Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012 (Text with EEA relevance)

REGULATION (EU) No 575/2013 OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

of 26 June 2013

on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Central Bank[(1)],

Having regard to the opinion of the European Economic and Social Committee[(2)],

Acting in accordance with the ordinary legislative procedure,

Whereas:

(1) The G-20 Declaration of 2 April 2009 on Strengthening of the Financial System called for internationally consistent efforts that are aimed at strengthening transparency, accountability and regulation by improving the quantity and quality of capital in the banking system once the economic recovery is assured. That declaration also called for introduction of a supplementary non-risk based measure to contain the build-up of leverage in the banking system, and the development of a framework for stronger liquidity buffers. In response to the mandate given by the G-20, in September 2009 the Group of Central Bank Governors and Heads of Supervision (GHOS), agreed on a number of measures to strengthen the regulation of the banking sector. Those measures were endorsed by the G-20 leaders at their Pittsburgh Summit of 24-25 September 2009 and were set out in detail in December 2009. In July and September 2010, GHOS issued two further announcements on design and calibration of those new measures, and in December 2010, the Basel Committee on Banking Supervision (BCBS) published the final measures, that are referred to as the Basel III framework.

(2) The High Level Group on Financial Supervision in the EU chaired by Jacques de Larosière (the "de Larosière group") invited the Union to develop a more harmonised set of financial regulations. In the context of the future European supervisory architecture, the European Council of 18 and 19 June 2009 also stressed the need to establish a

'European Single Rule Book' applicable to all credit institutions and investment firms in the internal market.

(3) As stated in the de Larosière group's report of 25 February 2009 (the "de Larosière report"), "a Member State should be able to adopt more stringent national regulatory measures considered to be domestically appropriate for safeguarding financial stability as long as the principles of the internal market and agreed minimum core standards are respected".

(4) Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions[(3)] and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions[(4)] have been significantly amended on several occasions. Many provisions of Directives 2006/48/EC and 2006/49/EC are applicable to both credit institutions and investment firms. For the sake of clarity and in order to ensure a coherent application of those provisions, they should be merged into new legislative acts that are applicable to both credit institutions and investment firms, namely this Regulation and Directive 2013/36/EU of the European Parliament and of the Council[(5)]. For greater accessibility, the provisions of the Annexes to Directives 2006/48/EC and 2006/49/EC should be integrated into the enacting terms of Directive 2013/36/EU and this Regulation.

(5) Together, this Regulation and Directive 2013/36/EU should form the legal framework governing the access to the activity, the supervisory framework and the prudential rules for credit institutions and investment firms (referred to collectively as "institutions"). This Regulation should therefore be read together with that Directive

(6) Directive 2013/36/EU, based on Article 53(1) of the Treaty on the Functioning of the European Union (TFEU), should, inter alia, contain the provisions concerning the access to the activity of institutions, the modalities for their governance, and their supervisory framework, such as provisions governing the authorisation of the business, the acquisition of qualifying holdings, the exercise of the freedom of establishment and of the freedom to provide services, the powers of the competent authorities of the home and the host Member States in this regard and the provisions governing the initial capital and the supervisory review of institutions.

(7) This Regulation should, inter alia, contain the prudential requirements for institutions that relate strictly to the functioning of banking and financial services markets and are meant to ensure the financial stability of the operators on those markets as well as a high level of protection of investors and depositors. This Regulation aims at contributing in a determined manner to the smooth functioning of the internal market and should, consequently, be based on the provisions of Article 114 TFEU, as interpreted in accordance with the consistent case-law of the Court of Justice of the European Union.

(8) Directives 2006/48/EC and 2006/49/EC, although having harmonised the rules of Member States in the area of prudential supervision to a certain degree, include a significant number of options and possibilities for Member States to impose stricter rules than those laid down by those Directives. This results in divergences between national rules, which might hamper the cross-border provision of services and the

freedom of establishment and so create obstacles to the smooth functioning of the internal market.

(9) For reasons of legal certainty and because of the need for a level playing field within the Union, a single set of regulations for all market participants is a key element for the functioning of the internal market. In order to avoid market distortions and regulatory arbitrage, prudential minimum requirements should therefore ensure maximum harmonisation. As a consequence, the transitional periods provided for in this Regulation are essential for the smooth implementation of this Regulation and to avoid uncertainty for the markets.

(10) Having regard to work of the BCBS' Standards Implementation Group in monitoring and reviewing member countries' implementation of the Basel III framework, the Commission should provide update reports on an ongoing basis, and at least following the publication of each Progress Report by BCBS, on the implementation and domestic adoption of the Basel III framework in other major jurisdictions, including an assessment of the consistency of other countries' legislation or regulations with the international minimum standards, in order to identify differences that could raise level playing field concerns.

(11) In order to remove obstacles to trade and distortions of competition resulting from divergences between national laws and to prevent further likely obstacles to trade and significant distortions of competition from arising, it is therefore necessary to adopt a regulation establishing uniform rules applicable in all Member States.

(12) Shaping prudential requirements in the form of a regulation would ensure that those requirements will be directly applicable. This would ensure uniform conditions by preventing diverging national requirements as a result of the transposition of a directive. This Regulation would entail that all institutions follow the same rules in all the Union, which would also boost confidence in the stability of institutions, especially in times of stress. A regulation would also reduce regulatory complexity and firms' compliance costs, especially for institutions operating on a cross-border basis, and contribute to eliminating competitive distortions. With regard to the peculiarity of immovable property markets which are characterised by economic developments and jurisdictional differences that are specific to Member States, regions or local areas, competent authorities should be allowed to set higher risks weights or to apply stricter criteria based on default experience and expected market developments to exposures secured by mortgages on immovable property in specific areas.

(13) In areas not covered by this Regulation, such as dynamic provisioning, provisions on national covered bonds schemes not related to the treatment of covered bonds under the rules established by this Regulation, acquisition and holding of participations in both the financial and non-financial sector for purposes not related to prudential requirements specified in this Regulation, competent authorities or Member States should be able to impose national rules, provided that they are not inconsistent with this Regulation.

(14) The most important recommendations advocated in the de Larosière report and later implemented in the Union were the establishment of a singlerulebook and a European framework for macroprudential supervision where both elements in combination were

aimed at ensuring financial stability. The single rulebook ensures a robust and uniform regulatory framework facilitating the functioning of the internal market and prevents regulatory arbitrage opportunities. Within the internal market for financial services, macroprudential risks may however differ in a number of ways with a range of national specificities resulting in variances being observed for example with regard to the structure and size of the banking sector compared to the wider economy and the credit cycle.

(15) A number of tools to prevent and mitigate macroprudential and systemic risks have been built into this Regulation and Directive 2013/36/EU ensuring flexibility while at the same time ensuring that the use of those tools are subject to appropriate control in order not to harm the function of the internal market while also ensuring that the use of such tools is transparent and consistent.

(16) Beyond the systemic risk buffer tool included in Directive 2013/36/EU, where macroprudential or systemic risks concern a Member State, the competent or designated authorities of the relevant Member State should have the possibility to address those risks by certain specific national macroprudential measures, when this is considered more effective to tackle those risks. The European Systemic Risk Board ("ESRB") established by Regulation (EU) No 1092/2010 of the European Parliament and of the Council of 24 November 2010[(6)] and the European Supervisory Authority (European Banking Authority) ("EBA") established by Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010[(7)] should have the opportunity to provide their opinions on whether the conditions for such national macroprudential measures are met and there should be a Union mechanism to prevent national measures from proceeding, where there is very strong evidence that the relevant conditions are not satisfied. Whilst this Regulation establishes uniform microprudential rules for institutions, Member States retain a leading role in macroprudential oversight because of their expertise and their existing responsibilities in relation to financial stability. In that specific case, since the decision to adopt any national macroprudential measures includes certain assessments in relation to risks which may ultimately affect the macroeconomic, fiscal and budgetary situation of the relevant Member State, it is necessary that the power to reject the proposed national macroprudential measures is conferred on the Council in accordance with Article 291 TFEU, acting on a proposal by the Commission.

