

The graphic on the left side of the slide features a vertical orange bar. To its left, there are stylized blue and white patterns, including a large five-pointed star and a series of vertical lines that resemble a stylized 'E' or a series of columns. The background of the entire slide is a dark blue gradient.

EBA

EBA Consultation Paper on
draft RTS on own funds

Public hearing
14 June 2012

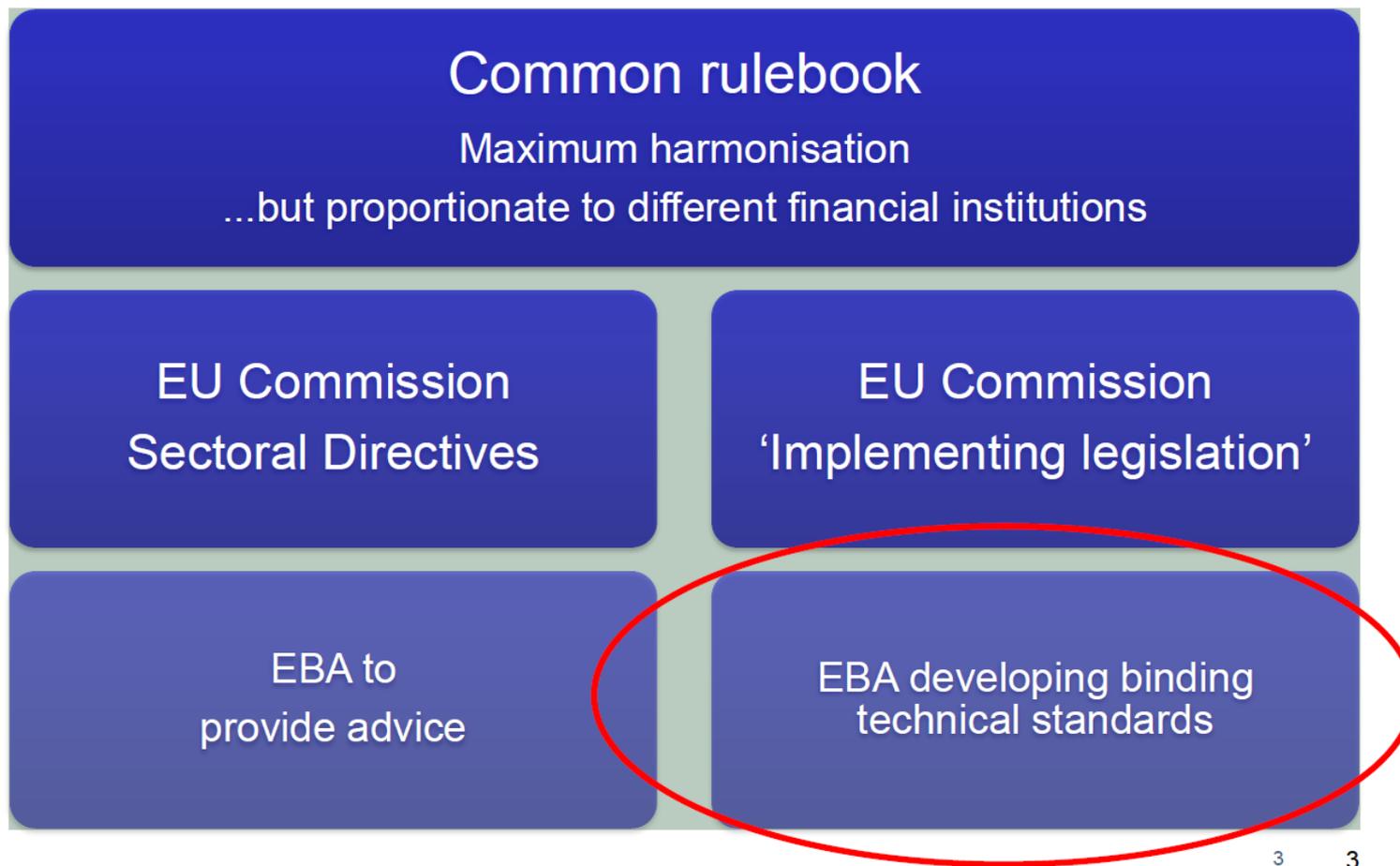
European
Banking
Authority

European System of Financial Supervision

Agenda

- **Background - EBA tasks** : mandate to develop regulatory technical standards - focus on own funds
- **List of RTS on own funds published** on 4 April
- **A few specific RTS on:** Instruments, deductions, cooperatives, general requirements/other aspects
- **Draft ITS on disclosure** for own funds by institutions
- **Next steps and timeline**

