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**MINISTER FOR BUSINESS AND
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Danish response to the European Commission's Consultation on the Green paper on the long-term financing of the European economy

Denmark welcomes the Commission's Green Paper on the long-term financing of the European economy and the Commission's aim to start a broad debate on how to address the challenges associated with financing long-term investment needs by governments and companies.

Denmark supports many of the ideas in the Green Paper, and we particularly find it positive that the Commission focuses on alternative financing sources, developing the venture capital market and creating securitization instruments for small and medium-sized enterprises (SMEs).

If the Commission proceeds with its thoughts on harmonizing the framework for covered bonds, it is essential to take into account the proven stability of such systems which should not be undermined by a totally harmonized solution with a less prudent starting point. The Danish model for covered bonds (Danish mortgage covered bonds - "realkredit") has proven to be stable during the financial crisis providing sufficient funding to the real economy in difficult times and is thus an important example of long-term stable financing. Please, refer to our answer to question number 13 in this regard.

Although Denmark recognizes the role of life insurance companies and pension funds in providing long-term financing, we find that any initiative in this regard should take into account the insurance policy holder protection. Please, refer to our answer to question number 7 for further details in this regard.

Financial regulation in the aftermath of the financial crisis has been extensive and an impact analysis on the overall impact could be relevant, including how the initiatives in the Green Paper could potentially balance some of the negative consequences for long-term financing of the financial regulation. Denmark would suggest that the Commission in collaboration with the three European Supervisory Authorities initiates an in-depth impact assessment. In this respect, we find the work of EIOPA as

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initiated by the Commission on the rethinking of risk assessments on long-term investments an important task.

In general, several governments have already taken initiatives to address the challenges mentioned in the Green Paper. Denmark finds that EU initiatives should take into account existing national initiatives and make sure that they can still have an impact.

Danish answers to selected questions in the Green Paper

7) How can prudential objectives and the desire to support long-term financing best be balanced in the design and implementation of the respective prudential rules for insurers, reinsurers and pension funds, such as IORPs?

As mentioned above, although Denmark recognizes the role of life insurance companies and pension funds in providing long-term financing, we find that any initiatives in this regard should take into account the importance of insurance policy holder protection. This means that the companies should hold an adequate level of capital to remain healthy and to balance the high return and risk profile associated with long-term investments.

In Denmark, the Danish FSA has noticed that the pension funds increasingly invest in long-term investments such as infrastructure. In order to balance prudential objectives and the desire to support long-term financing, the Danish FSA has requested the companies to describe the treatment of investments in “alternative assets”. Investments in alternative assets typically give a higher return, because the company accepts to hold the assets over the long-term and therefore is compensated for the lack of liquidity as compared to short-term assets. The Danish FSA has communicated its expectation that the board of supervisors in each company have to take responsibility regarding the valuation and risk assessment of investments in alternative assets.

13) What are pros and cons of developing a more harmonized framework for covered bonds? What elements could compose this framework?

Denmark does not see the need for a fully fledged harmonized framework for covered bonds, since the diversity in markets and local systems have to be reflected in the regulatory framework. The Danish model for covered bonds (Danish mortgage covered bonds - “realkredit”) has proven to be stable during the financial crisis providing sufficient funding to the real economy in difficult times and is thus an important example of long-term stable financing.

If the Commission proceeds with its thoughts on harmonizing the framework for covered bonds, it is essential to take into account the proven

stability of such systems which should not be undermined by a total harmonized solution with less prudent starting point. Furthermore, the review clauses built into CRD4/CRR in relation to covered bonds and private initiatives such as “Labeling of Covered Bonds” by the European Covered Bond Council should be awaited before further regulation should be pursued here.

20) To what extent do you consider that the use of fair value accounting principles has led to short-termism in investor behavior? What alternatives or other ways to compensate for such effects could be suggested?

The experience from Denmark is that the use of fair value accounting principles has not led to short-termism in investor behavior. On the contrary, the experience is that the use of fair value accounting principles in life insurance companies and pension funds with long-term obligations means that the companies invest in assets with a similar long-term horizon in order to match the volatility on the assets and liabilities. Based on this experience, we find that fair value accounting could encourage long-term investments in the life insurance companies and pension funds and therefore could be an important remedy in this respect. It should be noted that the same experience is observed in Denmark in terms of non-financial companies.

21) What kind of incentives could help promote better long-term shareholder engagement?

Denmark welcomes the intention to enhance the transparency surrounding corporate governance and shareholder engagement. In order to promote better long-term shareholder engagement, it could be considered whether the establishment of an independent forum could have the intended impact. The independent forum should formulate guidelines for shareholders, including for their shareholder engagement, because corporate governance is aimed at the company as an organization rather than the investors.

25) Is there a need to develop specific long-term benchmarks?

Denmark shares the view that benchmarks and in particular the development of long-term benchmarks could serve as a means to assist long-term investors.

26) What further steps could be envisaged, in terms of EU regulation or other reforms, to facilitate SME access to alternative sources of finance?

In Denmark, new legislation is being prepared with the aim to improve the banks’ opportunities to securitize corporate loans. The aim of this scheme is to make it easier for banks to provide funding for Danish firms and in particular Danish SMEs. At the same time, new legislation is being prepared aiming at creating a firm legal basis for the use of representa-

tives (trustees) on Danish bond issues meant to make the corporate bonds market more accessible, also for others than the largest companies.

The new pieces of legislation involve very specific changes and modifications to the existing Danish legal framework, and it should be noted that there can be difficulties in developing EU-regulation in this field on a one-size-fits-all basis. EU regulation, if adopted, should strive to take into account the legal framework of the individual Member States. Total harmonization is not advised as it could potentially hinder the development due to uncertainty and too much administrative hassle.

27) How could securitisation instruments for SMEs be designed? What are the best ways to use securitisation in order to mobilize financial intermediaries' capital for additional lending/investments to SMEs?

It is important to keep in mind that banks know the SMEs best. As such, banks deal with SMEs on an everyday basis and have the best conditions for making a valid credit analysis. Therefore, SME financing schemes should take into account the knowledge of the SMEs nested in the banks.

In Denmark, a new model for securitisation of corporate loans will provide Danish banks with an opportunity to gain liquidity and in some cases also capital relief when securitizing corporate loans. The Danish model is inspired by the German refinancing register, but adapted to fit Danish circumstances and legal framework. The model will enable large investors such as pension funds to buy corporate credit risk via the banks, also from smaller firms, and thus stimulate new funding to SMEs.

28) Would there be merit in creating a fully separate and distinct approach for SME markets? How and by whom could a market be developed for SMEs, including for securitised products specifically designed for SMEs' financing needs?

The Danish starting point is that products can be traded on traditional market places. In Denmark, the Copenhagen Stock Exchange - Nasdaq OMX - in December 2012 opened up a new alternative market place for issuing corporate bonds called the First North bond market. This more lightly regulated market place could help facilitate more bond issues going forward from a wider range of companies than we have seen so far. It is expected that the new legislation regarding the use of representatives (trustees) for bond issues mentioned above will help facilitate the development of this alternative market place.

29) Would an EU regulatory framework help or hinder the development of this alternative non-bank sources of finance for SMEs? What reforms could help support their continued growth?

From a Danish standpoint, we welcome new initiatives from the Commission, such as the work towards creating a European framework for issuing corporate bonds for SME's.

However, it should be noted that there can be difficulties in developing EU regulation in this field on a one-size-fits-all basis. EU regulation, if adopted, should strive to take into account the legal framework of the individual member states.

Yours sincerely,

Annette Vilhelmsen