(17) Where the Commission has submitted to the Council a proposal to reject national macroprudential measures, the Council should examine that proposal without delay and decide whether or not to reject the national measures. A vote could be taken in accordance with the Rules of Procedure of the Council[(8)] at the request of a Member State or of the Commission. In accordance with Article 296 TFEU, the Council should state the reasons for its decision with respect to the conditions laid down in this Regulation for its intervention. Considering the importance of the macroprudential and systemic risk for the financial market of the Member State concerned and therefore the need for rapid reaction, it is important that the time limit for such a Council decision is set to one month. If the Council, after having examined the proposal by the Commission to reject the proposed national measures in depth, comes to the conclusion that the

conditions laid down in this Regulation for the rejection of the national measures were not fulfilled, it should always provide its reasons in a clear and unambiguous manner.

(18) Until the harmonisation of liquidity requirements in 2015 and the harmonisation of a leverage ratio in 2018, Member States should be able to apply such measures as they consider appropriate, including measures to mitigate macroprudential or systemic risk in a specific Member State.

(19) It should be possible to apply systemic risk buffers or individual measures taken by Member States to address systemic risks concerning those Member States, to the banking sector in general or to one or more subsets of the sector, meaning subsets of institutions that exhibit similar risk profiles in their business activities, or to the exposures to one or several domestic economic or geographic sectors across the banking sector.

(20) If two or more Member States' designated authorities identify the same changes in the intensity of systemic or macroprudential risk posing a risk to financial stability at the national level in each Member State which the designated authorities consider would better be addressed by means of national measures, the Member States may submit a joint notification to the Council, the Commission, the ESRB and EBA. When notifying the Council, the Commission, the ESRB and EBA Member States should submit relevant evidence, including a justification of the joint notification.

(21) The Commission should furthermore be empowered to adopt a delegated act temporarily increasing the level of own funds requirements, requirements for large exposures and public disclosure requirements. Such provisions should be applicable for a period of one year, unless the European Parliament or the Council has objected to the delegated act within a period of three months. The Commission should state the reasons for the use of such a procedure. The Commission should only be empowered to impose stricter prudential requirements for exposures which arise from market developments in the Union or outside the Union affecting all Member States.

(22) A review of the macroprudential rules is justified in order for the Commission to assess, among other things, whether the macroprudential tools in this Regulation or Directive 2013/36/EU are effective, efficient and transparent, whether new instruments should be proposed, whether the coverage and the possible degrees of overlap of the macroprudential tools for targeting similar risks in this Regulation or Directive 2013/36/EU are appropriate and how internationally agreed standards for systemically important institutions interacts with this Regulation or Directive 2013/36/EU.

(23) Where Member States adopt guidelines of general scope, in particular in areas where the adoption by the Commission of draft technical standards is pending, those guidelines shall neither contradict Union law nor undermine its application.

(24) This Regulation does not prevent Member States from imposing, where appropriate, equivalent requirements on undertakings that do not fall within its scope.

(25) The general prudential requirements set out in this Regulation are supplemented by individual arrangements that are decided by the competent authorities as a result of their ongoing supervisory review of individual institutions. The range of such supervisory

arrangements should, inter alia, be set out in Directive 2013/36/EU since the competent authorities should be able to exert their judgment as to which arrangements should be imposed.

(26) This Regulation should not affect the ability of competent authorities to impose specific requirements under the supervisory review and evaluation process set out in Directive 2013/36/EU that should be tailored to the specific risk profile of institutions.

(27) Regulation (EU) No 1093/2010 aims at upgrading the quality and consistency of national supervision and strengthening oversight of cross-border groups.

(28) Given the increase in the number of tasks conferred on EBA by this Regulation and by Directive 2013/36/EU, the European Parliament, the Council and the Commission should ensure that adequate human and financial resources are made available without delay.

(29) Regulation (EU) No 1093/2010 requires EBA to act within the scope of Directives 2006/48/EC and 2006/49/EC. EBA is also required to act in the field of activities of institutions in relation to issues not directly covered in those Directives, provided that such actions are necessary to ensure the effective and consistent application of those Directives. This Regulation should take into account the role and function of EBA and facilitate the exercise of EBA's powers set out in Regulation (EU) No 1093/2010.

(30) After the observation period and the full implementation of a liquidity coverage requirement in accordance with this Regulation, the Commission should assess whether granting EBA a power of initiative to intervene with binding mediation in relation to the reaching of joint decisions by the competent authorities under Articles 20 and 21 of this Regulation would facilitate the practical formation and operation of single liquidity sub-groups as well as the determination of whether criteria for a specific intragroup treatment for cross-border institutions are met. Therefore, at that time, as part of one of the regular reports on the operation of EBA under Article 81 of Regulation (EU) No 1093/2010, the Commission should specifically examine the need to grant EBA such powers and include the results of this examination in its report, which should be accompanied by appropriate legislative proposals, where appropriate.

(31) The de Larosière report stated that microprudential supervision cannot effectively safeguard financial stability without adequately taking account of developments at macro level, while macroprudential oversight is not meaningful unless it can somehow impact on supervision at the micro level. Close cooperation between EBA and the ESRB is essential to give full effectiveness to the functioning of the ESRB and follow up to its warnings and recommendations. In particular, EBA should be able to transmit to the ESRB all relevant information gathered by competent authorities in accordance with the reporting obligations set out in this Regulation.

(32) Considering the devastating effects of the latest financial crisis the overall objectives of this Regulation are to encourage economically useful banking activities that serve the general interest and to discourage unsustainable financial speculation without real added value. This implies a comprehensive reform of the ways savings are channelled into productive investments. In order to safeguard a sustainable and diverse banking

environment in the Union, competent authorities should be empowered to impose higher capital requirements for systemically important institutions that are able, due to their business activities, to pose a threat to the global economy.

(33) Equivalent financial requirements for institutions holding money or securities belonging to their clients are necessary to ensure similar safeguards for savers and fair conditions of competition between comparable groups of institutions.

(34) Since institutions in the internal market are engaged in direct competition, monitoring requirements should be equivalent throughout the Union taking into account the different risk profiles of the institutions.

(35) Whenever in the course of supervision it is necessary to determine the amount of the consolidated own funds of a group of institutions, the calculation should be effected in accordance with this Regulation.

(36) According to this Regulation own funds requirements apply on an individual and consolidated basis, unless competent authorities do not apply supervision on an individual basis where they deem this appropriate. Individual, consolidated and cross-border consolidated supervision are useful tools in overseeing institutions.

(37) In order to ensure adequate solvency of institutions within a group it is essential that the capital requirements apply on the basis of the consolidated situation of those institutions within the group. In order to ensure that own funds are appropriately distributed within the group and available to protect savings where needed, the capital requirements should apply to individual institutions within a group, unless this objective can be effectively achieved otherwise.

(38) The minority interests arising from intermediate financial holding companies that are subject to the requirements of this Regulation on a sub-consolidated basis may also be eligible, within the relevant limits, as Common Equity Tier 1 capital of the group on a consolidated basis, as the Common Equity Tier 1 capital of an intermediate financial holding company attributable to minority interests and the part of that same capital attributable to the parent company support both pari passu the losses of their subsidiaries when they occur.

(39) The precise accounting technique to be used for the calculation of own funds, their adequacy for the risk to which an institution is exposed, and for the assessment of the concentration of exposures should take account of the provisions of Council Directive 86/635/EEC of 8 December 1986 on the annual accounts and consolidated accounts of banks and other financial institutions[9], which incorporates certain adaptations of the provisions of Seventh Council Directive 83/349/EEC of 13 June 1983 on consolidated accounts[10] or of Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards[11], whichever governs the accounting of the institutions under national law.

(40) For the purposes of ensuring adequate solvency it is important to lay down capital requirements which weight assets and off-balance sheet items according to the degree of risk.

(41) On 26 June 2004 the BCBS adopted a framework agreement on the international convergence of capital measurement and capital requirements ('Basel II framework'). The provisions in Directives 2006/48/EC and 2006/49/EC that this Regulation has taken over form an equivalent to the provisions of the Basel II framework. Consequently, by incorporating the supplementary elements of the Basel III framework this Regulation forms an equivalent to the provisions of the Basel II and III frameworks.