Background – EBA tasks



Background – EBA tasks

- Commission legislative package to strengthen the regulation of the banking sector and the proposal replaces the current Capital Requirements Directives (2006/48 and 2006/49) with a Directive and a Regulation
- New proposals on capital requirements (CRR / CRDIV) was published on 20 July 2011
- The proposal includes a substantial number of responsibilities/tasks to be delivered by the EBA within tight deadlines. Tasks include amongst others drafting 100+ Binding Technical Standards and 20 guidelines
- Presidency compromise texts published on 9 January 2012, 1 March 2012, 2 and 27 April 2012, 11 May 2012

Background – EBA tasks - BTS

- Development of the draft BTS by a Project Team (standing committee, working group or other internal body identified in the EBA) with the support/lead of EBA Staff (policy and legal experts)
- Cost-benefit and Impact Assessment analysis of proposals (unless where inappropriate or disproportionate, e.g. in cases of externally imposed deadlines) to be carried out according to EU standards
- Adoption of draft proposals by the Board of Supervisors according to its rules of procedures
- Public consultation and consultation of the BSG
- Feedback process and updating of the proposal
- Adoption of the draft RTS, publication and submission to the Commission

Background – EBA tasks – BTS on own funds

- Draft RTS on own funds to be delivered for the vast majority before 01/01/2013 to EU Comm by EBA based on the EU Comm original proposal
- 1st set of RTS published on 4 April 2012 (3 months consultation) – 14 single standards grouped together for consistency reasons
- Proposed standards to cover all areas of own funds, from features for instruments of the highest quality (Common Equity Tier 1 instruments) to instruments of a lower quality (Tier 2 instruments)
- End of consultation period = 4 July 2012

Background – EBA tasks – BTS on own funds

- Structure of the draft RTS following the structure of the CRR – appropriate references to the legal basis included
- Various provisions of the draft technical standards contributing to increase the permanence of capital instruments through specifications of features of the instruments and specifications of provisions in relation with the supervisory consent for reducing own funds.
- Draft standards to increase the loss absorbency features of hybrid instruments.

List of RTS published on 4 April

RTS published for consultation in April (14 RTS)

➤ RTS related to instruments

- Article 26(3) - Applicable forms and nature of indirect funding of capital instruments + distributable items
- Article 49(2) – incentives to redeem, trigger events, write-downs/write-ups, features of instruments that could hinder the recapitalisation of the institution, use of SPEs for indirect issuance of own funds instruments
- Article 78(2) - Qualifying Additional Tier 1 and Tier 2 capital issued by a SPE

➤ RTS related to deductions

- Article 24(3) – foreseeable charge or dividend

List of RTS published on 4 April

- Article 33(2) – deductions = losses of the current financial year, DTAs relying on future profitability, defined benefit pension fund assets, foreseeable tax charges, types of capital instrument of financial institutions, insurance and reinsurance undertakings to be deducted from own funds
- Article 38(2) - Deduction of defined benefit pension fund assets
- Article 71(3) - Indirect holdings arising from index holdings

➤ **RTS related to cooperatives**

- Article 46(5) – cooperative networks, exemption from, and alternatives to, deduction where consolidation is applied
- Article 25(2) point b) – cooperatives/mutuals, features that could cause the condition of an institution to be weakened as a going concern during periods of market stress;

List of RTS published on 4 April

- Article 27(6) - Limitations on redemption of own funds instruments issued by mutuals, cooperative societies and similar institutions
- **RTS related to general requirements/other aspects**
 - Article 73(3) - Supervisory consent for reducing own funds = meaning of sustainable for the income capacity of the institution, redemptions, reductions and repurchases announced by the institution, application to be submitted by the institution, content and timing of the application, processing of the application by the competent authority
 - Article 74(2) - Temporary waiver from deduction from own funds
 - Article 461(4)/Article 465(3) – transitional provisions

A few specific RTS

A few remarkable standards:

Instruments

- ✓ Incentives to redeem (art. 19 of the draft RTS)
- ✓ Conversion and write-downs/write-ups (art. 20-21-22)
- ✓ Meaning of minimal and insignificant regarding qualifying AT1/T2 capital issued by a SPE (art. 34)

Deductions

- ✓ Foreseeable dividends (art. 2)

A few specific RTS

Cooperatives

- ✓ Limitations on redemption of own funds instruments issued by mutuals, cooperative societies and similar institutions (art. 8)

