EMF ECBC Market Insights & Updates 05.2016

May 2016

Summary

Contact:
EMF-ECBC Secretariat
Tel: +32 2 285 40 30
E-mail: emfinfo@hypo.org
Web: www.hypo.org

European Mortgage Federation

ECBC European Covered Bond Council

TO RECEIVE MARKET INSIGHTS & UPDATES IN YOUR MAILBOX EVERY MONTH, PLEASE CLICK HERE

Basel IV – Challenges & Opportunities

By Bruno Deletré, Director General, Crédit Foncier de France & Chairman of the European Mortgage Federation (EMF)

"Basel IV" is the term that is being widely used to refer to a series of new measures from the Basel Committee on Banking Supervision (BCBS) to enhance methods banks must use to calculate risk and therefore how much capital they should set aside. Key changes are being made in relation to **credit risk**, operational risk, market risk, and large exposures. The reforms to the calculation of credit risk, which include a new standardised approach, limits on how banks calibrate IRB models and possibly new floors, will almost certainly represent a game change for the mortgage and covered bond industries in terms of minimum capital requirements and disclosed capital ratios. The BCBS has repeatedly assured the market that it has no intention of significantly increasing overall capital requirements; however, if the conservative nature of the calibration of the proposals so far are anything to go by, there is a real risk that there will be a significant additional tightening of capital requirements.

With the potentially significant impact of the new regulatory landscape on the mortgage industry in mind, the EMF-ECBC has been analysing the revisions from both funding and origination perspectives and has been developing a coordinated approach in examining and responding to all consultation papers published by the BCBS and the European Institutions.

Most recently, the EMF-ECBC responded to the second BCBS consultation on the revision to the standardised approach. In this second version, although improvements have been made, there are still a number of proposals of significant concern for the mortgage and covered bond industries. The EMF-ECBC highlighted the following key points in its official response to the consultation in March 2016:

- Given the diversity of global real estate (RE) markets in terms of risk profile, a one-size-fits-all approach is not appropriate.
- There should be consistency between risk weights across different exposure classes, so that secured

exposures are not penalised compared to unsecured exposures.

- The proposed risk weights lead to significantly higher standardised approach capital charges for higher LTV loans. Loan splitting could help limit this impact and avoid threshold effects that would trigger regulatory arbitrage in the future.
- A more balanced approach is needed for Income Producing Real Estate as there is no evidence that cash flow producing real estate is generally riskier exposure.
- A fine-tuning of operational requirements is needed with regards to recognition of guarantees and financial collaterals, and valuation basis and frequency.
- The standardised approach and capital floors consultations should be seen together because the capital floors will be based upon the standardised approach.

With regards to the last point it is important to mention that the impact of floors on the capital charge could be significant. A 60-90% output floor for IRB banks, as suggested by the Basel Committee in the IRB consultation, would be of great concern. The EMF-ECBC is currently examining the IRB consultation with a view to delivering its comments by the June 2016 deadline.

It has been suggested in the press that Basel IV could cost the world's largest banks some €115 billion in extra capital and that European banks would bear the brunt of the new costs coming from the BCBS: around €70 billion of the total. As a consequence, there seems to be a consensus across many and relevant jurisdictions on the need to limit the increase of risk weights, for instance by allowing loan splitting. We are glad to see that on arguably the most important issues several global regions are very much aligned.

Basel IV is not the only regulatory concern on the Industry's radar. The calibration of the leverage ratio (LR) and of the net stable funding requirements (NSFR) at EU level are of the utmost importance too. The European Commission is expected to announce its intentions with regard to both by the end of 2016. The EMF-ECBC has already commented extensively on both files and has been in regular dialogue with the European Commission and European Banking Authority (EBA). Recent and expected developments at EBA level – i.e. the publication of its NSFR Report in December 2015 and the forthcoming publication of its LR report, expected in July 2016, have resulted in an updated EMF-ECBC Position Paper on the NSFR and will prompt further internal considerations on the LR (watch this space for an updated EMF-ECBC Position Paper on this file too).

The EMF-ECBC is playing the role of a discussion forum here and acting as a catalyst by trying to analyse and increase awareness of the potential impact of the measures under discussion, as well as to take the lead in proposing pan-European market initiatives which could ensure financial stability and market due diligence. In this context, on the 3rd of June 2016, the EMF-ECBC will bring together its decision-makers, in the form of its Executive and Steering Committees, with senior representatives of the BCBS and the European Commission to exchange views on the challenges of the ongoing and upcoming regulatory changes for the mortgage and covered bond industries. The panel will also consider a current EMF-ECBC initiative, a solely market initiative, to bring energy efficient mortgages to borrowers on a mainstream scale, which will deliver micro-economic benefits to all of the actors in the chain: borrowers, lenders, investors, governments etc. in terms of wealth conservation, risk mitigation, capital relief and energy savings – a "win-win" situation. We believe that dialogue amongst stakeholders will play a pivotal role. Exchanging views on the current challenges and opportunities is a constructive way to pave the way for the future of the mortgage and covered bond industries in Europe. We are all aware that more has to be done and we are ready to contribute to growth and financial stability by securing the European approach to banking in the current global debate on the future of the financial system.

We will be posting regular updates on this initiative in future editions of our newsletter and also on our blog, so keep an eye open for the latest news!

New opening of the Polish covered bond market

By Jakub Niesłuchowski, Deputy CEO, PKO Bank Hipoteczny S.A.

NEW OPENING

On the 1st of January 2016 the new Polish Law on Covered Bonds and Mortgage Banks entered into force. This represents a fundamental change of the legal framework for mortgage banks and covered bonds. In the period between 1997-2015, the business of Polish mortgage banks and covered bond issuances have not developed as originally expected due to a number of factors such as cheap funding from parent banks abroad for mortgage lending, internal competition between universal and mortgage banks, and – last but not least – constraints resulting from existing laws. Hence, the new law creates a unique window of opportunity for the dynamic expansion of the covered bond market. The amended law will substantially improve the covered bond market in Poland in at least three major areas:

1. Increase of credibility and safety of covered bonds.
2. Extension of covered bond supply.
3. Extension of demand for covered bonds.

The credibility and safety of Polish covered bonds is improved mainly through the introduction of the conditional pass-through structure. The changes implemented to the Polish regulations are in line with the best market practices and with recommendations of the European Central Bank (ECB) and credit rating agencies. According to the new regulations, upon declaration of a mortgage bank's insolvency, the maturity of the bank's obligations as an issuer of covered bonds is extended immediately by 12 months and the Asset Coverage Test and Liquidity Tests are applicable to determine repayment of interest and principal. Should the bank fail either of the tests, repayments will switch to a pass-through structure whereby the maturity of all bonds will be extended to the longest dated asset plus three years. Such a solution substantially reduces repayment risk to investors. Other changes introduce a minimum legal overcollateralisation requirement at the level of 10% and a mandatory liquidity reserve funded by mortgage banks using cash or eligible securities covering at least six months of interest due on the covered bonds outstanding.

The law amendment implemented on the 1st of January 2016 should also support the supply of Polish covered bonds. According to the new regulations, the refinancing limit for mortgage covered bonds has been increased from 60% to 80% of Mortgage Lending Value for residential property, which is also in line with the CRR definition of exposures in the form of covered bonds.

Additionally, the amended law should also stimulate demand due to the introduction of the exemption of foreign investors in covered bonds from withholding tax on all payments made under the covered bonds, and by implementation of the separate limit for investments in covered bonds made by domestic pension funds and credit unions.

