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Revision of regulatory framework
CRR / CRD IV

Conference on Completing the Banking Union

Wednesday, 14 February 2018

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EU banking reform: components

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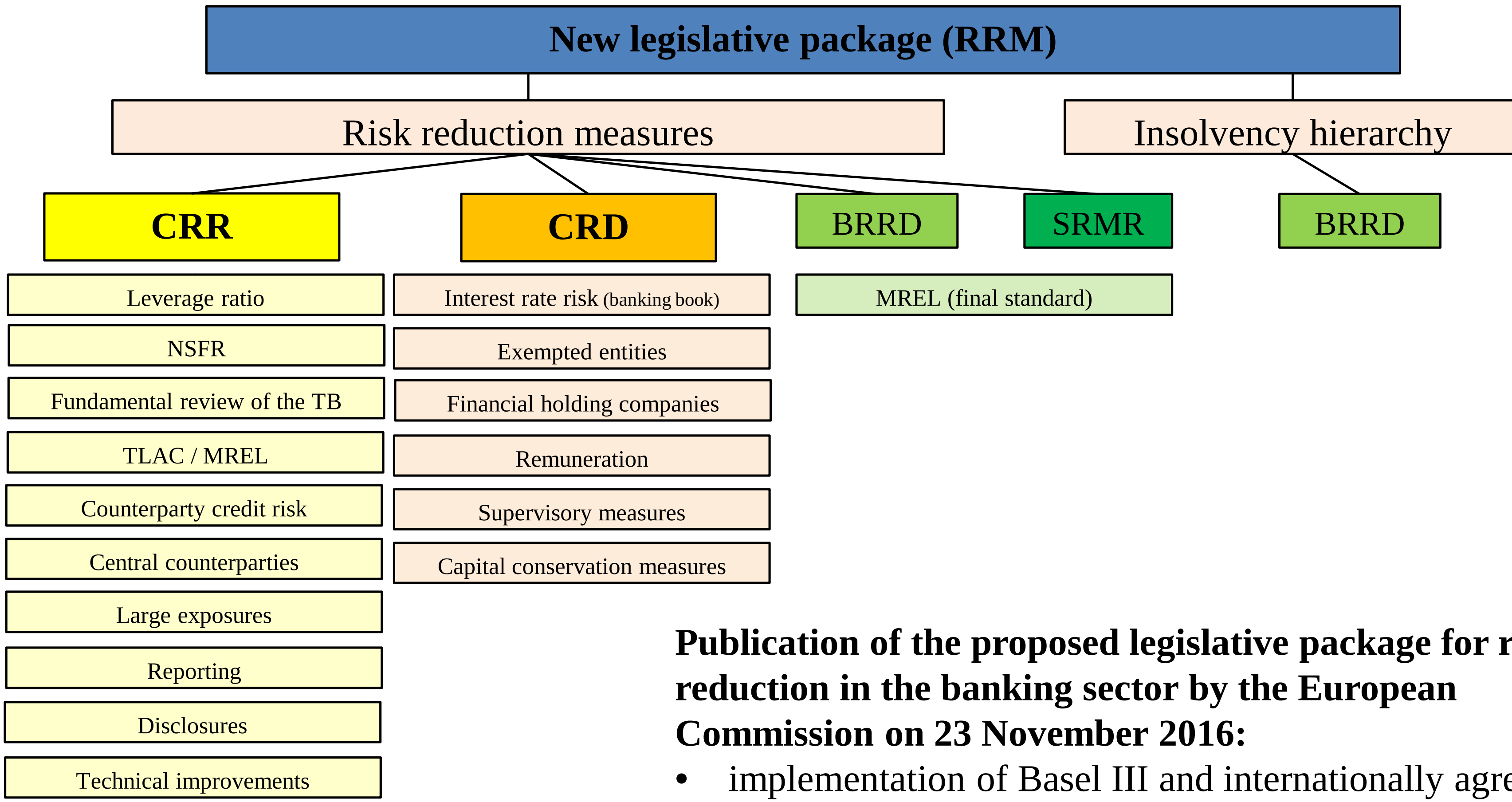

Publication of the proposed legislative package for risk reduction in the banking sector by the European Commission on 23 November 2016:

- implementation of Basel III and internationally agreed standards of resolution in EU legislation
- amendments of various elements of the regulatory framework