(42) It is essential to take account of the diversity of institutions in the Union by providing alternative approaches to the calculation of capital requirements for credit risk incorporating different levels of risk-sensitivity and requiring different degrees of sophistication. Use of external ratings and institutions' own estimates of individual credit risk parameters represents a significant enhancement in the risk-sensitivity and prudential soundness of the credit risk rules. Institutions should be encouraged to move towards the more risk-sensitive approaches. In producing the estimates needed to apply the approaches to credit risk of this Regulation, institutions should enhance their credit risk measurement and management processes to make available methods for determining regulatory own funds requirements that reflect the nature, scale, and complexity of individual institutions' processes. In this regard, the processing of data in connection with the incurring and management of exposures to customers should be considered to include the development and validation of credit risk management and measurement systems. That serves not only to fulfil the legitimate interests of institutions but also the purpose of this Regulation, to use better methods for risk measurement and management and also use them for regulatory own funds purposes. Notwithstanding this, the more risk-sensitive approaches require considerable expertise and resources as well as data of high quality and sufficient volume. Institutions should therefore comply with high standards before applying those approaches for regulatory own funds purposes. Given the ongoing work on ensuring appropriate backstops to internal models, the Commission should prepare a report on the possibility of extending the Basel I floor together with a legislative proposal, if appropriate.

(43) The capital requirements should be proportionate to the risks addressed. In particular the reduction in risk levels deriving from having a large number of relatively small exposures should be reflected in the requirements.

(44) Small and medium-sized enterprises (SMEs) are one of the pillars of the Union economy given their fundamental role in creating economic growth and providing employment. The recovery and future growth of the Union economy depends largely on the availability of capital and funding to SMEs established in the Union to carry out the necessary investments to adopt new technologies and equipment to increase their competitiveness. The limited amount of alternative sources of funding has made SMEs established in the Union even more sensitive to the impact of the banking crisis. It is therefore important to fill the existing funding gap for SMEs and ensure an appropriate flow of bank credit to SMEs in the current context. Capital charges for exposures to SMEs should be reduced through the application of a supporting factor equal to 0,7619 to allow credit institutions to increase lending to SMEs. To achieve this objective, credit institutions should effectively use the capital relief produced through the application of

the supporting factor for the exclusive purpose of providing an adequate flow of credit to SMEs established in the Union. Competent authorities should monitor periodically the total amount of exposures to SMEs of credit institutions and the total amount of capital deduction.

(45) In line with the decision of the BCBS, as endorsed by the GHOS on 10 January 2011, all additional Tier 1 and Tier 2 instruments of an institution should be capable of being fully and permanently written down or converted fully into Common Equity Tier 1 capital at the point of non-viability of the institution. Necessary legislation to ensure that own funds instruments are subject to the additional loss absorption mechanism should be incorporated into Union law as part of the requirements in relation to the recovery and resolution of institutions. If by 31 December 2015, Union law governing the requirement that capital instruments should be capable of being fully and permanently written down to zero or converted into Common Equity Tier 1 instruments in the event that an institution is no longer considered viable has not been adopted, the Commission should review and report on whether such a provision should be included in this Regulation and, in light of that review, submit appropriate legislative proposals.

(46) The provisions of this Regulation respect the principle of proportionality, having regard in particular to the diversity in size and scale of operations and to the range of activities of institutions. Respect for the principle of proportionality also means that the simplest possible rating procedures, even in the Internal Ratings Based Approach ('IRB Approach'), are recognised for retail exposures. Member States should ensure that the requirements laid down in this Regulation apply in a manner proportionate to the nature, scale and complexity of the risks associated with an institution's business model and activities. The Commission should ensure that delegated and implementing acts, regulatory technical standards and implementing technical standards are consistent with the principle of proportionality, so as to guarantee that this Regulation is applied in a proportionate manner. EBA should therefore ensure that all regulatory and implementing technical standards are drafted in such a way that they are consistent with and uphold the principle of proportionality.

(47) Competent authorities should pay appropriate attention to cases where they suspect that information is regarded as proprietary or confidential in order to avoid disclosure of such information. Although an institution may opt not to disclose information as the information is regarded as proprietary or confidential, the fact that information is being regarded as proprietary or confidential should not discharge liability arising from non-disclosure of that information when such non-disclosure is found to have material effect.

(48) The 'evolutionary' nature of this Regulation enables institutions to choose amongst three approaches to credit risk of varying complexity. In order to allow especially small institutions to opt for the more risk-sensitive IRB Approach, the relevant provisions should be read so that exposure classes include all exposures that are, directly or indirectly, put on a par with them throughout this Regulation. As a general rule, the competent authorities should not discriminate between the three approaches with regard to the Supervisory Review Process, i.e. institutions operating according to the

provisions of the Standardised Approach should not for that reason alone be supervised on a stricter basis.

(49) Increased recognition should be given to techniques of credit risk mitigation within a framework of rules designed to ensure that solvency is not undermined by undue recognition. The relevant Member States' current customary banking collateral for mitigating credit risks should wherever possible be recognised in the Standardised Approach, but also in the other approaches.

(50) In order to ensure that the risks and risk reductions arising from institutions' securitisation activities and investments are appropriately reflected in the capital requirements of institutions it is necessary to include rules providing for a risk-sensitive and prudentially sound treatment of such activities and investments. To this end, a clear and encompassing definition of securitisation is needed that captures any transaction or scheme whereby the credit risk associated with an exposure or pool of exposures is tranched. An exposure that creates a direct payment obligation for a transaction or scheme used to finance or operate physical assets should not be considered an exposure to a securitisation, even if the transaction or scheme has payment obligations of different seniority.

(51) Alongside surveillance aimed at ensuring financial stability, there is a need for mechanisms designed to enhance and develop an effective surveillance and prevention of potential bubbles in order to ensure optimum allocation of capital in the light of the macroeconomic challenges and objectives, in particular with respect to long term investment in the real economy.

(52) Operational risk is a significant risk faced by institutions requiring coverage by own funds. It is essential to take account of the diversity of institutions in the Union by providing alternative approaches to the calculation of operational risk requirements incorporating different levels of risk-sensitivity and requiring different degrees of sophistication. There should be appropriate incentives for institutions to move towards the more risk-sensitive approaches. In view of the emerging state of the art for the measurement and management of operational risk the rules should be kept under review and updated as appropriate including in relation to the charges for different business lines and the recognition of risk mitigation techniques. Particular attention should be paid in this regard to taking insurance into account in the simple approaches to calculating capital requirements for operational risk.

(53) The monitoring and control of an institution's exposures should be an integral part of its supervision. Therefore, excessive concentration of exposures to a single client or group of connected clients may result in an unacceptable risk of loss. Such a situation can be considered prejudicial to the solvency of an institution.

(54) In determining the existence of a group of connected clients and thus exposures constituting a single risk, it is also important to take into account risks arising from a common source of significant funding provided by the institution itself, its financial group or its connected parties.

(55) While it is desirable to base the calculation of the exposure value on that provided for the purposes of own funds requirements, it is appropriate to adopt rules for the monitoring of large exposures without applying risk weightings or degrees of risk. Moreover, the credit risk mitigation techniques applied in the solvency regime were designed with the assumption of a well-diversified credit risk. In the case of large exposures dealing with single name concentration risk, credit risk is not well-diversified. The effects of those techniques should therefore be subject to prudential safeguards. In this context, it is necessary to provide for an effective recovery of credit protection for the purposes of large exposures.

(56) Since a loss arising from an exposure to an institution can be as severe as a loss from any other exposure, such exposures should be treated and reported in the same manner as any other exposures. An alternative quantitative limit has been introduced to alleviate the disproportionate impact of such an approach on smaller institutions. In addition, very short-term exposures related to money transmission including the execution of payment services, clearing, settlement and custody services to clients are exempt to facilitate the smooth functioning of financial markets and of the related infrastructure. Those services cover, for example, the execution of cash clearing and settlement and similar activities to facilitate settlement. The related exposures include exposures which might not be foreseeable and are therefore not under the full control of a credit institution, inter alia, balances on inter-bank accounts resulting from client payments, including credited or debited fees and interest, and other payments for client services, as well as collateral given or received.

