation structures and ex post performance adjustment:** mix of cash / equity consistent with risk alignment and other features of compensation systems
- S8  $\geq 50\%$  of variable compensation awarded in shares / share-linked instruments
- S9 Remaining portion of the deferred compensation can be paid as cash vesting gradually, unvested portions are to be clawed back
- S11 Guaranteed bonuses are forbidden except: new staff hired or first year only
- S12 Contractual payments related to termination of employment should be re-examined
- S14 Hedging strategies / insurance are forbidden

#### Effective supervisory oversight and engagement by stakeholders

- P8 Supervisory review should be rigorous and sustained**
- S10 In case of government intervention, supervisors can restructure compensation schemes
- S13 Significant financial institutions should comply with the FSB P&S
- S16 Supervisors ensure effective implementation of FSB P&S
- S17 Supervisors require firms to demonstrate risk, capital and liquidity compliance
- S18 Supervisors can take remedial action or corrective measures
- S19 Supervisors need to coordinate internationally to ensure harmonised implementation
- P9 Disclosure: firms must disclose clear, comprehensive and timely information**
- S15 Disclosure: annual report on compensation with details on decision making process / design characteristics / aggregate quantitative information

## Annex 2

### List of laws and regulations governing compensation schemes in the banking sector<sup>45</sup>

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#### France

- Banking and Financial Regulation Act 2010-1249 of 22 October 2010;
- CRBF Regulation 97-02 on internal control amended by:
  - the Order of 3 November 2009 on the compensation of employees whose activities could have an impact on the risk exposure of credit institutions and investment firms,
  - the Order of 13 December 2010 on the compensation of employees whose activities could have an impact on the risk exposure of credit institutions and investment firms.

#### International organisations

- FSB Principles for Sound Compensation Practices, 2 April 2009;
- FSB Principles for Sound Compensation Practices – Implementation Standards, 25 September 2009;
- Basel Committee Document: Enhancements to the Basel II framework, July 2009;
- European Directive 2010/76/EU of 24 November 2010 on the supervisory review of remuneration policies.

#### United Kingdom

- Documents published by the Financial Services Authority (FSA):
  - CP<sup>46</sup>09/10: Reforming remuneration practices in financial services, March 2009,
  - PS<sup>47</sup>09/15: Reforming remuneration practices in financial services, Feedback on CP 09/10 and final rules, August 2009,
  - CP 10/19: Revising the remuneration code, July 2010,
  - PS 10/20: Revising the remuneration code, Feedback on CP 10/19 and final rules, December 2010,
  - PS 10/21: Implementing CRD3 requirements on the disclosure of remuneration, Feedback on CP 10/27 and final rules, December 2010;
- FSA Handbook online at <http://FSAhandbook.info/FSA/html/handbook>:
  - section on remuneration: SYSC Senior management, arrangements, systems and controls, Part 19A: Remuneration code,
  - section on disclosures requiring specific treatment under Pillar III of the Basel II Accord: BIPRU, 11 .5.18. Disclosures: Remuneration.

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45. Some legislation includes specific sections dealing with the insurance sector, which are not included in this list. 48. CP : « Consultation Paper ».

46. CP: Consultation Paper.

47. PS: Policy Statement.

## Germany

- BaFin Regulation on minimum requirements for risk management for banks and financial services institutions (MARISK), 14 August 2009;
- BaFin Circular 22/2009 (BA): Supervisory Requirements for Institutions' Remuneration Systems, 21 December 2009;
- Cover Letter for BaFin Circular 22/2009, 21 December 2009;
- Federal Act of 21 July 2010, *Gesetz über die aufsichtsrechtlichen Anforderungen an die Vergütungssysteme von Instituten und Versicherungsunternehmen* (Requirement concerning the legal supervision of remuneration systems of [financial] institutions and insurance companies);
- Implementing decree of Federal Act of 12 October 2010 ("*Instituts - VergV*") in the banking sector.

## Switzerland

- FINMA Circular 2010/1: Remuneration Schemes, 21 October 2009;
- FINMA Circular: Key Points, 11 November 2009;
- Press Release of 19 January 2011, FINMA Circular on Remuneration Schemes: transition period for implementation ends; some evidence of progress being made;
- FINMA Newsletter No. 20, 19 January 2011:
  - Guidance for Institutions Subject to FINMA Circular 2010/01 on Disclosures under Principle 9 of the Circular,
  - Guidance for these Institutions and their External Auditors regarding Report due to FINMA 30 April 2011;
- FINMA website: [www.finma.ch](http://www.finma.ch)

## United States

- Proposed Guidance on Sound Incentive Compensation Policies published by the Fed on 27 October 2009;
- SEC Final Rule: Proxy disclosure enhancements, 16 December 2009;
- Guidance on Sound Incentive Compensation Policies published jointly by the Department of the Treasury – Office of the Comptroller of the Currency (OCC), the Fed, the Federal Deposit Insurance Corporation (FDIC) and the Department of the Treasury – Office of Thrift Supervision (OTS). Date of publication in the Federal Register: 25 June 2010;
- Dodd Frank Act, Title IX: Investor protections and improvements to the regulation of securities, Subtitle E: Accountability and executive compensation, 21 July 2010;
- FDIC Proposed Rule: Incentive-Based Compensation Arrangements, 4 February 2011;
- SEC Proposed Rule: Listing Standards for Compensation Committees (section 952), 6 April 2011;

- Incentive-Based Compensation Arrangements issued jointly by the Department of the Treasury – Office of the Comptroller of the Currency (OCC), the Fed, the Federal Deposit Insurance Corporation (FDIC), the Department of the Treasury – Office of Thrift Supervision (OTS), the National Credit Union Administration and the SEC (section 956). Date of publication in the Federal Register: 14 April 2011;
- SEC website: [www.sec.gov](http://www.sec.gov)
- Federal Register website: [www.gpoaccess.gov/fr](http://www.gpoaccess.gov/fr)
- Fed website: [www.federalreserve.gov/](http://www.federalreserve.gov/)

### **Banks**

Websites of banks whose compensation disclosure policies were analysed as part of this report:

- United Kingdom:
  - Royal Bank of Scotland, HSBC and Barclays;
- Germany:
  - Deutsche Bank, Commerzbank, DZ Bank and Hypovereinsbank;
- Switzerland:
  - Crédit Suisse and UBS;
- United States:
  - Bank of America, Citigroup, JP Morgan Chase, Goldman Sachs and Morgan Stanley.

## Annex 3

### List of French and foreign banks covered by the study

- France:
  - BNPP,
  - Société Générale,
  - Crédit Agricole,
  - Crédit Mutuel (CM5CIC),
  - BPCE (excl. NATIXIS),
  - NATIXIS,
  - DEXIA Crédit Local,
  - HSBC France;
- United Kingdom:
  - Royal Bank of Scotland,
  - HSBC,
  - Barclays;
- Germany:
  - Deutsche Bank,
  - Commerzbank,
  - DZ Bank (additional inclusion),
  - Hypovereinsbank (additional inclusion);
- Switzerland:
  - Crédit Suisse,
  - UBS;
- United States:
  - Bank of America,
  - Citigroup,
  - JP Morgan Chase,
  - Goldman Sachs,
  - Morgan Stanley.



ISSN: 2112-7891  
Editor: Danièle Nouy  
Produced by: ACP Communication Unit