Bank of Slovenia's position with regard to the European Commission proposal

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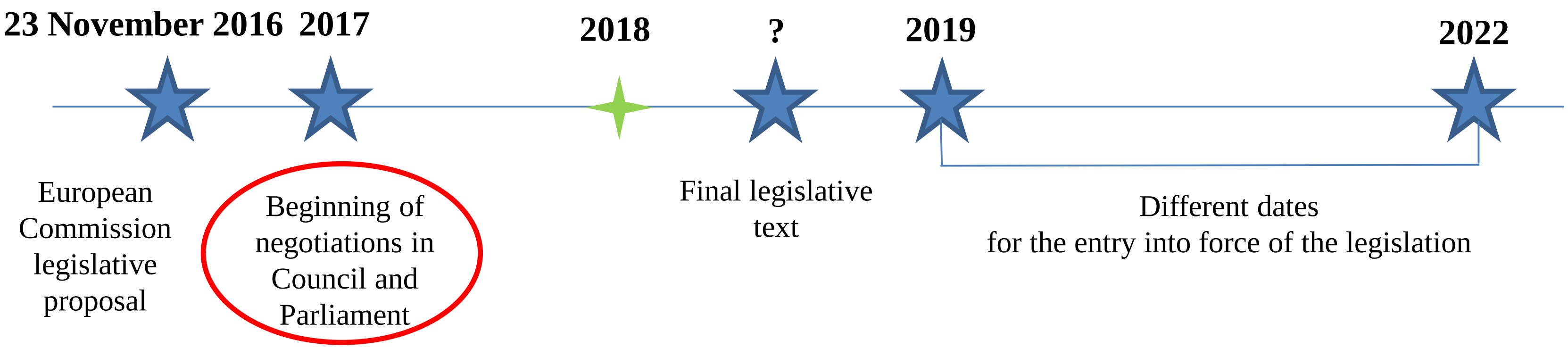
- **Bank of Slovenia support in principle further reform of the risk reduction measures in the banking system**
- **Support for proposals that:**
  - introduce greater clarity into legislative text
  - give the supervisor greater flexibility in exercising supervisory powers
  - apply the principle of proportionality in regulations and supervision
  - level the playing field for banking operations inside and outside the EU
- **Reservations with regard to proposals that:**
  - are unclear from the perspective of consequences or application in practice
  - increase the complexity of rules while adding limited substantive value
  - restrict the basis for conducting supervision in practice
  - fail to take account of actual burden-sharing in the event of bank difficulties

EU banking reform: timetable



<u>Negotiations at the EU Council</u>:

- Malta presidency
  - general approach (transitional arrangements for IFRS 9 and insolvency hierarchy)
  - progress on key issues
- Estonia presidency
  - completion of trilogue with regard to compromise proposal for IFRS 9 and insolvency hierarchy, and publication of new CRR and BRRD in OJ EU
  - continuation of negotiations in connection with other issues
- Bulgaria presidency
  - general approach to RRM package in March 2018

