European Parliament

2014-2019

Committee on Economic and Monetary Affairs

15.11.2017

PROVISIONAL AGREEMENT RESULTING FROM INTERINSTITUTIONAL NEGOTIATIONS

Subject: Proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) No 575/2013 as regards transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds and the large exposures treatment of certain public sector exposures denominated in non-domestic currencies of Member States
(COM(2016)0850 – C8-0158/2017 – 2016/0360B(COD))

The interinstitutional negotiations on the aforementioned proposal for a regulation have led to a compromise. In accordance with Rule 69f(4) of the Rules of Procedure, the provisional agreement, reproduced below, is submitted as a whole to the Committee on Economic and Monetary Affairs for decision by way of a single vote.

REGULATION (EU) …/…
OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

of …

amending Regulation (EU) No 575/2013 as regards *transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds and the large exposures treatment of certain public sector exposures denominated in non-domestic currencies of Member States*

(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,

1 OJ, C , , p. .

2 OJ, C [redacted]

Whereas:

(1) ***On 24 July 2014, the International Accounting Standards Board published International Financial Reporting Standard (IFRS) 9 Financial Instruments. The standard aims to improve the financial reporting of financial instruments by addressing concerns that arose in this area during the financial crisis. In particular, IFRS 9 responds to the G20's call to move to a more forward-looking model for the recognition of expected credit losses on financial assets. In relation to the recognition of expected credit losses on financial assets it replaces International Accounting Standard (IAS) 39.***

(2) ***The European Commission adopted IFRS 9 through Commission Regulation (EC) No 2016/2067[1]. In accordance with that Regulation, each institution that uses IFRS to prepare its financial statements will be required to apply IFRS 9 as of the starting date of the institution's first financial year beginning on or after 1 January 2018.***

1 ***Commission Regulation (EU) 2016/2067 of 22 November 2016 amending Regulation (EC) No 1126/2008 adopting certain international accounting standards in accordance with Regulation (EC) No 1606/2002 of the European Parliament and of the Council as regards International Financial Reporting Standard 9 (OJ L 323, 29.11.2016, p. 1).***

(3) The application of IFRS 9 may lead to a sudden significant increase inexpected credit loss (ECL) provisions and consequently a sudden decrease in institutions' Common Equity Tier 1 (CET1) capital.
While the Basel Committee on Banking Supervision (BCBS) is currently considering the longer-term regulatory treatment of provisions, transitional arrangements allowing institutions to mitigate the potential significant negative impact on CET1 capital arising from ECL accounting should be adopted in Regulation (EU) No 575/2013.

(4) In its resolution of 6 October 2016, the European Parliament called for a progressive phase-in regime that would mitigate the impact of the new impairment model of IFRS 9.

(5) Where an institution's opening balance sheet as of the day when first applying IFRS 9 in 2018 reflects a decrease in CET1 capital as a result of increased ECL provisions, including the loss allowance for lifetime expected losses for financial assets that are credit impaired as defined in Appendix A of the Annex to Commission regulation (EU) No 2016/2067, compared to the closing balance sheet on the previous day, the institution should be allowed to include in its CET1 capital a portion of the increased ECL provisions during a transitional period. This transitional period should have a duration of 5 years and should start on the first day of 2018 on which the institution first applies IFRS 9. The portion of ECL provisions that can be included in CET1 capital during the transitional period should decrease over time down to zero to deliver full implementation on the day immediately after the end of the transitional period. The impact of the ECL provisions on Common Equity Tier 1 capital should not be fully neutralised during the transitional period.