The new law, which was widely discussed with the banking sector, the Polish Financial Supervision Authority and rating agencies during the legislation process, is a very robust basis for the stable development of the Polish covered bond market. All these elements increase the safety, soundness and the quality of the Polish covered bond market as they increase the potential to reach the rating at the level of the country ceiling (Aa3 for Poland in the case of Moody's).

HIGH POTENTIAL OF POLISH COVERED BOND MARKET

Poland is the largest country in Central Europe, with a population close to 39 million, and one of the biggest Member States of European Union. It has over 13.8 million dwellings spread across the country. Many of them are financed by mortgage loans, the outstanding level reaches almost PLN 400 bn. (EUR 93 bn.), of which c. 60% is denominated in PLN. However, there are still high housing needs and they are financed in a large part by mortgage loans. The housing deficit, as reflected in dwellings per 1,000 inhabitants, is 446 per 1,000 in Poland, while other countries such as Germany or the Czech Republic operate at the c. 550-600 level (based on 2014 data). The volume of mortgage loans in Poland has been steadily growing over the last 25 years but in relation to GDP it is still far behind EU average (20% vs. 50%).

The new legal framework, steady and dynamic development of residential mortgage loan volumes by continuous new sales based on PLN denominated loans, creates high potential for Polish covered bonds and a unique opportunity both for issuers and investors. Banking groups, especially those having subsidiary mortgage banks, can leverage these synergies by transferring portfolios from universal to mortgage banks and directing at least part of their new sales to mortgage banks and finance them by issuance of covered bonds.

Another important factor stimulating the covered bond market are the limitations on funding from international mother companies and the increasing need of Polish banks to find a new, long-term and stable source of financing, including meeting new funding requirements such as the Net Stable Funding Requirement (NSFR).

This is only the beginning of the story. There have already been a few issues of covered bonds in 2016 under the new law, but these have been predominantly allocated to domestic investors. However, the Polish jurisdiction can now significantly increase the supply of covered bonds by offering it also to international investors.

Figure 1 ▶ Mortgage loans new sales in Poland [PLN bn]

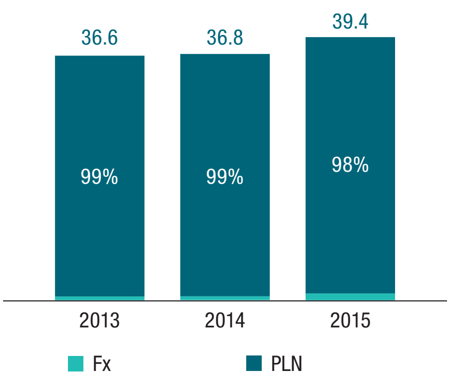
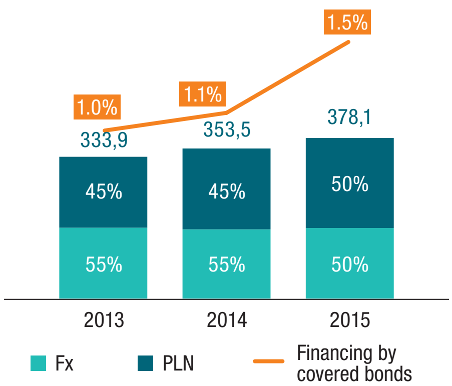


Figure 2 ▶ Outstanding value of mortgage loans in Poland [PLN bn]



PKO BANK HIPOTECZNY

PKO BP, the biggest Polish credit institution, established PKO Mortgage Bank (PKO Bank Hipoteczny), which began its operational activity in April 2015. PKO Group has the leading position in residential mortgages having a c. 25% share in outstanding volume and new sales. Its current portfolio includes c. PLN 60 bn. (EUR 14 bn.) of residential mortgages denominated in PLN. Part of this portfolio is being transferred from PKO Bank Polski to PKO Bank Hipoteczny and together with new sales directed to PKO Bank Hipoteczny, they will be financed by covered bonds.

PKO Bank Hipoteczny has successfully established a domestic covered bond programme and issued the first benchmark covered bonds in Poland secured only by residential mortgage loans denominated in PLN. Due to high quality of the cover pool and the new regulatory regime, Moody's has assigned to PKO Bank Hipoteczny covered bonds the highest possible rating for Polish financial instruments at the level of Aa3 (Country ceiling level). PKO Bank Hipoteczny has already started work on establishing an international programme and is planning to become a regular covered bonds issuer on the European market.

Figure 3 ▶ Dwellings per 1.000 inhabitants (over 18 years old) for 2014 [no.]

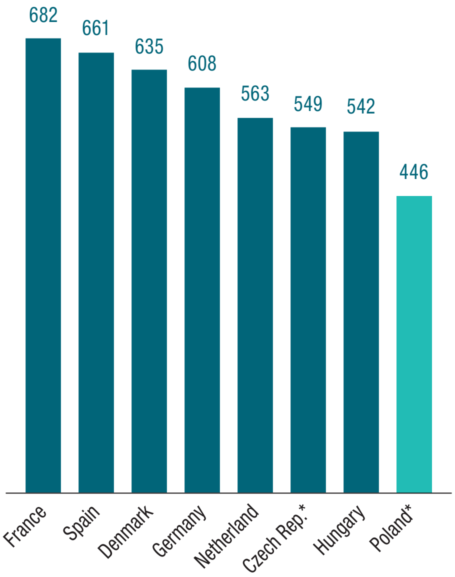
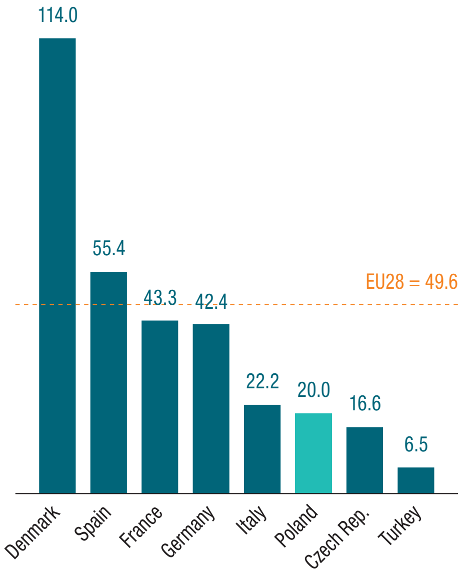


Figure 4 ▶ Total outstanding residential loans to GDP ratio for 2014 [%]



** Data as of 2013*

Source: National Bank of Poland, Polish Bank Association, banks' websites, EMF

Figure 4 ▶ Covered bond: one of the safest debt instruments in financial market

Bank Hipoteczny

8. Conditional pass-through structure

1. Covered bonds and mortgage banks in Poland are strictly regulated by the Act on covered bonds and mortgage banks, the banking law, the bankruptcy law, numerous resolutions of the Finance Ministry, and Polish FSA recommendations

7. Covered bonds exempt from bail-in (BRRD)

2. By law, covered bonds issuance in Poland is restricted to specialized mortgage banks

6. Segregation of assets through cover pool (only mortgages, cash, sovereign debt or similar)

3. Constant supervision by the Cover Pool Monitor (appointed by Polish FSA) over a mortgage bank activities and its cover pool

5. Strict regulatory limits on mortgage banks and covered bonds including min. 10% OC

4. Conservative approach to determining the mortgage lending value (through-the-cycle) of real estate

EMF-ECBC Updates its Position Paper on NSFR

By Jennifer Johnson, Head of Legal & Economic Affairs, EMF-ECBC

On the 11th of May 2016, the EMF-ECBC delivered an updated version of its July 2015 Paper on the Basel Committee on Banking Supervision's proposed Net Stable Funding Ratio (NSFR) Standard to the European Commission and the European Banking Authority (EBA). The Paper was updated notably to take account of the recommendations of the EBA in its December 2015 Report on the NSFR.