EU banking reform: legislative process

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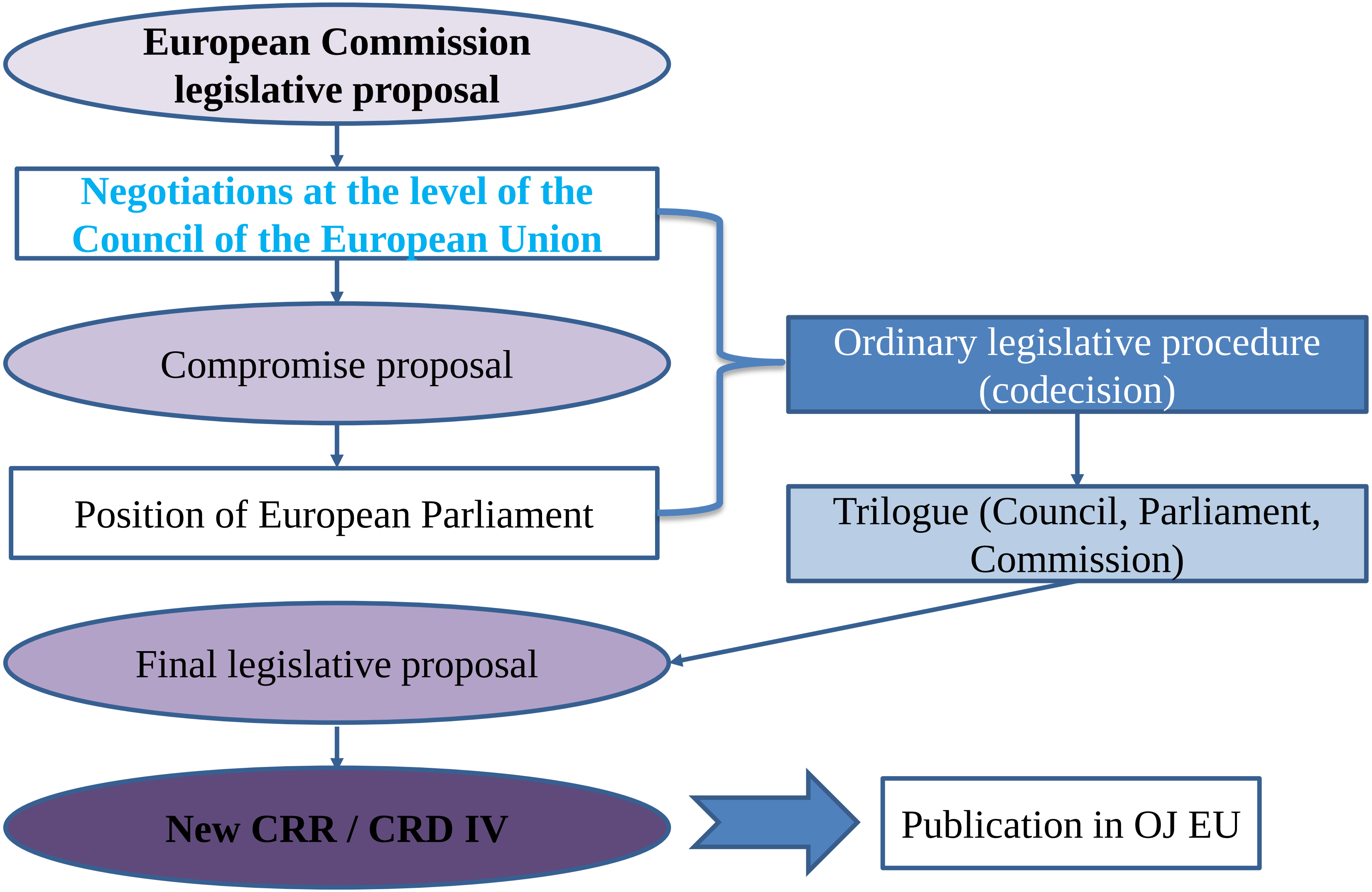

Prudential impact of IFRS 9 on capital

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1. **Procedure:**
   - separate legislative procedure (fast-track)
   - publication of final regulation in December 2017
   - effective as of 1 January 2018 (consistent with effective date of IFRS 9)

2. **Purpose:**
   - mitigation of potential adverse impact on impairments and provisions from application of IFRS 9 to CET1

3. **Content:**
   a. length of transition: 5 years (2018 to 2022)
   b. decision on application: by institution (subsequent decision on application with supervisor’s permission)
   c. approach:
      - static, potential upgrade with dynamic component
      - gradual introduction (5%, 15%, 30%, 50% and 75%)
   d. elimination of double-counting effects: recalculations of RWA, DTA and T2
   e. disclosures: capital, capital ratios, leverage ratio

Proportionality - reporting

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1. **Purpose**: reducing costs from the perspective of reporting and strengthening proportionality with regard to the size and complexity of the institution

2. **Content:**
   a. definition of small institution: average value of assets over the four-year period ≤ EUR 1.5 billion
   b. reduce granularity of reporting for small institutions
   c. EBA mandate with regard to assessment of costs and benefits of regulatory reporting
   d. clarification of duplication of reporting (potential waivers)
   e. development of IT tools for compliance by EBA

3. **Expected impact:**
   - reduction in reporting burden and costs
   - maintenance of sufficient bases for banking supervision

Proportionality - disclosures

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1. **Purpose**: strengthening of proportionality with regard to the size and complexity of the institution, compliance with international standards and adjustment to changes in legislation

2. **Content:**
   a. classification of institutions into three categories: large, small and other, with further distinction between listed and non-listed institutions
   b. scope of disclosures with regard to categorisation (sliding scale), with differentiation in the substance and frequency of disclosures
   c. key prudential metrics table:
      - minimum standards for all banks
      - own funds, RWA, P2R, CBR, LR, LCR, NSFR, MREL

3. **Expected impact:**
   - reduction in administrative burden and costs
   - comparability of disclosures at global level

Proportionality - remuneration

1. **Purpose**: elimination of disproportionality of certain existing rules for the smallest, less-complex institutions, and for staff with low variable remuneration