(6) ***Institutions should decide whether to apply these transitional arrangements and inform the competent authority accordingly. In order to mitigate the potential significant negative impact on CET1 capital arising from ECL accounting, during the transitional period, an institution should have the possibility to amend once its initial decision to apply transitional provisions relating to the introduction of IFRS9, subject to the prior permission of the competent authority which should ensure that such decision is not motivated by considerations of regulatory arbitrage.***

(7) ***As provisions incurred after the first day of 2018 on which the institution first applies IFRS 9 could rise unexpectedly due to a worsening macroeconomic outlook, institutions should be granted some additional relief in such cases through the transitional arrangements.***

(8) ***Institutions that benefit from transitional arrangements aimed at smoothing the impact of ECL provisions on CET1 capital should be required to adjust the calculation of regulatory items which are directly affected by ECL provisions to ensure that they do not receive inappropriate capital relief. For example, the specific credit risk adjustments by which the exposure value is reduced under the Standardised Approach for credit risk should be reduced by a factor which has the effect of increasing the exposure value. This would ensure that an institution would not benefit from both an increase in its CET1 capital due to transitional arrangements as well as a reduced exposure value.***

(9) ***Institutions should publicly disclose their own funds, capital ratios, and leverage ratio both with and without the application of the IFRS 9 transitional arrangements specified in this Regulation to enable the public to determine the impact of those arrangements . Where an institution decides not to apply such transitional arrangements, it should not be required to disclose their effect.***

(10) It is also appropriate to provide for transitional arrangements for the exemption from the large exposure limit available to exposures to certain public sector debt of Member States denominated in non-domestic currencies of Member States. The transitional period should have a duration of three years starting from 1 January 2018 for exposures of this type incurred on or after [date of adoption to be added when the text is published], whilst exposures of this type incurred before that date should be grandfathered and continue to benefit from the large exposures exemption.

(11) Since the objectives of this Regulation, namely to reinforce and refine already existing Union legislation ensuring uniform prudential requirements that apply to credit institutions and investment firms throughout the Union, cannot be sufficiently achieved by the Member States but can rather, by reason of their scale and effects, be better achieved at Union level, the Union may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty on European Union. In accordance with the principle of proportionality, as set out in that Article, this Regulation does not go beyond what is necessary in order to achieve those objectives.

(12) Regulation (EU) No 575/2013 should therefore be amended accordingly,

HAVE ADOPTED THIS REGULATION:

Article 1

Regulation (EU) No 575/2013 is amended as follows:

(1) The following new Article 473a is inserted after Article 473:

"*Article 473a*

Introduction of IFRS 9

1. ***By way of derogation from Article 50, until the end of the transition period set out in paragraph 6,*** institutions that prepare their accounts in conformity with the international accounting standards adopted in accordance with the procedure laid down in Article 6(2) of Regulation (EC) No 1606/2002***, institutions that pursuant to Article 24(2) effect the valuation of assets and off-balance sheet items and the determination of own funds in accordance with international accounting standards adopted pursuant to the procedure laid down in Article 6(2) of Regulation (EC) No 1606/2002 and institutions that effect the valuation of assets and off-balance sheet items in conformity with accounting standards in accordance with Directive 86/635/EEC that use an expected credit loss model that is the same as the one used in accounting standards adopted in accordance with the procedure laid down in Article 6(2) of Regulation (EC) No 1606/2002 may include in*** their Common Equity Tier 1 capital the amount calculated ***as the sum of the following:***

(a) ***for exposures subject to risk weighting in accordance with Chapter 2 of Title II of Part Three, the amount (AB_{SA}) calculated in accordance with the following formula:***

$$AB_{SA} = (A_{2,SA} + A_{4,SA} - t)\, f$$

where:

$A_{2,SA}$ ***= the amount calculated in accordance with paragraph 2;***

$A_{4,SA}$ ***= the amount calculated in accordance with paragraph 4 based on the amounts calculated in accordance with paragraph 3;***

f ***= the applicable factor laid down in paragraph 6;***

t***= increase of Common Equity Tier 1 capital that is due to tax deductability of the amounts*** $A_{2,SA}$ ***and*** $A_{4,SA}$***.***

(b) for exposures subject to risk weighting in accordance with Chapter 3 of Title II of Part Three, the amount (AB_{IRB}) calculated in accordance with the following formula:

$$AB_{IRB} = (A_{2,IRB} + A_{4,IRB} - t) \cdot f$$

where:

$A_{2,IRB}$ = the amount calculated in accordance with paragraph 2 adjusted in accordance with point (a) of paragraph 5;