In its latest Paper, the EMF-ECBC cautions that the current NSFR proposal from the BCBS would unduly restrict the covered bond market and, as a result, long-term financing. The Industry also recalls that covered bonds played a pivotal role in bank wholesale funding during the recent financial turmoil as one of the only asset classes able to restore investor confidence and ensure access to debt capital markets for European issuers.

With this in mind, the EMF-ECBC advocates in particular the setting of Required Stable Funding (RSF) and Available Stable Funding (ASF) to zero for **interdependent assets and liabilities**, including all situations where a matching principle exists in law.

In **structures where there are no interdependent assets and liabilities**, the EMF-ECBC highlights:

(i) the potential for derogation from the NSFR on an individual institution basis where the institution is part of a group/sub group;

(ii) the adjustment upwards of ASF factors for covered bonds with a residual maturity of less than one year;

(iii) the need for identical treatment of mortgages in terms of RSF weighting, regardless of whether they are funded through covered bonds or not; and

(iv) the recognition of the secured nature of the asset in the assignment of RSF factors to swap agreements on covered bonds.

Finally, **from an investor perspective**, the EMF-ECBC welcomes the fact that extremely high liquidity and quality as well as high liquidity and quality covered bonds are assigned RSF factors in line with their categorisation under the European Commission's Delegated Act on the Liquidity Coverage Requirement (here). However, the EMF-ECBC asserts that covered bonds backed by cover pools with high credit quality should not be treated differently in the NSFR because of differences in issue size so as to ensure that covered bonds issued from the same prime cover pools fulfil the same stable funding requirements.

On the 26th of May 2016, the European Commission launched a targeted consultation to gather the views of selected stakeholders (in particular financial institutions that could be impacted by the implementation of the NSFR at EU level, associations representing their interests and supervisory authorities) on specific issues that could be raised by the implementation of the NSFR. The consultation (available here) runs until the 24th of June 2016.

The EMF-ECBC will be closely monitoring the evolution of this file over the coming months as the European Commission prepares for the presentation of a legislative proposal on the NSFR to the European Parliament and Council by the end of the year.

Central & Eastern Europe: The Next Wave of Covered Bonds

By Richard Kemmish, Editorial Consultant, Euromoney Conferences and Founder, Richard Kemmish Consulting

On Tuesday the 10th of May 2016 the **European Covered Bond Council** along with **Euromoney Conferences** and the **European Bank for Reconstruction and Development** (EBRD) held its first ever Central and Eastern European (CEE) Covered Bond Forum in London. Delegates from 20 countries learnt about the role that covered bonds can play in the development of local capital markets and in enhancing financial stability, heard about the recent positive developments in Turkey, Romania and Poland, and debated what needs to be done to develop this funding tool from scratch.

The development of the covered bond markets in the region has been a slow process, a point referred to in the introductory remarks made by Philip Bennett, First Vice President and Chief Operating Officer of the EBRD. As he pointed out, it took the financial crisis, and the strong resilience shown by the product to bring them up the agenda: *"Before 2008 covered bonds were not a "hot" discussion topic.. [but] following the..crisis, the strategic importance of covered bonds as a long-term funding tool has been recognised globally"*.

Bennett went on to acknowledge the potential role of covered bonds in one of the EBRD's three private sector strategic initiatives: the development of local capital markets. The EBRD achieves this objective, as he put it, *"through all available tools in the development institution toolbox – i.e.: (i) policy dialogue; (ii) technical cooperation; and (iii) investments"*. He went on to highlight specific examples of the work that the EBRD had undertaken in particular in Turkey, Poland and Romania – all countries which were discussed in dedicated workshops.

In his opening address, John Baskott of Euromoney Conferences compared the development of the CEE covered bond markets to other waves of market development, such as that in non-traditional markets in Western Europe such as the UK after 2003, in non-European markets such as Canada and Singapore following the financial crisis, and argued that recent developments in the CEE represent the third wave of the product's global development.

COVERED BONDS: A FORCE AWAKENS

The opening panel of the day started with a discussion of why covered bonds had taken so long to develop – as moderator Richard Kemmish pointed out, they still represent less than 1% of GDP in the CEE region compared to nearly 25% in Western Europe. Janos Szuda of FHB Bank pointed out this was partially due to a lower development of the use of bonds to fund banks in general: *"In the CEE region deposits represent 70 to 80% of the funding need, debt securities 3- 4%, in Germany and France it's 30-40% deposits, 20-25% ..securities"*. Raluca Nicolescu of Raiffeisen Bank Romania said that the problem was exacerbated in Romania by *"the low penetration of mortgage loans in the economy"* and by a heavy reliance of many banks on funding from foreign parents. But as Philip Bennett commented in his opening address, the Vienna 2 initiative calls for a reduction in reliance on parental funding and efforts to explore local funding.

Moving on to the optimal model for a new covered bond, Rebecca Holter of Fitch Ratings – whilst at pains to emphasise the strengths of the German Pfandbrief law – said that she *"wouldn't call the German law the benchmark for countries..it's not the perfect law to be copied [where covered bonds have had] less historic importance than in Germany"*. She went on to explain that strong systemic support for the product in Germany can mitigate potential weaknesses such as the lack of certainty regarding 'voluntary' over-collateralisation (meaning, over-collateralisation over and above the legal minimum). Furthermore, given historical precedents in Germany, six months of liquidity coverage within a cover pool is considered sufficient – but that this wouldn't necessarily be the case in countries where it isn't clear how easy it is to liquidate a mortgage pool.

Matthias Melms of NORD/LB pointed out that because in some countries it is not as easy to liquidate a mortgage pool *"you need other elements like conditional pass through structures to pay back the covered bonds in time"*. The topic of conditional pass through structures to mitigate refinancing risk was a recurrent theme throughout the day. Melms did however go on to emphasise that some features should be copied from German covered bond law, using that law's strict transparency requirements as an example.

A further topic that was discussed on this panel was the European Commission's recent focus on covered bonds as part of the Capital Markets Initiative. Will this produce a covered bond directive? Is it possible that this would work given national specificities? In response to a question from the floor, Kemmish emphasised that there is a difference between covered bond rules and guidelines. Strict rules are impractical given local legal specificities, guidelines describing outcomes rather than methodologies are useful guidance.

FOREIGN CURRENCY/LOCAL CURRENCY?

One of the key decisions that issuers in all new covered bond jurisdictions will need to make is whether to start issuing into their local currency market or to start with the attractive spreads and volumes available in the euro denominated market.

The development of the local capital markets is key to this decision. Jim Turnbull of the EBRD said that their first questions were *"how developed the local capital markets were and how they could move them to the next level"*. In many countries of EBRD operation, the capital markets are effectively limited to equities, government securities and money markets so covered bonds represent a good opportunity to *"help the markets to the next level"*.

Turnbull emphasised that this development opportunity also applied to derivatives in the local currency. Petr Vybíral of Allen and Overy Czech Republic explained some of the features that covered bond swaps needed to incorporate as part of this.