(57) It is important that the interests of undertakings that 're-package' loans into tradable securities and other financial instruments (originators or sponsors) and undertakings that invest in these securities or instruments (investors) are aligned. To achieve this, the originator or sponsor should retain a significant interest in the underlying assets. It is therefore important for the originators or the sponsors to retain exposure to the risk of the loans in question. More generally, securitisation transactions should not be structured in such a way as to avoid the application of the retention requirement, in particular through any fee or premium structure or both. Such retention should be applicable in all situations where the economic substance of a securitisation is applicable, whatever legal structures or instruments are used to obtain this economic substance. In particular where credit risk is transferred by securitisation, investors should make their decisions only after conducting thorough due diligence, for which they need adequate information about the securitisations.

(58) This Regulation also provides that there be no multiple applications of the retention requirement. For any given securitisation it suffices that only the originator, the sponsor or the original lender is subject to the requirement. Similarly, where securitisation transactions contain other securitisations as an underlying, the retention requirement should be applied only to the securitisation which is subject to the investment. Purchased receivables should not be subject to the retention requirement if they arise from corporate activity where they are transferred or sold at a discount to finance such activity. Competent authorities should apply the risk weight in relation

to non-compliance with due diligence and risk management obligations in relation to securitisation for non-trivial breaches of policies and procedures which are relevant to the analysis of the underlying risks. The Commission should also review whether avoidance of multiple applications of the retention requirement could be conducive to practices circumventing the retention requirement and whether the rules on securitisations are enforced effectively by the competent authorities.

(59) Due diligence should be used in order to properly assess the risks arising from securitisation exposures for both the trading book and the non-trading book. In addition, due diligence obligations need to be proportionate. Due diligence procedures should contribute to building greater confidence between originators, sponsors and investors. It is therefore desirable that relevant information concerning the due diligence procedures is properly disclosed.

(60) When an institution incurs an exposure to its own parent undertaking or to other subsidiaries of its parent undertaking, particular prudence is necessary. The management of such exposures incurred by institutions should be carried out in a fully autonomous manner, in accordance with the principles of sound management, without regard to any other considerations. This is especially important in the case of large exposures and in cases not simply related to intragroup administration or usual intragroup transactions. Competent authorities should pay particular attention to such intragroup exposures. Such standards need not, however be applied where the parent undertaking is a financial holding company or a credit institution or where the other subsidiaries are either credit or financial institutions or undertakings offering ancillary services, provided that all such undertakings are covered by the supervision of the credit institution on a consolidated basis.

(61) In view of the risk-sensitivity of the rules relating to capital requirements, it is desirable to keep under review whether these have significant effects on the economic cycle. The Commission, taking into account the contribution of the European Central Bank (ECB), should report on these aspects to the European Parliament and to the Council.

(62) The capital requirements for commodity dealers, including those dealers currently exempt from the requirements of Directive 2004/39/EC of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments[12], should be reviewed.

(63) The goal of liberalisation of gas and electricity markets is both economically and politically important for the Union. With this in mind, the capital requirements and other prudential rules to be applied to firms active in those markets should be proportionate and should not unduly interfere with achievement of the goal of liberalisation. This goal should, in particular, be kept in mind when reviews of this Regulation are carried out.

(64) Institutions investing in re-securitisations should exercise due diligence also with regard to the underlying securitisations and the non-securitisation exposures ultimately underlying the former. Institutions should assess whether exposures in the context of asset-backed commercial paper programmes constitute re-securitisation exposures, including those in the context of programmes which acquire senior tranches of separate pools of whole loans where none of those loans is a securitisation or re-securitisation

exposure, and where the first-loss protection for each investment is provided by the seller of the loans. In the latter situation, a pool- specific liquidity facility should generally not be considered a re-securitisation exposure because it represents a tranche of a single asset pool (that is, the applicable pool of whole loans) which contains no securitisation exposures. By contrast, a programme-wide credit enhancement covering only some of the losses above the seller-provided protection across the various pools generally would constitute a tranching of the risk of a pool of multiple assets containing at least one securitisation exposure, and would therefore be a re-securitisation exposure. Nevertheless, if such a programme funds itself entirely with a single class of commercial paper, and if either the programme-wide credit enhancement is not a re-securitisation or the commercial paper is fully supported by the sponsoring institution, leaving the commercial paper investor effectively exposed to the default risk of the sponsor instead of the underlying pools or assets, then that commercial paper generally should not be considered a re-securitisation exposure.

(65) The provisions on prudent valuation for the trading book should apply to all instruments measured at fair value, whether in the trading book or non- trading book of institutions. It should be clarified that, where the application of prudent valuation would lead to a lower carrying value than actually recognised in the accounting, the absolute value of the difference should be deducted from own funds.

(66) Institutions should have a choice whether to apply a capital requirement to or deduct from Common Equity Tier 1 items those securitisation positions that receive a 1 250 % risk weight under this Regulation, irrespective of whether the positions are in the trading or the non-trading book.

(67) Originator or sponsor institutions should not be able to circumvent the prohibition of implicit support by using their trading books in order to provide such support.

(68) Without prejudice to the disclosures explicitly required by this Regulation, the aim of the disclosure requirements should be to provide market participants with accurate and comprehensive information regarding the risk profile of individual institutions. Institutions should therefore be required to disclose additional information not explicitly listed in this Regulation where such disclosure is necessary to meet that aim. At the same time, competent authorities should pay appropriate attention to cases where they suspect that information is regarded as proprietary or confidential by an institution in order to avoid disclosure of such information.

(69) Where an external credit assessment for a securitisation position incorporates the effect of credit protection provided by the investing institution itself, the institution should not be able to benefit from the lower risk weight resulting from that protection. The securitisation position should not be deducted from capital if there are other ways to determine a risk weight in line with the actual risk of the position which does not take that credit protection into account.

(70) Given their recent weak performance, the standards for internal models to calculate market risk capital requirements should be strengthened. In particular, their capture of risks should be completed regarding credit risks in the trading book. Furthermore, capital charges should include a component adequate to stress conditions to strengthen

capital requirements in view of deteriorating market conditions and in order to reduce the potential for pro-cyclicality. Institutions should also carry out reverse stress tests to examine what scenarios could challenge the viability of the institution unless they can prove that such a test is dispensable. Given the recent particular difficulties of treating securitisation positions using approaches based on internal models, the recognition of institutions' modelling of securitisation risks to calculate capital requirements in the trading book should be limited and a standardised capital charge for securitisation positions in the trading book should be required by default.

(71) This Regulation lays down limited exceptions for certain correlation trading activities, in accordance with which an institution may be permitted by its supervisor to calculate a comprehensive risk capital charge subject to strict requirements. In such cases the institution should be required to subject those activities to a capital charge equal to the higher of the capital charge in accordance with that internally developed approach and 8 % of the capital charge for specific risk in accordance with the standardised measurement method. It should not be required to subject those exposures to the incremental risk charge but they should be incorporated into both the value-at-risk measures and the stressed value-at-risk measures.

(72) In light of the nature and magnitude of unexpected losses experienced by institutions during the financial and economic crisis, it is necessary to improve further the quality and harmonisation of own funds that institutions are required to hold. This should include the introduction of a new definition of the core elements of capital available to absorb unexpected losses as they arise, enhancements to the definition of hybrid capital and uniform prudential adjustments to own funds. It is also necessary to raise significantly the level of own funds, including new capital ratios focusing on the core elements of own funds available to absorb losses as they arise. It is expected that institutions whose shares are admitted to trading on a regulated market should meet their capital requirements regarding the core elements of capital with such shares that meet a strict set of criteria for the core capital instruments and the disclosed reserves of the institution only. In order to adequately take into account the diversity of legal forms institutions within the Union are operating under, the strict set of criteria for the core capital instruments should ensure that core capital instruments for institutions whose shares are not admitted to trading on a regulated market are of the highest quality. This should not prevent institutions from paying, on shares that have differentiated or no voting rights, distributions that are a multiple of those paid on shares which have relatively higher levels of voting rights, provided that, irrespective of the level of voting rights, the strict criteria for Common Equity Tier 1 instruments are met, including those relating to the flexibility of payments, and provided that where a distribution is paid it is to be paid on all shares issued by the institution concerned.

