

Comments on EBA's Draft regulatory technical standards "On the treatment of equity exposures under the IRB Approach under Article 495(3) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR)" [EBA/CP/2014/06]

Submission from the EBA Banking Stakeholder Group

Under Article 495(3) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR), competent authorities are given power to temporarily exempt from internal ratings-based treatment certain equity exposures held by institutions as at 31 December, 2007. The CRR imposes specific conditions on competent authorities that must be met for the exemption to be granted. The purpose of this RTS is to establish the necessary conditions.

General comments

This RTS establishes certain conditions under which some member states can continue applying a waiver on the use of the IRB approach for certain equity exposures. The BSG welcomes the development of regulatory technical standards that contribute to the harmonization of prudential regulation. However, this draft RTS basically proposes maintaining the *status quo* as at the end of 2007, without more elaborate analysis on whether the above mentioned exceptions (which imply a less demanding treatment) were granted. As such, it does not imply any significant progress towards convergence in prudential rules. A more ambitious approach could be followed instead of simply "grandfathering" this treatment (although admittedly only until the end of 2017). For example, and in the interests of transparency, certain disclosure requirements for the portfolios benefiting from this favorable treatment could be considered, .

In order to smooth the transition from Basel I to Basel II, at a time when it was common practice for banks in some jurisdictions to maintain relevant portfolios of industrial holdings, CRD I included an exemption from the IRB treatment, and the application of the less demanding standard method for equity portfolios, that had to be granted by national competent authorities on a fully discretionary basis. The exercise of this national discretion gave rise to competitive distortions between

banks using internal models, as some national competent authorities applied the exemption to institutions under their supervision whilst others did not¹.

Maintaining the *status quo* of those equity portfolios that benefit from lower capital requirements does not imply progress towards the desired harmonisation of capital requirements in the EU. Nevertheless, there are two factors that limit the possible impact of this exception: (i) the fact that the volume of shares in the portfolios that could benefit from this better treatment have a very restricted ability to increase over time but; on the contrary, they tend to decrease steadily as positions are sold or mature, and (ii) the temporary nature of this exemption, that expires on 31 December 2017. Furthermore, the results of the survey conducted by EBA suggest that the impact of any proposed change would be immaterial in most institutions. Although the conclusion seems warranted for most institutions, according to the figures provided by EBA, it could be more important for some entities, as Figure 1 of the draft shows, where maximum values are material. As disclosed capital ratios are affected by criteria used for capital requirements, it would be misleading to compare entities applying different criteria.

Some of the justifications provided in the draft for maintaining the *status quo* are relevant, such as the fact that it provides continuity with the former legislative framework and that the power to harmonize has limited potential since the empowerment to competent authorities to grant the exemption has already been introduced in the CRR.

Nevertheless, we consider that as the CRR, differently from CRD I, narrows the freedom of competent authorities and imposes specific conditions to be met, it could be useful to require, as additional criteria to the one considered in the draft, that institutions disclose in their Pillar III information on equity portfolios that are benefiting from this exemption from the IRB treatment provided for in Article 495 of CRR. This would increase transparency (thereby facilitating investors' assessment and comparability of capital ratios) while at the same time preserving the legitimate expectations of the institutions which were, under the former regime, granted the exemption.

Regarding the suggestion to require disclosure as an additional criterion to the one considered in this submission, BSG member Sandra Hafner (EAPB) holds the opinion that this additional requirement is neither necessary nor warranted. According to Art. 452 part c (v) of EU 575/2013, the treatment

¹ The information disclosed in the EBA website on the application of this national discretion shows that it is being applied differently in different Member States

of equity exposures in the IRB approach is already subject to disclosure. The mandate given to EBA in Art. 495 para 3 of EU 575/2013 addresses the conditions according to which competent authorities shall afford the exemption and not the obligation for disclosure. In addition, the exercise of the national discretion in Art. 495 para 1 of EU 575/2013 is subject to supervisory disclosure by the competent authority."

Submitted on behalf of the Banking Stakeholder Group

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