Piotr Cyburt of mBank Hipoteczny pointed out that some of their commercial real estate properties are denominated in euros and that some foreign currency funding represented a natural hedge for them.

The panel also discussed the benefits of having a domestic investor base for an issuer's appeal to investors off-shore.

HOW TO STRUCTURE COVERED BONDS?

The third panel of the day focussed on some of the practical considerations about how to structure a covered bond law. Starting with the assets that should be funded, Otmar Stöcker of the Association of German Pfandbrief Banks argued that assets should be eligible if they were long-term, marketable collateral and relatively standardised. As such, for example, loans to small and medium sized enterprises would not be suitable.

In contrast, Fatih Saglik of the Capital Markets Board of Turkey emphasised that the criteria should be more based on the needs of society – which is why Turkish covered bonds allowed loans to the SME sector as eligible collateral. He pointed out that this would add to the 'buy-in' to the asset class.

INVESTOR NEEDS

The exemption of covered bonds from bail-in was emphasised as being crucial by Jozef Prokes of BlackRock. He said that this rule on its own fundamentally changes the way that he thinks about the product, in particular moving it away from being a 'credit' product – a view that Marcin Pyszak of ING DiBa disagreed with. Pyszak said that he viewed the exemption from bail-in as being 'the icing on the cake' but that covered bonds were still fundamentally a credit product. Andreea Moraru of the EBRD pointed out that in some countries with imperfect laws the exemption from bail-in was the only benefit currently from the covered bond structure.

Another topic of discussion was whether covered bonds issued from a country could ever survive the failure of the government. Although it would be difficult, Jozef Prokes pointed to the example of Greece but emphasised that this was more likely in the Eurozone and that he could not assume that the same would happen in emerging markets.

Moraru of the EBRD emphasised that negative actions such as the redenomination of Swiss franc mortgages or the new Romanian 'walk away law', although negative for banking credit in general, could be mitigated by covered bond structures and that this was an important part of their value to investors.

Another topic covered by the panel was conditional pass throughs. Pyszak of ING DiBa said that rating agencies *"played the biggest trick on investors with pass throughs..they give a credit opinion that is positive [on a feature] that has negative impacts on investors"*. Agnieszka Tułodziecka from the Polish Mortgage Credit Foundation disagreed saying that this feature was introduced into Polish legislation in the interests of investors and addressed, for example, risks such as time subordination.

THE NEWEST EURO COVERED BOND MARKET: TURKEY

Turkey is famous in covered bond circles for being the first jurisdiction in the world to allow loans to small to medium sized enterprises as collateral for covered bonds. Zeki Önder of Şekerbank described the rational for this development and the process leading up to the world's first SME covered bond in 2011.

In contrast, the first publicly placed covered bond was backed by residential mortgages and was recently issued by VakifBank. Mustafa Turan described the work that needed to be done, from IT development to 'tweaks' of the law in co-operation with the Capital Markets Board to bring this successful deal to market.

The success of the transaction was underpinned by its appeal to many types of investor. As Turan pointed out, the target was 'traditional covered bond investors' – rather than those who already knew VakifBank – and that orders were received from over 300 investors, including most 'well known' covered bond investors. This investor demand allowed the bond to price at just five basis points over the Turkish sovereign curve, a fact which did not surprise Turan who had provided guidance that the first deal will price in this region but that future transactions would start to price at spreads tighter than the Turkish government in euros.

Turan emphasised that 'within 12 months' we will see other banks as regular issuers from Turkey.

POLAND: A PACKAGE OF REFORMS

The Polish workshop discussed the new covered bond law which came into effect on the 1st of January this year. Karol Prazmo of mBank described the new law as *"a game changer"*. He went on to list the positive developments in the law – *"we have abolished withholding tax on interest payments to foreigners..[introduced] a mandatory overcollateralisation of 10%...a CPT [conditional pass through] structure [and] a mandatory liquidity buffer"*.

The conditional pass through structure was also touched on by Jakub Niesłuchowski of PKO Bank Hipoteczny who acknowledged that *"there are of course different points of view"* about the structure and that some investors would appreciate the higher potential recovery rate in an insolvency scenario offered by this feature whilst others would prefer an early exit.

One feature of the Polish covered bond law that was not changed was its continued reliance on the 'special bank' model for covered bond issuers. Discussing this Piotr Kowalski of Fitch Polska said that this choice of model meant *"we won't see a rush of banks setting up mortgage banks"*. The reticence is caused largely by the uncertainty that universal banks face with regard to the capital treatment of mortgages transferred to a mortgage bank subsidiary and the implications of the adoption of MREL into Polish law which could significantly affect the efficiency of the structure.

An important point for foreign investors in Polish euro denominated covered bonds will be that they should be eligible for repo at the European Central Bank. Piotr Borowski of the Warsaw Stock Exchange highlighted the work that was being undertaken to allow this, including the establishment of a bridge to an international central securities depository and the clarification of tax administration. He was confident that this could be achieved by the end of this year.

Already PKO Bank Hipoteczny has issued a transaction under the new law in Polish Zloty and the first euro denominated transaction should be expected shortly.

ROMANIA: GOT THE LAW, READY TO GO?

The newest entrant to the covered bond market is Romania with the laws and accompanying secondary regulations only having been published in the last few months. The process of drafting the regulations was described by Mirela Dima and Alexie Alupoaiei of the National Bank of Romania.

One of the concerns about the new law raised by James Stewart of Raiffeisen Bank Romania and Sergiu Oprescu of the Romanian Banking Association was the economics of issuance. In particular the limit on issuance, which can range from 4% to 8% of a bank's balance sheet – depending on various factors on a bank-by-bank basis – will limit issuance and as a consequence the notional over which onerous upfront costs – including IT and payments to an asset pool monitor – can be amortised.

A further development in Romania that was discussed at length was the introduction of a new law whereby mortgage borrowers can discharge their mortgage obligations by handing back the mortgaged property with no further personal liability for the debts (datio in solutum). Whilst this does not apply to all mortgages, it may be challenged as being unconstitutional and all of the banks in Romania have taken mitigating measures. The panel agreed that it represented a significant negative for the banking sector in general, for the development of the Romanian mortgage market and for the signal that it sends to international investors. Having said all of that it is clear that strong features within the new covered bond law will do a lot to insulate covered bond investors from this new development.

CLOSING THE CONFERENCE

Negative developments, such as the introduction of a 'walk away law' in Romania are an inevitable fact of life. But it is clear from the developments in many countries, not just Poland, Turkey and Romania that covered bond technology is being developed in the CEE region to protect investors from just this sort of credit shock.

As Philip Bennett emphasised in his opening remarks, the credit crisis was a catalyst for the development of covered bonds in the CEE region. By providing strong investor protection and the adoption of state of the art covered bond technology, covered bonds can fulfil their wider role of improving systemic stability, enhancing the local capital markets and improving access to housing finance.

We look forward to next year's second instalment of this conference and the further developments towards these goals.

NEWS IN BRIEF

ESMA Update on Reporting of SFI Information under the CRA Regulation

On the 27th of April 2016, the European Securities and Markets Authority (ESMA) published an update on the reporting of Structured Finance Instruments (SFI) information under the Credit Rating Agencies (CRA) Regulation (available here).