General requirements/other aspects

- ✓ Supervisory consent for reducing own funds (art. 27 to 32)
- ✓ Temporary waiver from deduction from own funds (art. 33)

RTS related to instruments

Incentives to redeem (art. 19)

⇒ The RTS includes a list of situations qualifying as incentives to redeem, which will help to reach a uniform understanding on the nature of incentives to redeem (in line with Basel 3 rules text)

In particular:

- Step-ups
- Mandatory conversion or at the investor's hand if the call is not exercised
- A marketing of the instrument in a way which suggests that the instrument will be called

RTS related to instruments

Conversion and write-downs/write-ups (art. 20-21-22)

⇒ The RTS also increases the loss absorbency features of hybrid instruments. More stringent rules are defined for the activation of loss absorbency mechanisms for these instruments.

RTS related to instruments

- 3 types of loss absorbency mechanisms: conversion, permanent write-down, temporary write-down
- Institutions shall determine without delay that a trigger event has occurred, shall immediately notify the competent authority and the holders of the instruments, and shall determine within one month maximum the amount to be written-down or converted; irrevocable obligation to write-down or convert the instrument
- Write-down to be operated on a pro rata basis to all holders of instruments with a similar write-down mechanism and identical trigger level

RTS related to instruments

- There are no distributions of coupons while the temporary write-down is in effect
- Write-ups shall be based on profits; the maximum amount to be attributed to the write-up shall be based on the proportion of AT1 instruments in Tier 1; subject to restrictions relating to the Maximum Distributable Amount (art. 131 of the CRD)

RTS related to instruments

Meaning of minimal and insignificant regarding qualifying AT1/T2 capital issued by a SPE (art. 34)

⇒ Assets of a SPE minimal and insignificant where:

(a) the assets of the special purpose entity which are not constituted by the investments in the own funds of the related subsidiary are limited to cash assets dedicated to payment of coupons and redemption of the own funds instruments that are due, and;

(b) the amount of other assets of the special purpose entity different from the ones mentioned in point (a) are not higher than 0.5% of the average total assets of the special purpose entity over the last three years.

⇒ EBA is considering deleting point (b) (limit = 0% instead of 0.5%), views sought in the CP

RTS related to instruments

Questions and answers session

RTS related to deductions

Foreseeable dividends (art. 2)

⇒ the RTS prescribes the way foreseeable dividends have to be deducted from interim or year-end profits with the introduction of a hierarchy to evaluate the need for and extent of deduction: in the first place, decision on distributions from the relevant body; second, the dividend policy; third, an historical payout ratio.

RTS related to deductions

- Where the management body has formally taken a decision or proposed a decision to the relevant body on the amount of dividends to be distributed, this amount shall be deducted from the interim or year-end profits under consideration.
- Before the management body has formally taken a decision or proposed a decision to the relevant body on the distribution of dividends, the amount of foreseeable dividends to be deducted by institutions from the interim or year-end profits equals the amount of interim or year-end profits multiplied by the dividend payout ratio.

RTS related to deductions

- The dividend payout ratio shall be determined on the basis of the dividend policy approved by the management body or other relevant body. In the absence of an approved dividend policy, or when, in the opinion of the competent authority, it is likely that the institution will not apply its dividend policy or this policy is not a prudent basis to determine the amount of deduction, the dividend payout ratio shall be based on the highest of the following:
 - (a) the dividend payout ratio calculated as an average of the dividend payout ratios of the three years prior to the year under consideration;
 - (b) the dividend payout ratio of the year preceding that of the year under consideration.

RTS related to deductions

Questions and answers session

RTS related to cooperatives

Limitations on redemption of own funds instruments issued by mutuals, cooperative societies and similar institutions (art. 8)

⇒ the RTS clarifies how limitations to the redemption of cooperative shares, where the refusal by the institution of the redemption is prohibited under national law, shall be exercised and brings more transparency in this area

RTS related to cooperatives

- The institution shall have the possibility to defer the redemption and to limit the amount to be redeemed for an unlimited period of time when justified by the prudential situation;
- The prudential situation is assessed via the overall financial, liquidity and solvency situation and the excess of capital compared to the minimum requirements + buffers + Pillar 2 requirements;
- The supervisor can prevent further the redemption of the cooperatives shares, will assess the provisions governing the redemption of the cooperative shares and may ask for modifications of these provisions if it is not satisfied that the bases of limitations are appropriate;
- Any decision to limit redemption shall be documented.