(73) Trade finance exposures are diverse in nature but share characteristics such as being small in value and short in duration and having an identifiable source of repayment. They are underpinned by movements of goods and services that support the real economy and in most cases help small companies in their day-to-day needs, thereby creating economic growth and job opportunities. Inflows and outflows are usually matched and liquidity risk is therefore limited.

(74) It is appropriate that EBA keeps an up-to-date list of all of the forms of capital instruments in each Member State that qualify as Common Equity Tier 1 instruments. EBA should remove from that list non-State aid instruments issued after the date of entry into force of this Regulation not meeting the criteria specified in this Regulation and should publicly announce such removal. Where instruments removed by EBA from the list continue to be recognised after EBA's announcement, EBA should fully exercise its powers, in particular those conferred by Article 17 of Regulation (EU) No 1093/2010 concerning breaches of Union law. It is recalled that a three-step mechanism applies for a proportionate response to instances of incorrect or insufficient application of Union law, whereby, as a first step, EBA is empowered to investigate alleged incorrect or insufficient application of Union law obligations by national authorities in their supervisory practice, concluded by a recommendation. Second, where the competent national authority does not follow the recommendation, the Commission is empowered to issue a formal opinion taking into account the EBA's recommendation, requiring the competent authority to take the actions necessary to ensure compliance with Union law. Third, to overcome exceptional situations of persistent inaction by the competent authority concerned, the EBA is empowered, as a last resort, to adopt decisions addressed to individual financial institutions. Moreover, it is recalled that, under Article 258 TFEU, where the Commission considers that a Member State has failed to fulfil an obligation under the Treaties, it has the power to bring the matter before the Court of Justice of the European Union.

(75) This Regulation should not affect the ability of competent authorities to maintain pre-approval processes regarding the contracts governing Additional Tier 1 and Tier 2 capital instruments. In those cases such capital instruments should only be computed towards the institution's Additional Tier 1 capital or Tier 2 capital once they have successfully completed these approval processes.

(76) For the purposes of strengthening market discipline and enhancing financial stability it is necessary to introduce more detailed requirements for disclosure of the form and nature of regulatory capital and prudential adjustments made in order to ensure that investors and depositors are sufficiently well informed about the solvency of institutions.

(77) It is further necessary for competent authorities to have knowledge of the level, at least in aggregate terms, of repurchase agreements, securities lending and all forms of encumbrance of assets. Such information should be reported to the competent authorities. For the purposes of strengthening market discipline, there should be more detailed requirements for disclosure of repurchase agreements and secured funding.

(78) The new definition of capital and regulatory capital requirements should be introduced in a manner that takes account of the fact that there are different national starting points and circumstances, with initial variance around the new standards reducing over the transition period. In order to ensure the appropriate continuity in the level of own funds, instruments issued within the context of a recapitalisation measure pursuant to State aid rules and issued prior to the date of application of this Regulation will be grandfathered for the extent of the transition period. Reliance on State aid should be

reduced as much as possible in the future. However, to the extent that State aid proves necessary in certain situations, this Regulation should provide for a framework to deal with such situations. In particular, this Regulation should specify what should be the treatment for own funds instruments issued within the context of a recapitalisation measure pursuant to State aid rules. The possibility for institutions to benefit from such treatment should be subject to strict conditions. Furthermore, to the extent that such treatment allows for deviations from the new criteria on the quality of own funds instruments those deviations should be limited to the largest extent possible. The treatment for existing capital instruments issued within the context of a recapitalisation measure pursuant to State aid- rules, should clearly distinguish between those capital instruments that comply with the requirements of this Regulation and those that do not. Appropriate transitional provisions for the latter case should therefore be laid down in this Regulation.

(79) Directive 2006/48/EC required credit institutions to provide own funds that are at least equal to specified minimum amounts until 31 December 2011. In the light of the continuing effects of the financial crisis in the banking sector and the extension of the transitional arrangements for capital requirements adopted by the BCBS, it is appropriate to reintroduce a lower limit for a limited period of time until sufficient amounts of own funds have been established in accordance with the transitional arrangements for own funds provided for in this Regulation that will be progressively phased in from the date of application of this Regulation to 2019.

(80) For groups which include significant banking or investment business and insurance business, Directive 2002/87/EC of the European Parliament and of the Council of 16 December 2002 on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate[13], provides specific rules to address such 'double counting' of capital. Directive 2002/87/EC is based on internationally agreed principles for dealing with risk across sectors. This Regulation strengthens the way those financial conglomerates rules shall apply to bank and investment firm groups, ensuring their robust and consistent application. Any further changes that are necessary will be addressed in the review of Directive 2002/87/EC, which is expected in 2015.

(81) The financial crisis highlighted that institutions greatly underestimated the level of counterparty credit risk associated with over-the-counter (OTC) derivatives. This prompted the G-20, in September 2009, to call for more OTC derivatives to be cleared through a central counterparty (CCP). Furthermore, they asked for those OTC derivatives that could not be cleared centrally to be subject to higher own funds requirements in order to properly reflect the higher risks associated with them.

(82) Following the G-20 call, the BCBS, as part of the Basel III framework, materially changed the counterparty credit risk regime. The Basel III framework is expected to significantly increase the own fund requirements associated with institutions' OTC derivatives and securities financing transactions and to create important incentives for institutions to use CCPs. The Basel III framework is also expected to provide further incentives to strengthen the risk management of counterparty credit exposures and to

revise the current regime for the treatment of counterparty credit risk exposures to CCPs.

(83) Institutions should hold additional own funds due to credit valuation adjustment risk arising from OTC derivatives. Institutions should also apply a higher asset value correlation in the calculation of the own fund requirements for counterparty credit risk exposures arising from OTC derivatives and securities-financing transactions to certain financial institutions. Institutions should also be required to considerably improve measurement and management of counterparty credit risk by better addressing wrong-way risk, highly leveraged counterparties and collateral, accompanied by the corresponding enhancements in the areas of back-testing and stress testing.

(84) Trade exposures to CCPs usually benefit from the multilateral netting and loss-sharing mechanism provided by CCPs. As a consequence, they involve a very low counterparty credit risk and should therefore be subject to a very low own funds requirement. At the same time, this requirement should be positive in order to ensure that institutions track and monitor their exposures to CCPs as part of good risk management and to reflect that even trade exposures to CCPs are not risk-free.

(85) A CCP's default fund is a mechanism that allows the sharing (mutualisation) of losses among the CCP's clearing members. It is used where the losses incurred by the CCP following the default of a clearing member are greater than the margins and default fund contributions provided by that clearing member and any other defence the CCP may use before recurring to the default fund contributions of the remaining clearing members. In view of this, the risk of loss associated with exposures from default fund contributions is higher than that associated with trade exposures. Therefore, this type of exposures should be subject to a higher own funds requirement.

(86) The "hypothetical capital" of a CCP should be a variable needed to determine the own funds requirement for a clearing member's exposures from its contributions to a CCP's default fund. It should not be understood as anything else. In particular, it should not be understood as the amount of capital that a CCP is required to hold by its competent authority.

(87) The review of the treatment of counterparty credit risk, and in particular putting in place higher own funds requirements for bilateral derivative contracts in order to reflect the higher risk that such contracts pose to the financial system, forms an integral part of the Commission's efforts to ensure efficient, safe and sound derivatives markets. Consequently, this Regulation complements Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories[14].