As background information, the CRA Regulation requires issuers, originators and sponsor entities to report information in respect of SFI to ESMA. ESMA is responsible under Article 8(b) of the CRA Regulation for setting-up a website where information on SFIs should be published (the SFI-website). The European Commission's Delegated Regulation (EU 2015/3 of 30 September 2014) requires that, in order to implement Article 8(b), *"The reporting entities shall submit data files in accordance with the reporting system of the SFIs website and the technical instructions to be provided by ESMA on its website"*. The ESMA is required to issue these technical instructions by the 1st of July 2016, given the reporting obligations will apply from the 1st of January 2017.

The ESMA has encountered several issues in preparing the set-up of the SFI website, including the absence of a legal basis for the funding of the website. Consequently, it is unlikely that the SFI website will be available to reporting entities by the 1st of January 2017. Similarly, it is unlikely that ESMA will be in a position to publish the technical instructions by the 1st of July 2016.

Given these issues, the ESMA does not expect to be in a position to receive the information related to SFI from reporting entities from the 1st of January 2017.

The ESMA expects that new securitisation legislation, which is currently in the legislative process, will provide clarity on the future obligation regarding reporting on SFIs.

EBA Discussion Paper on Innovative Uses of Consumer Data by Financial Institutions

On the 4th of May 2016, the European Banking Authority (EBA) published a Discussion Paper on innovative uses of consumer data by financial institutions, in line with its mandate to monitor financial innovation (more information is available here).

In its Discussion Paper (available here), the EBA has identified a preliminary list of risks and potential benefits that the innovative uses of consumer data may bring for consumers, financial institutions and financial stability more widely. Institutions may obtain continuous insight into purchasing habits and preferences, as consumers engage in payment transactions through their accounts or cards. The work of the EBA focuses on the use of consumer data in the banking sector, including mortgages, personal loans, payments accounts, payment services and electronic money.

Although general provisions apply to financial institutions on secrecy and conduct and on data protection that impose restrictions to the use of consumer data, only few requirements presently exist in EU legislation specific to the financial sector that address the use of consumer data by financial institutions. The EBA hopes that the responses to this Discussion Paper will allow it to make a better informed decision on which, if any, regulatory and/or supervisory actions are needed to ensure that the regulatory framework mitigates the risks while also allowing market participants to harness the benefits from the innovation.

The deadline for comments to be submitted to the EBA on this matter is the 4th of August 2016.

EMF and EAA Map Features and Application of AVMs

On the 9th of May 2016, the European Mortgage Federation (EMF) announced the publication of a joint paper together with the European AVM Alliance (EAA) examining the features and key applications of Automated Valuation Models (AVMs) and of the state of the Industry across Europe.

AVMs are statistical valuation solutions providing an estimate of value of any specified property at a specified date, using sophisticated modelling techniques in an automated manner and typically including a comparables-based approach similar to surveyor valuations. As AVMs have been established in more and more jurisdictions in recent years and have been the subject of increasing attention, the EMF and the EAA have for the first time joined forces to map the use and functions of these and other statistical valuation techniques in the different Member States.

The findings of this joint EMF and EAA paper indicate that AVMs are:

- **i.** primarily used across many jurisdictions for the purpose of portfolio valuations alongside other valuation techniques; and that
- **ii.** AVMs are also used to determine property values for a variety of other purposes depending on the jurisdiction, such as mortgage origination, re-mortgaging and quality control.

In addition, the paper discusses the shift in the use of AVMs since 2008 as well as the existing rules, guidance and standards on AVM use in the different countries. In commenting on the joint paper, **Luca Bertalot**, EMF-ECBC Secretary General, stated, *"In light of the increasing establishment of AVMs in Europe in recent years, it is vital, as an industry, to have a thorough understanding of their application across jurisdictions. The accurate and reliable valuation of property is one of the fundamental cornerstones of the mortgage lending and covered bond businesses."*

The joint EMF and EAA paper on Automated Valuation Models & Portfolio Valuations is available here.

ESMA Amends MiFID II Standards on Non-Equity Transparency and Position Limits

On the 2nd of May 2016, the European Securities and Markets Authority (ESMA) issued two Opinions (see below) proposing amendments to its draft Regulatory Technical Standards (RTSs) under the Markets in Financial Instruments Directive (MiFID II) and Regulation (MiFIR). The ESMA proposes to revise the RTS on non-equity transparency – which includes requirements in respect of bonds, covered bonds, other structured finance products, emission allowances and derivatives – and the RTS on the methodology for the calculation and application of position limits for commodity derivatives. The Opinions were produced in response to proposed amendments by the European Commission to these draft RTSs.

OPINION 1: PHASE-IN REGIME FOR NON-EQUITY TRANSPARENCY (available here with its annex)
MiFID II will extend transparency requirements to non-equity products, the implementation of which is detailed in the ESMA's draft RTS. While overall supportive of the approach taken in the draft RTS, on the 20th of April 2016 the Commission requested the ESMA to phase-in the application of certain parts of this new transparency regime to mitigate possible liquidity risks to bond markets. Under the phased-in approach, initially less demanding transparency requirements would be applied. These would be gradually strengthened over a period of four years until they reach the level of transparency initially proposed by ESMA. Consequently, significantly fewer instruments than initially proposed would be subject to the real-time transparency regime at the start of MiFID II.

Under the Commission's proposal, the RTS would only specify the criteria applicable for the first stage of the phase-in and ESMA would conduct a yearly liquidity assessment. In the case of a favourable liquidity assessment, the transparency regime of the RTS would be strengthened by applying the regular legislative procedure for changing an RTS. Overall, the ESMA supports the more cautious transparency regime as suggested by the Commission. However, the ESMA proposes a different phase-in procedure. The Commission procedure for a regular RTS change risks to result in no meaningful improvement of transparency for many non-equity instruments, which would run contrary to the objective stated in MiFIR to strengthen transparency and improve the functioning of the internal market. In addition, it creates legal uncertainty and is burdensome for all parties involved. Therefore, the ESMA is proposing an automatic phase-in, with all the stages already prescribed in the RTS. This automated phase-in would be accompanied by an annual liquidity assessment by the ESMA and the RTS would be amended in case of significantly negative impacts on liquidity.

MAIN ADJUSTMENTS FOR COVERED BONDS
With respect to covered bonds the ESMA proposes some targeted adjustments to ensure the smooth applicability of the phased approach without undue side effects. This concerns in particular the temporary increase of the issuance size of corporate bonds and covered bonds for the first liquidity assessment of newly issued corporate bonds and covered bonds and the introduction of threshold floors for the pre-trade SSTI for bonds to ensure a meaningful level of transparency.

In particular, the coverage ratio of corporate bonds and covered bonds under instrument by instrument approach (IBIA) would be significantly smaller at the initial stages of the phase-in, whereas the first liquidity assessment of newly issued corporate bonds and covered bonds would remain subject to the same issuance size throughout the four stages of the phase-in. Without a change in the issuance size for the first liquidity assessment of newly issued bonds, there is therefore a risk of a significant cliff effect for corporate bonds and covered bonds during the first two stages of the phase-in where a significant amount of newly issued corporate bonds would be initially declared liquid based on their issuance size, but would change their liquidity status at the first quarterly IBIA assessment.

