



EUROPEAN COMMISSION

Directorate General Financial Stability, Financial Services and Capital Markets Union

Call for advice to the EBA to assist the Commission's implementation of the standardised approach for counterparty credit risk under the CRR review

Context

The European Commission is currently undertaking a review of the CRR and, as part of this review, is considering the impact of implementing the new standardized approach used for the calculation of the exposures value of derivative contracts ('SA-CCR') adopted by the Basel Committee on Banking Supervision (BCBS) in March 2014¹. This BCBS proposes to replace the existing methods for derivative exposures (the Standardized Method ('SM') and the Current Exposure Method ('CEM') known as Mark-to-Market Method ('MtM method') in the EU) in the counterparty credit risk capital requirements framework. In addition, the BCBS has decided that the SACCR will apply to other areas of the prudential framework for banks (eg the revised capital requirements for banks exposures to central counterparties², the final large exposures framework³) and is currently considering its application in the leverage ratio framework.

The European Commission is additionally mandated to review and report on the application of Article 275 of the CRR (use of the 'Original Exposure Method' or 'OEM') and submit that report to the European Parliament and the Council, and, if appropriate, a legislative proposal. OEM is also a standardized approach used for the calculation of the exposures values of derivative contracts but only institutions that are eligible for the derogation of small trading book business (Article 94 of the CRR) can use it. OEM was introduced as part of the 1988 Basel I Accords as a discretion for jurisdictions that wanted to a simple alternative to CEM. Although OEM was removed from the Basel framework since the 2005 Basel II Accords, the EU retained it in the subsequent versions of the CRD (including in CRDIV/CRR) based on the rationale that OEM was more suitable for institutions with little trading activities.

The main objective of this call for advice is therefore to gather information on the current use of the existing standardized approaches (including the SM, MtM method and OEM) and assess the potential impact of introducing the SA-CCR in the EU as a replacement for them. Particular attention should be paid on the application of SA-CCR to smaller institutions, with a view to consider whether the introduction of the SA-CCR would also be appropriate for these institutions or if an alternative method is warranted for them (eg simplified version of SA-CCR or maintaining the MtM method and/or the OEM).

¹ BCBS, March 2014 (<http://www.bis.org/publ/bcbs279.htm>)

² BCBS, April 2014 (<http://www.bis.org/publ/bcbs282.htm>)

³ BCBS, April 2014 (<http://www.bis.org/publ/bcbs283.htm>)

Before considering changes to the framework further, the European Commission would like to seek technical advice from EBA to assess the impact on EU banks of adopting the SA-CCR with a particular emphasis on a quantitative assessment.

In light of the on-going broader work related to investment firms, the EBA work should focus on credit institutions. However, those investment firms which, in the view of the EBA, are likely to remain subject to the CRR requirements going forward should also be included.

Considering the relatively short timeframe given to the EBA for producing the report, the Commission is not expecting the EBA to publicly consult on its findings. However, to the extent possible, the EBA is nonetheless encouraged to discuss the consequences of the proposals with the EU banking industry.

Finally, the European Commission is aware that limitations in data availability may restrict the EBA in assessing all aspects listed in the Call for Advice, just as a separate Quantitative Impact Study involving only EU banks may not be feasible within the given timeline. Should this be the case, the European Commission will ask the EBA to highlight these limitations in its final report. However, to aid the EBA in its report, Annex 1 provides a preliminary overview of data that could be relevant for the EBA to consider as part of its assessment.

Scope

The EBA is asked to consider the following three elements in its report:

1. Impact of the SA-CCR on EU institutions

This section should assess the impact of introducing the SA-CCR on EU institutions in the counterparty credit risk capital requirements (default risk charge only), the leverage ratio and, if possible, the large exposures framework. The overall capital impact should be measured relative to the existing framework in place in the EU. A broad representative sample of EU institutions should be selected for this assessment.

In light of these results, the report should determine whether the calibration of SA-CCR is appropriate for EU institutions or whether any adjustment is necessary to ensure that the introduction of SA-CRR would not create any undesirable consequences in the EU, such as an excessive increase in transactions costs for OTC derivatives (generally or for specific counterparties) or, in the context of the application of SA-CCR to the Leverage Ratio framework, a disincentive to centrally clear or bilaterally margin these transactions.

The report should also consider the operational burden of implementing SA-CCR and the level playing field across institutions with different business models.

2. Review of the Original Exposure Method

The report should include an estimate of the number of EU institutions that currently use the OEM under CRR, together with some general information about these institutions (eg overall size, business model⁴, size of derivative businesses, etc) and the materiality of OEM in their current capital requirements (ie the default risk charge and, estimated separately, the

⁴ It is noted that previous EBA reports, such as the NSFR report provided a break-down according to business models. Hence the EBA report could, if relevant, use existing classifications of business models.

application of article 385 to proxy CVA risks using a method based on OEM).

In light of these results, the report should determine whether it would be appropriate to keep the OEM in its current form, including the consideration to link it to the derogation of small trading book business and its specific use for CVA risks under article 385, or whether SA-CCR or a simplified version of SA-CCR could replace OEM in the prudential framework with creating undue operational burden for small banks or banks with small trading activities.

Final considerations

The Commission would appreciate it if the EBA could also report on any other issues or inconsistencies that competent authorities in the EU may have already identified in the BCBS new framework. Suggestions on how to rectify the identified issues and inconsistencies or on how to clarify the terminology used would be particularly welcome.

It is noted that the analysis provided should not prejudice the Commission's final decision. Moreover, in accordance with the established practices of the Commission Expert Group on Banking, Payments and Insurance, the Commission will continue, where appropriate, to consult the experts appointed by the Member States in the preparation of its report.

The European Commission is aware that time and resource constraints may restrict the range of analysis methodologies to be used by the EBA in certain aspects of the Call for Advice. Should this be the case, the EBA should highlight these limitations in its final report. In these cases, and in order to perform the analysis needed, the EBA could rely on alternative, simpler methodologies.

The deadlines for this call for advice are the following:

By June 1st 2016:

- A preliminary analysis of point 1 using the existing BCBS Leverage ratio QIS data already used for the EBA report on the Leverage ratio. If impacts on capital requirements for counterparty credit risk cannot be extracted from this data set, the EBA should provide at least an analysis of the impacts at the exposure level (on top of the impacts of SA-CCR in the Leverage ratio)
- A broad comparison between the OEM and the MtM market of a sample of EU institutions, as performed for the EBA report on the Leverage ratio.

By October 1st 2016

- The final report including all the elements of sections 1 to 2.

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