RTS related to cooperatives

Questions and answers session

RTS related to general requirements/other

Supervisory consent for reducing own funds (art. 27 to 32)

⇒ The provisions related to supervisory consent for reducing own funds will also contribute to improve the permanence of capital instruments

RTS related to general requirements/other

- Redemptions, reductions and repurchases of own funds instruments shall not be announced to holders before the institution has obtained the prior approval of the supervisor
- Once redemptions, reductions and repurchases are sufficiently certain, the amounts to be redeemed, reduced or repurchased shall be deducted from own funds before the effective redemptions, reductions or repurchases occur (taken from CEBS GL on core capital)

RTS related to general requirements/other

- Institutions have to provide a detailed list of information to the supervisor when asking for a redemption/reduction or repurchase of capital instruments (taken from CEBS GL on core capital)
- Institutions will have to provide the supervisor with all the necessary information to perform its assessment 3 months in advance of the date where the redemption/reduction or repurchase will be announced to the holders of the instruments
- Competent authorities may allow institutions on a case-by-case basis and under exceptional circumstances to transmit the application within a time frame shorter than the 3 months period

RTS related to general requirements/other

- Where the repurchasing of the instrument is made for market making purposes, competent authorities may give in advance their prior consent for a certain predetermined amount under the certain conditions (specific thresholds defined)
- For mutuals, cooperative societies or similar institutions, where the amounts to be redeemed are not material (specific thresholds defined), the competent authority may give in advance its prior consent

RTS related to general requirements/other

Temporary waiver from deduction from own funds (art. 33)

⇒ Temporary shall mean of a duration that does not exceed the timeframe envisaged under the financial assistance operation plan + Temporary shall mean waiver in relation only to new holdings of instruments in the relevant entity subject to the financial assistance operation.

⇒ EBA is considering setting a time limit the waiver shall not exceed (max of 5y), views sought in the CP

RTS related to general requirements/other

Questions and answers session

Draft ITS on disclosure for own funds

- Establishing appropriate disclosure requirements increases the transparency on regulatory capital held by European institutions and ultimately contributes to strengthening its quality and quantity
- Complement the first set of standards on own funds published on 4 April and focus on the disclosure requirements to be met by institutions
- Aim at ensuring a uniform approach to disclosure for own funds by institutions and across jurisdictions in order to allow detailed assessments of banks' capital positions and to make cross-jurisdictional comparisons
- Consultation runs until 31 July 2012

Draft ITS on disclosure for own funds

Main features of the ITS:

- Facilitating international comparisons + avoiding 2 different disclosure frameworks → BCBS approach followed with appropriate reference to the EU regulatory framework (CRR) and consistency with the COREP framework
- Requirements directed at institutions requested to complete 3 sets of templates:
- ✓ a general own funds disclosure template reflecting the capital position of institutions;

Draft ITS on disclosure for own funds

- ✓ A transitional disclosure template covering the phasing in (01/01/2013 – 31/12/2017) of the regulatory adjustments (deductions and filters) and reflecting the transitional provisions implemented by the institutions;
- ✓ A template describing the main features of an institution's capital instruments.
- ✓ In addition to the 3 templates, institutions are required to provide a balance sheet reconciliation between financial statements / regulatory own funds to address the disparities between these two sets of data.

Next steps and timeline

Separate consultations for draft RTS should follow, depending on the on-going negotiations on the CRR:

- Article 25(2) point a) - Type of undertaking recognised under applicable national law as a mutual, cooperative institution or similar institution
- Article 29(2) – gain on sale (published on 12 June 2012)
- Article 31(2) – additional value adjustments
- Article 46(4) - conditions of application of calculation methods listed in FICOD for the purposes of the alternatives to deduction (JCFC)
- Article 84(4) - Risk weighting and prohibition of qualifying holdings outside the financial sector = activities that are a direct extension of banking etc (guidelines?)
- Article 92(4) – Fixed overheads investment firms (2014?)
- *More articles coming from the final CRR text?*

Next steps and timeline

- New consultations to come on own funds (see previous slide); provided that deadline for submission to Commission is 01/01/2013 → shorter consultation periods
- Finalisation of the technical standards on own funds planned for 4Q2012
- Objective: all RTS on own funds intended to be one integrated draft Regulation = completion of the EU single rulebook for institutions in the area of own funds
- On the basis of the final CRR/CRD texts
- On the basis of the answers to the consultations

Next steps and timeline

Final questions



EBA

THANK YOU

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