To avoid such an outcome the ESMA considers it appropriate to temporarily raise the issuance size for newly issued corporate bonds and covered bonds for the initial liquidity determination. Therefore, and although this has not been suggested by the Commission in its letters, the ESMA recommends increasing the issuance thresholds used to determine whether newly issued corporate bonds and covered bonds have a liquid market during the first two stages of the phased-in approach from EUR 500 million to EUR 1 billion, that is until the first quarterly determination of the liquidity status of bonds based on transactions executed in the first quarter 2020. Hence, the first determination of the liquidity status of corporate bonds and covered bonds issued until the 31st of December 2019 should be based on an issuance size of EUR 1 billion. For corporate bonds and covered bonds issued thereafter the applicable issuance size for the determination of the initial liquidity status would be EUR 500 million.

OPINION 2: RTS ON POSITION LIMITS FOR COMMODITY DERIVATIVES (available here with its annex)
MiFID II will introduce position limits, or caps on the number of commodity contracts that can be held, to commodity derivatives which will need to be set by national regulators. In order to ensure a harmonised approach to applying such limits, the ESMA's draft RTS provides a methodology for calculating those limits on commodity derivatives traded on trading venues and economically equivalent OTC contracts. While overall supportive of the approach taken in the RTS, the European Commission asked ESMA to consider a number of amendments for:

- commodity derivatives with an agricultural underlying;
- the methodology in cases where deliverable supply and open interest of a contract differ significantly; and
- defining which contracts which are traded OTC only could be considered as economically equivalent to contracts traded on-venue.

The ESMA is supportive of most of the changes proposed by the Commission and understands the concerns about speculation and possible impacts on food prices. Therefore, the ESMA proposes to lower the position limits for derivatives with foodstuffs as an underlying to 2.5%. In addition, the ESMA suggests that in circumstances where deliverable supply and open interest diverge significantly, the other months' position limits should be adjusted accordingly. Finally, the definition of contracts traded "OTC only" has been slightly widened in order to prevent circumventions of the position limits regime by trading OTC.

BACKGROUND
As a matter of background, in September 2015, the ESMA submitted 28 draft RTSs under MiFID II/ MiFIR for endorsement to the Commission. On the 20th of April 2016, the Commission has asked the ESMA to amend three RTSs, notably on non-equity transparency, position limits and ancillary activities. On the 2nd of May 2016 the ESMA sent its two Opinions on non-equity transparency and position limits to the Commission which has to decide whether or not endorse the proposed changes. An Opinion on the third RTS on ancillary activities is currently being finalised by the ESMA and is expected shortly.

European Parliament Publishes Working Document on Common Rules on Securitisation and Creating a European Framework for STS Securitisation

On the 19th of May 2016, the Committee on Economic and Monetary Affairs (ECON) of the European Parliament published a Working document on Common rules on securitisation and creating a European framework for simple, transparent and standardised securitisation (STS Securitisation), which is available here.

The Working Document offers a good vantage point for the positions of the Rapporteur, Mr Paul Tang, a Dutch MEP of the Socialists & Democrats Group, with respect to the STS Securitisation proposal of the European Commission. Among the many views that the Rapporteur presents in the Working Document, a summary is presented below:

Bringing rules together in a single framework

- The legislators should ensure that rules are as consistent and thorough as possible, and do not unduly conflict with the overarching objective of market efficiency and broadening.

MORE DUE DILIGENCES AND TRANSPARENCY TO TACKLE THE ASYMMETRY OF INFORMATION

- The Rapporteur welcomes the restriction whereby only professional investors can invest in securitisations, because the due diligence that is expected cannot be performed by retail investors. Yet, he notes that although most fundamental concerns identified during the crisis had to do with issuers' behaviours, the proposal does not impose any restriction on the nature of the issuer, originator or of the securitisation vehicle, while most of the problems of moral hazard due to the asymmetry of information materialised on their side before the crisis.
- High expectations on due diligences also supposes that it is realistic for investors to build up a comprehensive analysis of securitisation products. Consequently due diligence requirements applicable to investors must go hand-in-hand with the disclosure requirements applicable to originators. This should also take into account the specificities of the type of securitisation and be tailored to the asset class.
- Nevertheless, and despite comprehensive due diligences, buyers may not be able to overcome the original asymmetry of information if the product is extremely complex. That is why confidence by investors requires simplicity, transparency and standardisation of products, which is the aim of the current proposal.

RISK RETENTION AND THE SKIN IN THE GAME PRINCIPLE TO OVERCOME MORAL HAZARD

- Extending and harmonising risk retention requirements across issuers makes sense. Most details of the Commission proposal rely on the technical advice presented by the European Banking Authority (EBA) in December 2014. The proposal maintains the level of retention of 5% of the securitised assets. Furthermore, it does not introduce a different level of retention for STS compared to non-STS products.
- The Rapporteur notes that alternative mechanisms to align interests have been dismissed by the EBA and by the Commission, on the grounds that the other mechanisms would be too complex and difficult to establish and enforce. The Rapporteur is open to strengthening the risk retention rules if necessary and in this light has taken good note of the recent EBA report which stresses that, though only a few credit institutions have been found non-compliant with the current risk retention rules, supervision practices could be improved and harmonised.

CERTIFICATION OF THE STS LABEL

- Without a proper certification system, the STS framework will not manage to restore confidence on the market. In the Commission proposal, the STS label would be self-awarded by the market participants and then, upon information by the issuer and automatically without any check, published on the ESMA website. To balance this option, the Commission introduced the strong disclosure requirements applicable to the issuer and a strict sanction regime on the issuer side (see below).

SELF-ATTESTATION HAS BEEN IDENTIFIED AS A POINT OF DISCUSSION.

- In its General Approach, the Council strengthened the self-attestation with an optional third-party certification and an obligation for the originator (or sponsor or SSPE) to explain how STS criteria are met. It also laid down the whole authorisation process, rights and duties of the third-party.

The Rapporteur supports the reasoning of the Commission, also followed by the ESMA, that the responsibility for adhering to the STS criteria should lay with the issuers and investors of STS securitisations. Self-certification of the STS label properly reflects this conception. Parties are allowed to hire a third-party to help certify their securitisations, but this will not alter their ultimate responsibility to do due diligence and liability for not following the rules of the STS framework.

COMPETENT AUTHORITIES

- The Commission proposal empowers a long list of competent authorities. This approach generates risks of regulatory fragmentation and arbitrage. The Rapporteur is of the view that this Regulation aims at restoring dynamics of confidence in a market in securities and that therefore the European Securities and Markets Authority (ESMA) should be the lead authority and have the power together with national market authorities to look into shortcomings of the securitisation market. In that sense, the Rapporteur would support the European Central Bank's view that STS compliance should be a matter for the securities markets' authorities only. By doing this the number of different National Competent Authorities will be reduced and the interpretation of the STS rules placed exclusively in the hands of the market authorities.

TRANSPARENCY AND RATING ISSUES

- The Commission proposal does introduce originator-to-investor transparency requirements and ensures a high granularity of transparency on the underlying loans under the STS transparency criteria, but those data at the level of the issuer and transaction do not give transparency to the whole market and to the supervisor. Yet, data availability is widely recognised as one of the major market issue. In particular, due to the particularities of the SME securitisation business (see below), making SME loan-level data available to investors would be useful (see ECB-BoE, 2014), even more than information on term securitisation and on ABCPs.

PUBLIC REGISTER FOR STS SECURITISATIONS

- Data comparison and analysis projects, based on continuous reporting on the relevant data of the underlying assets, are not within scope of the current proposal. The Rapporteur believes that transparency on the securitisations and their underlying assets should be improved, for the benefits of supervisors, potential market participants and other stakeholders like academics, through a public register. A data repository would capture and aggregate information for markets to extract and analyse. Based on the period loan-level reporting by the borrowers, the securitisation issuer can send the data to a trade repository to satisfy its supervisory obligation and its transparency obligation. The data collected would also allow market participants to calculate key risk factors on the underlying loans which will help them with their performance and loss probability measurement. Investors, especially those which have not built their own internal historical data, would benefit from further historical loan level data being available via a central repository.