$A_{4,IRB}$ = the amount calculated in accordance with paragraph 4 based on the amounts calculated in accordance with paragraph 3 which are adjusted in accordance with points (b) and (c) of paragraph 5;

f = the applicable factor laid down in paragraph 6;

t= increase of Common Equity Tier 1 capital that is due to tax deductability of the amounts $A_{2,IRB}$ and $A_{4,IRB}$

2. ***Institutions shall calculate separately for their exposures subject to risk weighting in accordance with Chapter 2 of Title II of Part Three and for their exposures subject to risk weighting in accordance with Chapter 3 of Title II of Part Three the amounts $A_{2,SA}$ and $A_{2,IRB}$ referred to, respectively, in points (a) and (b) of paragraph 1 as the greater of the amounts in points (a) and (b) of this paragraph:***

   (a) zero;

   (b) the amount calculated in accordance with point (i) reduced by the amount calculated in accordance with point (ii):

      (i) the sum of the twelve month expected credit losses determined in accordance with paragraph 5.5.5 of Commission Regulation (EU) No 2016/2067 and the amount of the loss allowance for lifetime expected losses determined in accordance with paragraph 5.5.3 of Commission Regulation (EU) No 2016/2067 as at 1 January 2018 or on the date of initial application of IFRS 9;

      (ii) the total amount of impairment losses on financial assets classified as loans and receivables, held to maturity investments and available for sale financial assets other than equity instruments and units or shares in collective investment undertakings, as defined in paragraph 9 of IAS 39, determined in accordance with paragraphs 63, 64, 65, 67, 68 and 70 of IAS 39 of Commission Regulation (EC) No 1126/2008 as at 31 December 2017 or the day before the date of initial application of IFRS 9.

3. Institutions shall calculate separately for their exposures subject to risk weighting in accordance with Chapter 2 of Title II of Part Three and for their exposures subject to risk weighting in accordance with Chapter 3 of Title II of Part Three the amount by which the amount referred to in point (a), exceeds the amount referred to in point (b) of this paragraph:

(a) the sum of the twelve month expected credit losses determined in accordance with paragraph 5.5.5 of Commission Regulation (EU) No 2016/2067 and the amount of the loss allowance for lifetime expected losses determined in accordance with paragraph 5.5.3 of Commission Regulation (EU) No 2016/2067 excluding the loss allowance for lifetime expected losses for financial assets that are credit-impaired as defined by Appendix A of Commission Regulation (EU) No 2016/2067 as of the reporting date;

(b) the sum of the twelve month expected credit losses determined in accordance with paragraph 5.5.5 of Commission Regulation (EU) No 2016/2067 and the amount of the loss allowance for lifetime expected losses determined in accordance with paragraph 5.5.3 of Commission Regulation (EU) No 2016/2067 excluding the loss allowance for lifetime expected losses for financial assets that are credit-impaired as defined by Appendix A of Commission Regulation (EU) No 2016/2067 as at 1 January 2018 or on the date of initial application of IFRS 9.

4. For exposures subject to risk weighting in accordance with Chapter 2 of Title II of Part Three, where the amount specified in accordance with point (a) of paragraph 3 exceeds the amount specified in point (b) of that paragraph, institutions shall set $A_{4,SA}$ equal to any positive amount resulting from that calculation, otherwise they shall set $A_{4,SA}$ equal to zero.

For exposures subject to risk weighting in accordance with Chapter 3 of Title II of Part Three, where the amount specified in accordance with point (a) of paragraph 3, after applying point (b) of paragraph 5, exceeds the amount for these exposures as specified in point (b) of paragraph 3, after applying point (c) of paragraph 5, institutions shall set $A_{4,IRB}$ equal to any positive amount resulting from that calculation, otherwise they shall set $A_{4,IRB}$ equal to zero.