(88) The Commission should review the relevant exemptions for large exposures by 31 December 2015. Pending the outcome of that review, Member States should continue being allowed to decide on the exemption of certain large exposures from those rules for a sufficiently long transitional period. Building on the work done in the context of the preparation and negotiation of Directive 2009/111/EC of the European Parliament and of the Council of 16 September 2009 amending Directives 2006/48/EC, 2006/49/EC and 2007/64/EC as regards banks affiliated to central institutions, certain own

funds items, large exposures, supervisory arrangements, and crisis management[15] and taking into account international and Union developments on those issues, the Commission should review whether those exemptions should continue to be applied in a discretionary or in a more general way and on whether the risks related to those exposures are addressed by other effective means laid down in this Regulation.

(89) In order to ensure that exemptions of exposures by competent authorities do not jeopardise the coherence of the uniform rules established by this Regulation on a permanent basis, after a transitional period, and in the absence of any outcome of that review, the competent authorities should consult EBA on whether or not it is appropriate to continue making use of the possibility to exempt certain exposures.

(90) The years preceding the financial crisis were characterised by an excessive build up in institutions' exposures in relation to their own funds (leverage). During the financial crisis, losses and the shortage of funding forced institutions to reduce significantly their leverage over a short period of time. This amplified downward pressures on asset prices, causing further losses for institutions which in turn led to further declines in their own funds. The ultimate results of this negative spiral were a reduction in the availability of credit to the real economy and a deeper and longer crisis.

(91) Risk-based own funds requirements are essential to ensure sufficient own funds to cover unexpected losses. However, the crisis has shown that those requirements alone are not sufficient to prevent institutions from taking on excessive and unsustainable leverage risk.

(92) In September 2009, the G-20 leaders committed to developing internationally-agreed rules to discourage an excessive leverage. To that end, they supported the introduction of a leverage ratio as a supplementary measure to the Basel II framework.

(93) In December 2010, the BCBS published guidelines defining the methodology for calculating the leverage ratio. Those rules provide for an observation period that will run from 1 January 2013 until 1 January 2017 during which the leverage ratio, its components and its behaviour relative to the risk-based requirement will be monitored. Based on the results of the observation period the BCBS intends to make any final adjustments to the definition and calibration of the leverage ratio in the first half of 2017, with a view to migrating to a binding requirement on 1 January 2018 based on appropriate review and calibration. The BCBS guidelines also provide for disclosure of the leverage ratio and its components starting from 1 January 2015.

(94) A leverage ratio is a new regulatory and supervisory tool for the Union. In line with international agreements, it should be introduced first as an additional feature that can be applied on individual institutions at the discretion of supervisory authorities. Reporting obligations for institutions would allow appropriate review and calibration, with a view to migrating to a binding measure in 2018.

(95) When reviewing the impact of the leverage ratio on different business models, particular attention should be paid to business models which are considered to entail low risk, such as mortgage lending and specialised lending with regional governments, local authorities or public sector entities. EBA, on the basis of data received and the findings

of the supervisory review during an observation period, should in cooperation with competent authorities develop a classification of business models and risks. Based on appropriate analysis, and also taking into account historical data or stress scenarios, there should be an assessment of the appropriate levels of the leverage ratio that safeguard the resilience of the respective business models and whether the levels of the leverage ratio should be set as thresholds or ranges. After the observation period and the calibration of the respective levels of the leverage ratio, and on the basis of the assessment, EBA can publish an appropriate statistical review, including averages and standard deviations, of the leverage ratio. After adoption of the leverage ratio requirements, EBA should publish an appropriate statistical review, including averages and standard deviations, of the leverage ratio in relation to the identified categories of institutions.

(96) Institutions should monitor the level and changes in the leverage ratio as well as leverage risk as part of the internal capital adequacy assessment process (ICAAP). Such monitoring should be included in the supervisory review process. In particular, after the entry into force of the leverage ratio requirements, competent authorities should monitor the developments in the business model and corresponding risk profile in order to ensure up to date and proper classification of institutions.

(97) Good governance structures, transparency and disclosure are essential for sound remuneration policies. In order to ensure adequate transparency to the market of their remuneration structures and the associated risk, institutions should disclose detailed information on their remuneration policies, practices and, for reasons of confidentiality, aggregated amounts for those members of staff whose professional activities have a material impact on the risk profile of the institution. That information should be made available to all stakeholders. Those particular requirements should be without prejudice to more general disclosure requirements concerning remuneration policies applicable horizontally across sectors. Moreover, Member States should be allowed to require institutions to make available more detailed information on remuneration.

(98) The recognition of a credit rating agency as an external credit assessment institution (ECAI) should not increase the foreclosure of a market already dominated by three main undertakings. EBA and ESCB central banks, without making the process easier or less demanding, should provide for the recognition of more credit rating agencies as ECAIs as a way to open the market to other undertakings.

(99) Directive 95/46/EC of the European Parliament and of the Council of 24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data[16] and Regulation (EC) No 45/2001 of the European Parliament and of the Council of 18 December 2000 on the protection of individuals with regard to the processing of personal data by the Community institutions and bodies and on the free movement of such data[17], should be fully applicable to the processing of personal data for the purposes of this Regulation.

(100) Institutions should hold a diversified buffer of liquid assets that they can use to cover liquidity needs in a short term liquidity stress. As it is not possible to know ex ante with certainty which specific assets within each asset class might be subject to shocks ex post,

it is appropriate to promote a diversified and high-quality liquidity buffer consisting of different asset categories. A concentration of assets and overreliance on market liquidity creates systemic risk to the financial sector and should be avoided. A broad set of quality assets should therefore be taken into consideration during an initial observation period which will be used for the development of a definition of a liquidity coverage requirement. When making a uniform definition of liquid assets at least government bonds, and covered bonds traded on transparent markets with an ongoing turnover would be expected to be considered assets of extremely high liquidity and credit quality. It would also be appropriate that assets corresponding to Article 416(1)(a) to (c) should be included in the buffer without limitations. When institutions use the liquidity stock, they should put in place a plan to restore their holdings of liquid assets and competent authorities should ensure the adequacy of the plan and its implementation.

(101) The stock of liquid assets should be available at any time to meet the liquidity outflows. The level of liquidity needs in a short term liquidity stress should be determined in a standardised manner so as to ensure a uniform soundness standard and a level playing field. It should be ensured that such a standardised determination has no unintended consequences for financial markets, credit extension and economic growth, also taking into account different business and investment models and funding environments of institutions across the Union. To this end, the liquidity coverage requirement should be subject to an observation period. Based on the observations and supported by reports from EBA, the Commission should be empowered to adopt a delegated act to introduce in a timely manner a detailed and harmonised liquidity coverage requirement for the Union. In order to ensure global harmonisation in the area of regulation of liquidity any delegated act to introduce the liquidity coverage requirement should be comparable to the liquidity coverage ratio set out in the final international framework for liquidity risk measurement, standards and monitoring of the BCBS taking into account Union and national specificities.

(102) To that end, during the observation period, EBA should review and assess, inter alia the appropriateness of a threshold of 60 % on level 1 liquid assets, a cap of 75 % of inflows to outflows and the phase-in of the liquidity coverage requirement from 60 % from 1 January 2015 increasing on a graduated basis to 100 %. When assessing and reporting on the uniform definitions of the stock of liquid assets, EBA should have regard to the BCBS definition of high quality liquid assets (HQLA) for the basis of its analysis, taking Union and national specificities into account. While EBA should identify those currencies where the needs of institutions established in the Union for liquid assets exceeds the availability of those liquid assets in that currency, EBA should also annually examine whether derogations, including those identified in this Regulation, should be applied. In addition, EBA should assess annually whether in relation to any such derogation as well as derogations already identified in this Regulation, any additional conditions should be attached to their use by institutions established in the Union or whether existing conditions should be revised. EBA should submit the results of its analysis in an annual report to the Commission.

(103) With a view to increasing efficiency and reducing the administrative burden, EBA should set up a coherent reporting framework on the basis of a harmonised set of

standards for liquidity requirements that should be applied across the Union. To this end, EBA should develop uniform reporting formats and IT solutions that take into account the provisions of this Regulation and Directive 2013/36/EU. Until the date of application of the full liquidity requirements, institutions should continue to meet their national reporting requirements.