- Given the confidentiality laws of Member States concerning the loan level data involved and the public objective pursued this initiative, the public register for STS securitisations could be designed as a non-for-profit utility to bridge the gap between originator, investor and supervisor. Indeed, such an infrastructure cannot be supported only by market participants or by individual countries.
- The European Datawarehouse of the ECB fulfils partly this task regarding loan-level data but it is questionable whether it could be expanded beyond.

PUBLICLY SUPPORTED SME SECURITISATION

- Relying on the conclusions drawn by the EBA report, the work on synthetic securitisation should be pursued to differentiate between balance sheet securitisation and arbitrage securitisation, to see how best to facilitate risk transfer and to boost balance sheet securitisation in favour of SMEs. SME securitisation represents less than 10% of the securitisation issuances in Europe. Only a few countries, namely Italy, Belgium and Spain, account for the majority of the market. The main lenders for EU SMEs are still big banks and therefore positive direct effects, via actual SME securitisation, and indirect effects, via increased SME loans thanks to capital relief obtained by securitising other loan portfolios, can result from the securitisation proposals.
- The Rpporteur believes that SME securitisations should be encouraged through solutions that enhance transparency and develop an appropriate framework within the STS proposals. For this reason, the example of the EIB/EIF which conditions its guarantee on securitisation on banks re-using the freed up capital to finance the real economy, like giving out more SME loans, should be looked upon favourably. So far SME loans have been a very small part of the securitisation market. Even if the STS initiative helps the securitisation market to revive the impact on financing SME's are expected to be modest.

BALANCE SHEET SYNTHETICS

- Without a proper certification system, the STS framework will not manage to restore confidence on the market. In the Commission proposal, the STS label would be self-awarded by the market participants and then, upon information by the issuer and automatically without any check, published on the ESMA website. To balance this option, the Commission introduced the strong disclosure requirements applicable to the issuer and a strict sanction regime on the issuer side (see below).

ADDITIONAL BACKGROUND

On the 2nd of December 2015, the Council agreed its negotiating position, after only nine weeks of talks, on the proposal from the Commission. The final negotiations between Council and EP, will start once the latter has adopted its report. It appears though that the ECON Committee members have indicated their preference to have the securitisation and the European Deposit Insurance Scheme (EDIS) proposals running in parallel. However, the EDIS is highly a controversial file and therefore it is possible that the securitisation file might be significantly bogged-down.

EMF-ECBC Event on the Future Development of EU Mortgage and Covered Bond Markets, and Implications of the Energy Efficiency Debate

On the 3rd of June 2016, in the context of it summer Board meetings, the EMF-ECBC will host a high-level panel discussion focusing on the subject of "The Future Development of EU Mortgage and Covered Bond Markets, and Implications of the Energy Efficiency Debate". This event is intended to advance discussions around the concept of a potential "Green Mortgage" product, which is currently being considered by the members of the EMF-ECBC.

The event will take place in the *Aula Mario Baratto of the Ca' Foscari* University, Venice and the choice of this venue is highly pertinent to the subject of the debate in that the *Ca' Foscari* building is the oldest in the world certified LEED EB:O&M, the USA protocol dedicated to buildings for the certification of their sustainability. Equally, in the context of the debate on energy efficiency, Venice will of course be one of the first victims of a failure to address the issue in a timely fashion.

The panellists include senior representatives of the **European Commission**, of the **Basel Committee on Banking Supervision**, of the **World Green Buildings Council** and of the European mortgage and covered bond industry. The audience will consist primarily of the members of the EMF-ECBC Boards (the EMF Executive Committee and the ECBC Steering Committee) as well as a number of other specially invited senior representatives of the European banking industry.

Keep an eye out for further updates on the EMF-ECBC initiative on Green Mortgages in future editions of *Market Insights & Updates*.

EBA Consults on LCR Disclosure

On the 11th of May 2016, the European Banking Authority (EBA) launched a consultation on its draft Guidelines on the Liquidity Coverage Ratio (LCR) disclosure. These Guidelines harmonise and specify both the qualitative and quantitative information that institutions are required to disclose on liquidity and namely on the LCR.

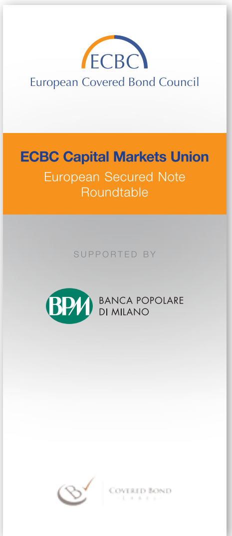
LCR disclosure is crucial for the assessment of liquidity risk management and for the decision-making process of market participants. To this end, the draft Guidelines that the EBA is developing under its own initiative provide uniform tools for the liquidity disclosure framework. In particular, they include: (i) a qualitative and quantitative harmonised table for the disclosure of general information on liquidity risk management – already laid down in the Capital Requirements Regulation (CRR); as well as (ii) qualitative and quantitative templates and relative instructions for the disclosure of information on the LCR composition. In addition, they specify the key figures and metrics in the context of liquidity risk.

The application of these Guidelines is expected to take place not earlier than the 30th of June 2017.

All contributions received will be published following the close of the consultation on the 11th of August 2016, unless requested otherwise. A Public Hearing will take place at the EBA premises in London on the 13th of June 2016.

The full EBA Consultation Paper can be accessed here.

ECBC 2nd Roundtable on ESNs



On the 11th of May 2016, the ECBC hosted its second European Secured Note (ESN) Roundtable, in Milan.

On the back of the introduction of legislative framework for an Italian ESN, pushed through parliament by the Italian government in April 2016, the ECBC organised this Roundtable in Milan to follow-up and build on the recent developments. The event was kindly hosted by **Banca Popolare di Milano** at its Milanese headquarters. During the Roundtable, a broad range of stakeholders and authorities, both national and European, debated on the nature of the ESN, the state of play in the interested counties, funding needs of SMEs and infrastructures, and the possible eligibility criteria for the cover assets.

The need for a European approach to the ESN emerged during the meeting. A European ESN can be achieved by setting common eligibility criteria across the EU. Thus, the ECBC will continue its pre-sounding operations, investigating which players could define these European criteria.

MIFID II-MIFIR: Council Confirms Agreement on One-Year Delay

On the 18th of May 2016, the Permanent Representatives Committee (Coreper – the Committee of the Member States' "Ambassadors" to the European Union) approved, on behalf of the Council, an agreement with the European Parliament on a one-year delay to new securities market rules, MIFID II and MIFIR.

EXTENDED DEADLINE

The one-year postponement of the transposition and application dates will affect the provision of services for investments in financial instruments and the operation of regulated financial markets. Provisional agreement was reached with the European Parliament on the 2nd of May 2016, and a regulation will now be adopted to enact the extension. Under the approach agreed with the European Parliament:

- the deadline for the Member States to transpose MIFID II into national legislation will be set for the 3rd of July 2017;
- the date of application of both MIFID II and MIFIR will be set for the 3rd of January 2018.