5. For exposures subject to risk weighting in accordance with Chapter 3 of Title II of Part Three, institutions shall apply paragraphs 2 to 4 as follows:

(a) for the calculation of $A_{2,IRB}$ institutions shall reduce each of the amounts calculated in accordance with points (b)(i) and (ii) of paragraph 2 by the sum of expected loss amounts calculated in accordance with Article 158(5), (6) and (10) as at 31 December 2017 or the day before the date of initial application of IFRS 9. Where for the amount referred to in point (b)(i) of paragraph 2 the calculation results in a negative number, the institution shall set the value of the amount referred to in point (b)(i) of paragraph 2 equal to zero. Where for the amount referred to in point (b)(ii) of paragraph 2 the calculation results in a negative number, the institution shall set the value of the amount referred to in point (b)(ii) of paragraph 2 equal to zero;

(b) ***institutions shall replace the amount calculated in accordance with point (a) of paragraph 3 by the sum of the twelve month expected credit losses determined in accordance with paragraph 5.5.5 of Commission Regulation (EU) No 2016/2067 and the amount of the loss allowance for lifetime expected losses determined in accordance with paragraph 5.5.3 of Commission Regulation (EU) No 2016/2067 excluding the loss allowance for lifetime expected losses for financial assets that are credit-impaired as defined by Appendix A of Commission Regulation (EU) No 2016/2067 reduced by the sum of related expected loss amounts for the same exposures calculated in accordance with Article 158(5), (6) and (10) as of the reporting date. Where the calculation results in a negative number, the institution shall set the value of the amount in point (a) of paragraph 3 equal to zero;***

(c) ***institutions shall replace the amount calculated in accordance with point (b) of paragraph 3 by the sum of the twelve month expected credit losses determined in accordance with paragraph 5.5.5 of Commission Regulation (EU) No 2016/2067 and the amount of the loss allowance for lifetime expected losses determined in accordance with paragraph 5.5.3 of Commission Regulation (EU) No 2016/2067 excluding the loss allowance for lifetime expected losses for financial assets that are credit-impaired as defined by Appendix A of Commission Regulation (EU) No 2016/2067 as at 1 January 2018 or on the date of initial application of IFRS 9 reduced by the sum of related expected loss amounts for the same exposures calculated in accordance with Article 158 (5), (6) and (10). Where the calculation results in a negative number, the institution shall set the value of the amount in point (b) of paragraph 3 equal to zero.***

6. Institutions shall apply the following factor to calculate the amounts AB_{SA} and AB_{IRB} referred to in paragraph 1 points (a) and (b) respectively:

(a) 0,95 in the period from 1 January 2018 to 31 December 2018;

(b) 0,85 in the period from 1 January 2019 to 31 December 2019;

(c) 0,7 in the period from 1 January 2020 to 31 December 2020;

(d) 0,5 in the period from 1 January 2021 to 31 December 2021;

(e) 0,25 in the period from 1 January 2022 to 31 December 2022.

Institutions whose financial year commences after 1 January 2018 but before 1 January 2019 shall adjust the dates in points (a) to (e) of the first subparagraph of this paragraph to correspond to their financial year, shall report the adjusted dates to their competent authority and shall disclose them.

Institutions which start to apply accounting standards as referred to in paragraph 1 on or after 1 January 2019 shall apply the relevant factors in accordance with points (b) to (e) starting with the factor corresponding to the year of first application of those accounting standards.

7. Where an institution includes in its Common Equity Tier 1 capital an amount in accordance with paragraph 1, the institution shall recalculate all requirements laid down in this Regulation and of Directive 2013/36/EU that use any of the following items by not taking into account the effects that the expected credit loss provisions that it included in its Common Equity Tier 1 capital have on those items:

(a) the amount of deferred tax assets that is deducted from Common Equity Tier 1 capital in accordance with Article 36(1)(c) or risk weighted in accordance with Article 48(4);

(b) the exposure value as determined in accordance with Article 111(1);

The specific credit risk adjustments by which the exposure value shall be reduced shall be multiplied by the following scaling factor (sf):

$sf = 1 – (AB_{SA} / RA_{SA})$

where:

AB_{SA} ***= the after-tax amount calculated in accordance with point a of paragraph 1;***