(104) EBA, in cooperation with the ESRB, should issue guidance on the principles for use of liquid stock in a stress situation.

(105) It should not be taken for granted that institutions will receive liquidity support from other institutions belonging to the same group when they experience difficulties in meeting their payment obligations. However, subject to stringent conditions and the individual agreement of all competent authorities involved, competent authorities should be able to waive the application of the liquidity requirement for individual institutions and subject those institutions to a consolidated requirement, in order to allow them to manage their liquidity centrally at group or sub-group level.

(106) In the same vein, where no waiver is granted, liquidity flows between two institutions belonging to the same group and which are subject to consolidated supervision, should, when the liquidity requirement becomes a binding measure, receive preferential inflow and outflow rates only in those cases where all the necessary safeguards are in place. Such specific preferential treatments should be narrowly defined and linked to the fulfilment of a number of stringent and objective conditions. The specific treatment applicable to a given intragroup flow should be obtained through a methodology using objective criteria and parameters in order to determine specific levels of inflows and outflows between the institution and the counterparty. Based on the observations and supported by the EBA report, the Commission should, as appropriate and as part of the delegated act which it adopts pursuant to this Regulation to specify the liquidity coverage requirement, be empowered to adopt delegated acts to lay down those specific intragroup treatments, the methodology and the objective criteria to which they are linked as well as joint decision modalities for the assessment of those criteria.

(107) Bonds issued by the National Asset Management Agency (NAMA) in Ireland are of particular importance to the Irish banking recovery and their issue has been granted prior approval by the Member States, and approved as a State aid by the Commission as a support measure introduced to remove impaired assets from the balance sheets of certain credit institutions. The issuance of such bonds, a transitional measure supported by the Commission and the ECB, is an integral part in the restructuring of the Irish banking system. Such bonds are guaranteed by the Irish government and are eligible collateral with monetary authorities. The Commission should address specific grandfathering mechanisms of transferable assets issued or guaranteed by entities with Union State aid approval, as part of the delegated act which it adopts pursuant to this Regulation to specify the liquidity coverage requirement. In that regard the Commission should take into account the fact that institutions calculating the liquidity coverage requirements in accordance with this Regulation should be permitted to include NAMA senior bonds as assets of extremely high liquidity and credit quality until December 2019.

(108) Similarly, the bonds issued by the Spanish Asset Management Company are of particular importance to the Spanish banking recovery and are a transitional measure supported by the Commission and the ECB, as an integral part in the restructuring of the Spanish banking system. Since their issuance is provided for in the Memorandum of Understanding on Financial Sector Policy Conditionality signed by the Commission and the Spanish Authorities on 23 July 2012, and the transfer of assets requires approval by the Commission as a State aid measure introduced to remove impaired assets from the balance sheets of certain credit institutions, and to the extent they are guaranteed by the Spanish government and are eligible collateral with monetary authorities. The Commission should address specific grandfathering mechanisms of transferable assets issued or guaranteed by entities with Union State aid approval as part of the delegated act which it adopts pursuant to this Regulation to specify the liquidity coverage requirement. In that regard the Commission should take into account the fact that institutions calculating the liquidity coverage requirements in accordance with this Regulation should be permitted to include Spanish Asset Management Company senior bonds as assets of extremely high liquidity and credit quality until at least December 2023.

(109) On the basis of the reports which EBA is required to submit and when preparing the proposal for a delegated act on liquidity requirements, the Commission should also consider if senior bonds issued by legal entities similar to NAMA in Ireland or the Spanish Asset Management Company, established for the same purpose and of particular importance for bank recovery in any other Member State, should be granted such treatment, to the extent they are guaranteed by the central government of the relevant Member State and are eligible collateral with monetary authorities.

(110) In developing draft regulatory technical standards to determine methods for the measurement of additional outflow, EBA should consider a historical look back standardised approach as a method of such measurement.

(111) Pending the introduction of the net stable funding ratio (NSFR) as a binding minimum standard, institutions should observe a general funding obligation. The general funding obligation should not be a ratio requirement. If, pending the introduction of the NSFR, a stable funding ratio is introduced as a minimum standard by way of a national provision, institutions should comply with this minimum standard accordingly.

(112) Apart from short-term liquidity needs, institutions should also adopt funding structures that are stable over a longer term horizon. In December 2010, the BCBS agreed that the NSFR will move to a minimum standard by 1 January 2018 and that the BCBS will put in place rigorous reporting processes to monitor the ratio during a transition period and will continue to review the implications of these standards for financial markets, credit extension and economic growth, addressing unintended consequences as necessary. The BCBS thus agreed that the NSFR will be subject to an observation period and will include a review clause. In that context, EBA should, based on reporting required by this Regulation, evaluate how a stable funding requirement should be designed. Based on this evaluation, the Commission should report to the European Parliament

and the Council together with any appropriate proposals in order to introduce such a requirement by 2018.

(113) Weaknesses in corporate governance in a number of institutions have contributed to excessive and imprudent risk-taking in the banking sector which led to the failure of individual institutions and systemic problems.

(114) In order to facilitate the monitoring of institutions' corporate governance practices and improve market discipline, institutions should publicly disclose their corporate governance arrangements. Their management bodies should approve and publicly disclose a statement providing assurance to the public that these arrangements are adequate and efficient.

(115) In order to take account of the diversity of business models of institutions in the internal market certain long-term structural requirements such as the NSFR and the leverage ratio should be examined closely with a view of promoting a variety of sound banking structures which have been and should continue to of service to the Union's economy.

(116) For the continuous provision of financial services to households and firms a stable funding structure is necessary. Long-term funding flows in bank-based financial systems in many Member States may generally possess different characteristics than those found in other international markets. In addition, specific funding structures may have developed in Member States to provide stable financing for long-term investment, including decentralised banking structures to channel liquidity or specialised mortgage securities which trade on highly liquid markets or are a welcome investment for long-term investors. Those structural factors should be carefully considered. It is essential to that purpose that, once international standards are finalised, EBA and the ESRB, based on reporting required by this Regulation, evaluate how a stable funding requirement should be designed fully taking into account the diversity of funding structures in the banking market in the Union.

(117) In order to ensure progressive convergence between the level of own funds and the prudential adjustments applied to the definition of own funds across the Union and to the definition of own funds laid down in this Regulation during a transition period, the phasing in of the own funds requirements of this Regulation should occur gradually. It is vital to ensure that this phasing in is consistent with the recent enhancements made by Member States to the required levels of own funds and to the definition of own funds in place in the Member States. To that end, during the transition period the competent authorities should determine within defined lower and upper limits how rapidly to introduce the required level of own funds and prudential adjustments laid down in this Regulation.

(118) In order to facilitate smooth transition from divergent prudential adjustments currently applied in Member States to the set of prudential adjustments laid down in this Regulation, competent authorities should be able during a transition period to continue to require institutions, to a limited extent, to make prudential adjustments to own funds that are a derogation from this Regulation.

(119) In order to ensure that institutions have sufficient time to meet the new required levels and definition of own funds, certain capital instruments that do not comply with the definition of own funds laid down in this Regulation should be phased out between 1 January 2013 and 31 December 2021. In addition, certain state-injected instruments should be recognised fully in own funds for a limited period. Furthermore, share premium accounts related to items that qualified as own funds under national transposition measures for Directive 2006/48/EC should under certain circumstances qualify as Common Equity Tier 1.

(120) In order to ensure progressive convergence towards uniform rules on disclosure by institutions to provide market participants with accurate and comprehensive information regarding the risk profile of individual institutions, disclosure requirements should be phased in gradually.

(121) In order to take account of market developments and experience in the application of this Regulation, the Commission should be required to submit reports to the European Parliament and to the Council, together with legislative proposals, where appropriate, on the possible effect of capital requirements on the economic cycle of minimum, own funds requirements for exposures in the form of covered bonds, large exposures, liquidity requirements, leverage, exposures to transferred credit risk, counterparty credit risk and the original exposure method, retail exposures, on the definition of eligible capital, and the level of application of this Regulation.