OTHER PROVISIONS

Additionally, amendments were agreed as concerns trading on own accounts, package transactions, alignment with the EU directive on securities financing transactions and the date of application of certain provisions of a regulation on market abuse. The amendments to regulation 600/2014 ("MIFIR") are available here and the amendments to directive 2014/65/EU ("MIFID II") are available here.

BACKGROUND INFORMATION

A recent revision of rules on financial instruments set out to promote the integration, competitiveness, and efficiency of EU financial markets. The Council adopted these in May 2014, amending and replacing an existing "MIFID" text that regulates markets in financial instruments.

The rules consist of two legislative instruments:

- MIFIR (regulation 600/2014), aimed at improving transparency and competition of trading activities by limiting the use of waivers on disclosure requirements and by providing for non-discriminatory access to trading venues and central counterparties (CCPs) for all financial instruments, and requiring derivatives to be traded on organised venues.
- MIFID II (directive 2014/65/EU), amending rules on the authorisation and organisational requirements for providers of investment services and on investor protection. The directive also introduces a new type of trading venue, the organised trading facility (OTF). Standardised derivatives contracts are increasingly traded on these platforms, which are currently not regulated.

The new framework requires trading venues and systematic internalisers to provide competent authorities with financial instrument reference data that describes in a uniform manner the characteristics of every financial instrument subject to the scope of MiFID II. In order to collect data in an efficient and harmonised manner, a new data collection infrastructure must be developed. This obliges the European Securities and Markets Authority (ESMA), in conjunction with competent national authorities, to establish a data system covering a wider range of financial instruments, given the extended scope of MiFID II. On the 2nd of October 2015, the ESMA informed the Commission that a delay in the technical implementation of MiFID II was unavoidable. Neither competent authorities nor market participants will be in a position to apply the new rules on the 3rd of January 2017. This would lead to legal uncertainty and potential market disruption.

The regulation extending the deadlines for transposition of MIFID II and application of MIFID II and MIFIR is expected to be approved by the European Parliament at first reading. It will then be submitted to the Council for adoption.

European Commission Delegated Regulation on Criteria for Banks to Hold Easily 'Bail-Inable' Instruments in Case of Resolution

On the 23rd of May 2016, the European Commission adopted a Delegated Regulation specifying the criteria for banks to hold easily 'bail-inable' instruments in case of resolution (here). This Delegated Regulation specifies the criteria that authorities responsible for resolving banks will need to consider when setting the minimum requirements for own funds and eligible liabilities (MREL) – or easily 'bail-inable' instruments – for the purpose of loss absorption and recapitalisation of banks. The Delegated Regulation will further clarify a key provision of the Bank Recovery and Resolution Directive (BRRD) and support the overall objective of having a robust MREL.

The BRRD does not foresee a harmonised minimum level of bail-in able instruments at the level of individual banks. The regulatory standard needs to respect this choice of the co-legislator. Instead, it gives resolution authorities detailed guidance for setting out these requirements for individual banks, while also allowing them discretion on the minimum level on MREL and, to a lesser degree, on the composition of MREL that is appropriate for each bank. The bank-specific nature of MREL recognises the diversity of business models and funding strategies among European banks, all of which fall under the broad scope of the BRRD.

The Delegated Regulation is based on the draft regulatory technical standard of the European Banking Authority (EBA), which are available here, which the Commission amended to ensure compliance with the BRRD.

BACKGROUND INFORMATION

The BRRD (here) requires that relevant resolution authorities draft resolution plans for banks, outlining options for applying resolution tools and powers. In accordance with the foreseen resolution approaches, the resolution plans should also include a minimum requirement for own funds and eligible liabilities (MREL), and a deadline by which to achieve it.

As specified in the BRRD, resolution authorities, namely the Single Resolution Board and National Resolution Authorities, consider a list of criteria when determining MREL, such as bank's size, funding model, risk profile and the need to ensure that the bank is recapitalised appropriately post-resolution. To ensure that MREL requirements are determined in a manner that is consistent across banks, the BRRD mandated the EBA to clarify, via a regulatory technical standard, how these criteria should be applied by resolution authorities.

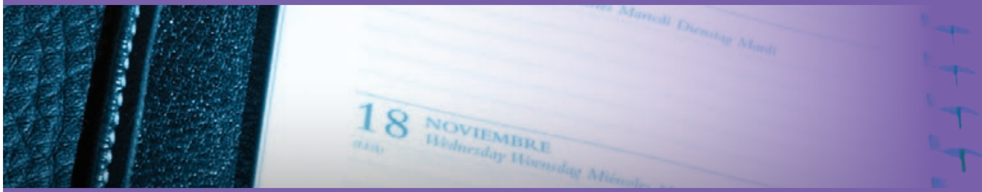
NEXT STEPS

- The draft regulation has now been passed on to the Council and the European Parliament for their consideration. They are entitled to an objection period of three months.
- Article 45 of the BRRD mandates the Commission to carry out an MREL review by the end of 2016. Importantly, this work will take into consideration the international TLAC standard for global systemically important banks, recently adopted by the G-20.
- The Commission intends to make a proposal to introduce this standard into EU law in 2016, well in time before its entry into force in 2019.

EP Publishes Draft Report on the Green Paper on Retail Financial Services

On the 25th of May 2016, the European Parliament's Committee on Economic and Monetary Affairs (ECON) published its draft Report on the European Commission's Green Paper on Retail Financial Services.

The draft Report of the ECON Committee can be accessed here.



AGENDA

JUNE 2016

01/06	European Banking Authority (EBA) Public Hearing on Draft RTS on Disclosure of Asset Encumbrance – London
01/06	Norddeutsche Landesbank Annual Capital Markets Conference – Hannover
02/06	European Covered Bond Council (ECBC) Steering Committee Meeting – Venice
03/06	European Mortgage Federation (EMF) Executive Committee Meeting – Venice
03/06	EMF-ECBC Event on the Future Development of EU Mortgage and Covered Bond Markets, and Implications of the Energy Efficiency Debate – Venice
06/06	European Banking Industry Committee (EBIC) Plenary Meeting – Brussels
08/06	European Mortgage Federation – European Covered Bond Council (EMF-ECBC) Annual Meeting with the European Central Bank (ECB) – Frankfurt
09/06	International Capital Market Association (ICMA) & The Covered Bond Report Covered Bond Investor Conference 2016 – Frankfurt
09/06	European Commission's Brussels Economic Forum – Brussels
13/06	European Banking Authority (EBA) Public Hearing on the Consultation on Draft Guidelines on the LCR Disclosure – London
14-16/06	IMN & Association for Financial Markets in Europe (AFME) 20th Global ABS Conference – Barcelona
21/06	European Banking Industry Committee (EBIC) Consumer Credit Working Group Meeting – Brussels
21/06	European Parliament Financial Services Forum (EPFSF) Event on Follow-Up to the Action Plan on Capital Markets Union (CMU) – Brussels
21/06	European Builders Confederation (EBC) Event on "A successfully Energy Efficiency approach in Europe" – Brussels
21-22/06	Italian Banking Association Conference on Banking Union & Basel III: Risk & Supervision 2016 – Rome
28/06	Conference of the Long-Term Investment and Reindustrialisation Intergroup "The Juncker Plan, and so what?" – Brussels

JULY 2016

12/07	European Commission Conference on "Insolvency at crossroads – The way forward at EU level" – Brussels
12/07	European Parliament Financial Services Forum (EPFSF) Event on Financial Education – Brussels