RA_{SA} ***= the total amount of specific credit risk adjustments.***

(c) the amount of Tier 2 items calculated in accordance with point (d) of Article 62;

8. ***During the period set out in paragraph 1, in addition to disclosing the information required in Part Eight, institutions which choose to apply this Article shall disclose the amount of own funds, Common Equity Tier 1 capital, Tier 1 capital, the Common Equity Tier 1 capital ratio, the Tier 1 capital ratio, the total capital ratio and leverage ratio they would have in case they would not apply this Article.***

In accordance with Article 16 of Regulation (EU) No 1093/2010, EBA shall issue guidelines by 30 June 2018 on the disclosure requirements laid down in this Article.

9. ***An institution shall decide whether to apply the treatment set out in this Article during the transitional period and shall inform the competent authority of its decision by 1 February 2018. During the transitional period, an institution may, on a one time basis, amend its decision to apply transitional provisions as set out in this Article where it has received the prior permission of the competent authority. Institutions shall disclose the decision taken in accordance with this sub-paragraph.***

An institution that has decided to apply the treatment set out in this Article may decide not to apply paragraph 4 in which case it shall inform the competent authority of its decision by 1 February 2018. In such a case, the institution shall set A_4 in paragraph 1 equal to zero. During the transitional period, an institution may decide once to reverse its initial decision and apply paragraph 4 where it has received the prior permission of the competent authority to do this. Institutions shall disclose the decision taken in accordance with this sub-paragraph.'.

(2) In Article 493 the following paragraphs are added:

'4. By way of derogation from Article ***395(1),*** competent authorities may allow institutions to incur ***any*** of the exposures provided for in ***paragraph 5 meeting the conditions set out in paragraph 6, up to the following limits***:

(a) 100 % of the institution's Tier 1 capital until 31 December 2018;

(b) 75 % of the institution's Tier 1 capital until 31 December 2019;

(c) 50 % of the institution's Tier 1 capital until 31 December 2020.

The limits referred to in points (a), (b) and (c) of the first subparagraph shall apply to exposure values after taking into account the effect of the credit risk mitigation in accordance with Articles 399 to 403.

5. The treatment set out in paragraph 4 shall apply to the following exposures:

(a) asset items constituting claims on central governments, central banks, or public sector entities of Member States;

(b) asset items constituting claims expressly guaranteed by central governments, central banks, or public sector entities of Member States;

(c) other exposures to, or guaranteed by, central governments, central banks, or public sector entities of Member States;

(d) asset items constituting claims on regional governments or local authorities of Member States treated as exposures to the central government in accordance with Article 115(2);

(e) other exposures to, or guaranteed by, regional governments or local authorities of Member States treated as exposures to the central government in accordance with Article 115(2).

For the purposes of points (a), (b) and (c) of the first subparagraph, the treatment set out in paragraph 4 shall apply only to asset items and other exposures to, or guaranteed by, public sector entities which are treated as exposures to a central government, a regional government or a local authority in accordance with Article 116(4). Where asset items and other exposures to, or guaranteed by, public sector entities are treated as exposures to a regional government or a local authority in accordance with Article 116(4), the treatment set out in paragraph 4 shall apply only where exposures to that regional government or local authority are treated as exposures to the central government in accordance with Article 115(2).

6. ***The treatment set out in paragraph 4 shall apply only where an exposure referred to in paragraph 5 meets all of the following conditions:***

(a) the exposure would be assigned a risk weight of 0 % in accordance with Article 495(2) as it stood before 1 January 2018;

(b) the exposure was incurred on or after [date of adoption to be added when the text is published].

7. ***An exposure as referred to in paragraph 5 incurred before... [date of adoption to be added when the text is published] to which a risk weight of 0 % was assigned on 31 December 2017 in accordance with Article 495(2) shall be exempted from the application of Article 395(1).'***

Article 2

Entry into force and date of application

1. This Regulation shall enter into force on the ▌ day following that of its publication in the Official Journal of the European Union.

2. This Regulation shall apply from 1 January 2018.

▌

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at Strasbourg,

▌

[signatures]