2. **Content:**
   a. derogations from the rules on deferral for the variable remuneration can be exercised for:
      ~ small, less-complex banks: total asset value ≤ EUR 5 billion
      ~ staff with variable remuneration ≤ EUR 50.000
   b. listed institutions may provide variable remuneration in the form of share-linked instruments

3. **Expected impact:**
   - reduction in administrative burden

Pillar 2: requirements and guidance

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1. **Purpose**: consistent application of rules, greater clarity

2. **Content:**
   a. introduction of Pillar 2 requirements (P2R) and Pillar 2 guidance (P2G)
   b. clarification of conditions for setting P2R
   c. clarification of stacking order and restrictions on distributions (P1, P2R, TLAC/MREL, CBR, P2G)
   d. exclusion of macroprudential component from P2R
   e. composition of capital for P2R
   f. P2R disclosures

3. **Expected impact:**
   – a level playing field for implementing Pillar 2 for all institutions
   – greater legal certainty

Macroprudential framework

1. **Purpose**: ensuring a flexible and comprehensive macroprudential toolbox, simplifying procedural requirements

2. **Content:**
   a. clarification of scope of SRB and O-SII buffer
   b. additivity and overall cap of O-SII buffer and SRB
   c. changes to O-SII buffer cap
   d. clarification of procedures (notifications, opinions, approvals) for application

3. **Expected impact:**
   – potential increase in capital requirements for preventing excessive increase in systemic risk

FHCs and MFHCs

1. **Purpose**: direct responsibility of parent (mixed) financial holding companies for compliance with prudential requirements

2. **Content:**
   a. procedure for granting authorisations for parent FHCs/MFHCs by consolidated supervisor
   b. conditions for obtaining authorisation
   c. conditions for withdrawing authorisation

3. **Expected impact:**
   – granting of authorisations for existing groups in the transitional period
   – greater legal certainty with regard to the responsibilities for the fulfilment of consolidated requirements

SME supporting factor

1. **Purpose**: further recalibration of capital requirements for exposures to SMEs with regard to their riskiness

2. **Content:**
   a. current treatment: 23.81% reduction in capital requirement for exposures ≤ EUR 1.5 million
   b. additional reduction of 15% in capital requirement for exposures > EUR 1.5 million

3. **Expected impact:**
   - incentives for increased lending to SMEs
   - lower capital requirements for aforementioned portfolio

Waivers from capital and liquidity

1. **Purpose**: more flexibility regarding waivers from prudential requirements for groups inside the SSM

2. **Content:**
   a. use of waivers from capital and liquidity requirements for subsidiary institutions headquartered in a different Member State from the parent institution but inside the SSM
   b. introduction of safeguards (guarantee for the waived requirement by parent undertaking)

3. **Expected impact:**
   – deletion of the proposed amendments at this stage

Basel standards (1/2)

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1. **Purpose:** compliance with international standards

2. **Content:**
   a. leverage ratio (LR)
   - binding LR of 3% (Tier 1 capital / total risk exposure)
   - prevent excessive leverage
   - introduce a backstop to risk-based capital requirements

   b. net stable funding ratio (NSFR)
   - binding requirement for NSFR (min NSFR of 1, i.e. 100%)
   - limit excessive maturity mismatches
   - limit overreliance on short-term funding
   - complement LCR requirement

   c. large exposure
   - Tier 1 capital as the base for determining large exposure limits

Current: Basel standards (2/2)

d. fundamental review of trading book
- clearer rule on the scope of application (trading book vs banking book)
- new standardised approach
- strengthening the conditions for using internal models
- proportional treatments for banks with small- and medium-sized trading book
- making requirements more customised and proportionate to reflect more accurately the actual risks

e. interest rate risk in the banking book
– introduction of a common standardised approach that institution might use to capture risks
– treatment remains part of P2R

3. Expected impact:
– limited impact on Slovenian banks

Challenges of future revisions to EU banking legislation

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- **Implementation of Basel agreement from December 2017**
  - comprehensive study of impact on EU banks
  - consideration of specificities of business models of EU banks
- **Reduction of options and discretions**
  - discretions of Member State / discretions of competent authority
  - clear delineation between microprudential and macroprudential powers, and the ECB and national supervisors
- **Completion of the banking union**
  - remaining elements of the RRM package
  - EDIS
  - …..

→ **Stable institutional and regulatory framework for banks and supervisors**