(122) The primary purpose of the legal framework for credit institutions should be to ensure the operation of vital services to the real economy while limiting the risk of moral hazard. The structural separation of retail and investment banking activities within a banking group could be one of the key tools to support this objective. No provision in the current regulatory framework should therefore prevent the introduction of measures to effect such a separation. The Commission should be required to analyse the issue of structural separation in the Union and submit a report, together with legislative proposals, if appropriate, to the European Parliament and the Council.

(123) Similarly, with a view to protecting depositors and preserving financial stability, Member States should also be permitted to adopt structural measures that require credit institutions authorised in that Member State to reduce their exposures to different legal entities depending on their activities, irrespective of where those activities are located. However, because such measures could have a negative impact by fragmenting the internal market, they should only be approved subject to strict conditions pending the entry into force of a future legal act explicitly harmonising such measures.

(124) In order to specify the requirements set out in this Regulation, the power to adopt acts in accordance with Article 290 TFEU should be delegated to the Commission in respect of technical adjustments to this Regulation to clarify definitions to ensure uniform application of this Regulation or to take account of developments on financial markets, to align terminology on, and frame definitions in accordance with, subsequent relevant acts, to adjust the provisions of this Regulation on own funds to reflect developments in accounting standards or Union law, or with regard to the convergence of supervisory practices, to expand the lists of exposure classes for the purposes of the Standardised

Approach or the IRB Approach to take account of developments on financial markets, to adjust certain amounts relevant to those exposure classes to take into account the effects of inflation; to adjust the list and classification of off- balance sheet items and to adjust specific provisions and technical criteria on the treatment of counterparty credit risk, the Standardised Approach and the IRB Approach, credit risk mitigation, securitisation, operational risk, market risk, liquidity, leverage and disclosure in order to take account of developments on financial markets or in accounting standards or Union law, or with regard to the convergence of supervisory practices and risk measurement and to take account of the outcome of the review of various matters relating to the scope of Directive 2004/39/EC.

(125) The power to adopt acts in accordance with Article 290 TFEU should also be delegated to the Commission in respect of prescribing a temporary reduction in the level of own funds or risk weights specified under this Regulation in order to take account of specific circumstances, to clarify the exemption of certain exposures from the application of provisions of this Regulation on large exposures, to specify amounts relevant to the calculation of capital requirements for the trading book to take account of developments in the economic and monetary field, to adjust the categories of investment firms eligible for certain derogations to required levels of own funds to take account of developments on financial markets, to clarify the requirement that investment firms hold own funds equivalent to one quarter of their fixed overheads of the preceding year to ensure uniform application of this Regulation, to determine the elements of own funds from which deductions of an institution's holdings of the instruments of relevant entities should be made, to introduce additional transitional provisions relating to the treatment of actuarial gains and losses in measuring defined benefit pension liabilities of institutions. It is of particular importance that the Commission carry out appropriate consultations during its preparatory work, including at expert level. The Commission, when preparing and drawing up delegated acts, should ensure a simultaneous, timely and appropriate transmission of relevant documents to the European Parliament and to the Council.

(126) In accordance with Declaration No 39 on Article 290 TFEU, the Commission should continue to consult experts appointed by the Member States in the preparation of draft delegated acts in the financial services area, in accordance with its established practice.

(127) Technical standards in financial services should ensure harmonisation, uniform conditions and adequate protection of depositors, investors and consumers across the Union. As a body with highly specialised expertise, it would be efficient and appropriate to entrust EBA with the elaboration of draft regulatory and implementing technical standards which do not involve policy choices, for submission to the Commission. EBA should ensure efficient administrative and reporting processes when drafting technical standards. The reporting formats should be proportionate to the nature, scale and complexity of the activities of the institutions.

(128) The Commission should adopt draft regulatory technical standards developed by EBA in the areas of mutuals, cooperative societies, savings institutions or similar institutions, certain own funds instruments, prudential adjustments, deductions from own funds,

additional own funds instruments, minority interests, services ancillary to banking, the treatment of credit risk adjustment, probability of default, loss given default, approaches to risk-weighting of assets, convergence of supervisory practices, liquidity, and transitional arrangements for own funds, by means of delegated acts pursuant to Article 290 TFEU and in accordance with Articles 10 to 14 of Regulation (EU) No 1093/2010. It is of particular importance that the Commission carry out appropriate consultations during its preparatory work, including at expert level. The Commission and EBA should ensure that those standards and requirements can be applied by all institutions concerned in a manner that is proportionate to the nature, scale and complexity of those institutions and their activities.

(129) The implementation of some delegated acts provided for in this Regulation, such as the delegated act concerning the liquidity coverage requirement, may potentially have a substantial impact on supervised institutions and the real economy. The Commission should ensure that the European Parliament and the Council are always well informed about relevant developments at international level and current thinking within the Commission well before the publication of delegated acts.

(130) The Commission should also be empowered to adopt implementing technical standards developed by EBA with regard to consolidation, joint decisions, reporting, disclosure, exposures secured by mortgages, risk assessment, approaches to risk-weighting of assets, risk-weights and specification of certain exposures, the treatment of options and warrants, positions in equity instruments and foreign exchange, the use of internal models, leverage, and off-balance sheet items by means of implementing acts pursuant to Article 291 TFEU and in accordance with Article 15 of Regulation (EU) No 1093/2010.

(131) Given the detail and number of regulatory technical standards that are to be adopted pursuant to this Regulation, where the Commission adopts a regulatory technical standard which is the same as the draft regulatory technical standard submitted by EBA, the period within which the European Parliament or the Council may object to a regulatory technical standard, should, where appropriate, be further extended by one month. Moreover, the Commission should aim to adopt the regulatory technical standards in good time to permit the European Parliament and the Council to exercise full scrutiny, taking account of the volume and complexity of regulatory technical standards and the details of the European Parliament's and the Council's rules of procedure, calendar of work and composition.

(132) In order to ensure a high degree of transparency, EBA should launch consultations relating to the draft technical standards referred to in this Regulation. EBA and the Commission should start preparing their reports on liquidity requirements and leverage, as provided for in this Regulation, as soon as possible.

(133) In order to ensure uniform conditions for the implementation of this Regulation, implementing powers should be conferred on the Commission. Those powers should be exercised in accordance with Regulation (EU) No 182/2011 of the European Parliament and of the Council of 16 February 2011 laying down the rules and general principles

concerning mechanisms for control by the Member States of the Commission's exercise of implementing powers[18].

(134) In accordance with Article 345 TFEU, which provides that the Treaties are in no way to prejudice the rules in Member States governing the system of property ownership, this Regulation neither favours nor discriminates against types of ownership which are within its scope.

(135) The European Data Protection Supervisor has been consulted in accordance with Article 28(2) of Regulation (EC) No 45/2001 and has adopted an opinion[19].

(136) Regulation (EU) No 648/2012 should be amended accordingly,

HAVE ADOPTED THIS REGULATION:

(1) OJ C 105, 11.4.2012, p. 1.

(2) OJ C 68, 6.3.2012, p. 39.

(3) OJ L 177, 30.6.2006, p. 1.

(4) OJ L 177, 30.6.2006, p. 201.

(5) See page 338 of this Official Journal.

(6) OJ L 331, 15.12.2010, p. 1.

(7) OJ L 331, 15.12.2010, p. 12.

(8) Council Decision 2009/937/EU of 1 December 2009 adopting the Council's Rules of Procedure (OJ L 325, 11.12.2009, p. 35).

(9) OJ L 372, 31.12.1986, p. 1.

(10) OJ L 193, 18.7.1983, p. 1.

(11) OJ L 243, 11.9.2002, p. 1.

(12) OJ L 145, 30.4.2004, p. 1.

(13) OJ L 35, 11.2.2003, p. 1.

(14) OJ L 201, 27.7.2012, p. 1.

(15) OJ L 302, 17.11.2009, p. 97.

(16) OJ L 281, 23.11.1995, p. 31.

(17) OJ L 8, 12.1.2001, p. 1.

(18) OJ L 55, 28.2.2011, p. 13.

(19) OJ C 175, 19.6.2012, p. 1.