COUNCIL OF THE EUROPEAN UNION

Brussels, 18 November 2011

Interinstitutional File:
2011/0202 (COD)
2011/0203 (COD)

17166/11

EF 161
ECOFIN 797
CODEC 2103

"I/A" ITEM NOTE

from: Presidency
to: Permanent Representatives Committee (Part 2) / Council

No. Cion prop.: 13285/11 EF 113 ECOFIN 532 CODEC 1285 - COM(2011) 453 final
13284/11 EF 112 ECOFIN 531 CODEC 1284 - COM(2011) 452 final +ADD1 +ADD2

Subject: Legislative package on capital requirements and prudential supervision:
b) Proposal for a Regulation of the European Parliament and of the Council on prudential requirements for credit institutions and investment firms
   - progress report

I. INTRODUCTION

1. The abovementioned Commission proposals have been transmitted to the Council on 20 July 2011. The objective of this legislative package is, inter alia, to ensure that the effectiveness of institution capital regulation in the EU is strengthened, the financial stability is enhanced and pro-cyclicality of the financial system is contained while maintaining the competitive position of the EU banking industry. These proposals also aim to transpose the agreements reached by the Basel Committee on Banking Supervision (i.e. the Basel III requirements), as endorsed by the G20 leaders.
2. All Member States recognise the importance of quick adoption of this legislative package and are committed to working towards an agreement which would also swiftly transpose the Basel III requirements into legislative acts of the European Union.

3. To date, the Working Party on Financial Services has met seven times (29 September, 7, 21, 27-28 October and 14-15 November 2011) to examine these texts. During this initial phase of deliberations at the Working Party level, the Presidency has collected the views of the Member States, with the aim of advancing the legal and technical review of the legislative proposals and identifying key issues that merit further discussion.

4. Without prejudice to the outcome of negotiations on this legislative package as a whole, in the view of the Presidency, there is a broad measure of agreement on a number of proposed provisions to improve current prudential requirements, in particular the need to improve significantly the qualitative and quantitative capital requirements.

5. In this Progress Report the Presidency aims to inform about some of those principal concerns expressed by Member States, where a solution would be needed to reach a compromise agreement at the Council. This Progress Report is without prejudice to the scope and content of other issues that would require further negotiations in the preparatory bodies of the Council.

II. STATE OF PLAY

National discretion and the single market objective (flexibility and maximum harmonisation)

6. One of the objectives of this legislative package is to achieve and ensure efficient functioning of the internal market in banking and investment sectors across the European Union. The Commission therefore proposes a maximum harmonisation approach based on the single rule-book principle, which was recommended in the Conclusions of June 2009 European Council, with a set of provisions that allow for some prudential flexibility (application of more stringent rules and additional prudential criteria) in order to ensure that market developments, structural issues and other macro-prudential concerns are appropriately addressed.
7. However, a number of Member States have concerns about reduced national discretion and limited scope of flexibility within the framework of harmonised rules. They fear that the proposed approach might have a negative impact on Member States due to differences in their national financial systems. In particular, a number of delegations pointed out that they would favour additional powers for Member States to set stricter requirements within their jurisdictions (e.g. the possibility of increasing minimum level of capital ratio). They have indicated that as the ultimate (fiscal) responsibility for ensuring financial stability within its jurisdiction is borne by a Member State, Member States must have effective supervisory tools at their disposal. On the other hand, some delegations support the framework and the single rule book principle proposed by the Commission. Those delegations consider that the framework proposed by the Commission already provides for sufficient flexibilities, including through a strengthened "Pillar 2" measures and the countercyclical buffer.

8. The proposed Article 443 of the Regulation empowers the Commission to impose temporary more stringent prudential requirements by way of delegated acts, where this is necessary to address changes in the intensity of micro-prudential and macro-prudential risks. Some delegations oppose such powers being granted to the Commission, while other delegations generally support this idea, provided that the operational framework of these provisions is fine-tuned and delegation of powers is adequately framed.

Liquidity coverage requirement

9. There is agreement that a liquidity coverage requirement (LCR) should be introduced, in order to close an important gap in EU prudential requirements. In view of this general objective, a number of Member States have raised the concerns set out below.
10. Article 444 of the proposed Regulation foresees that the LCR shall be implemented by a delegated act of the Commission (Article 401 and 402 of the proposed Regulation). Such an approach is supported by some Member States that stress the importance of a clear political commitment and to ensure that the 2015 date is met. However, a number of Member States insist that, given the importance of this issue and its possible impact on the economy, the LCR should be implemented by subsequently amending the Regulation under the ordinary legislative procedure while still ensuring that the 2015 date is met. Moreover, provisions dealing with the principle of having adequate liquid assets at all times, are subject to further examination, given that many Member States wish to render the wording more precise.

11. In addition, the proposed framework introduces some changes to the structure of liquidity supervisory arrangements. The main concerns are related to the possibility of establishing single liquidity sub-groups and intra-group treatment. The proposed Regulation foresees an obligation to establish a single liquidity sub-group once certain conditions are met. There seems to be a prospect of agreement on the principle of having a single liquidity sub-group, subject to sufficient safeguards being defined, especially in terms of procedure and conditions of application. Notably, in place of the proposed obligatory waiver of liquidity requirements to subsidiaries if certain conditions are met, a large number of Member States suggests providing for discretion of national competent authorities in this respect. Moreover, the proposed Regulation contains a requirement to apply liquidity intra-group treatment where the single liquidity sub-group has not been established. The proposed solution has very similar features to the single liquidity sub-group issue. Some Member States, however, are of the view that there are no safeguards foreseen within the suggested procedure. The structure of liquidity supervision is subject to further examination.
Leverage ratio requirement

12. With regard to the issue of leverage ratio, the proposed Regulation foresees an obligation to disclose the leverage ratio from 2015, before decision is taken whether it becomes a binding measure upon amendment of the Regulation (Articles 436 and 487) (i.e. before the introduction of mandatory levels of leverage ratio which institutions would be required to meet, with calibration for those levels and appropriate adjustments to the capital measure and total exposure measure). On this issue, some Member States are of the opinion that such disclosure might have a negative impact on market participants and should be postponed till the leverage ratio calibration requirements are completed.

13. Some delegations insist that after revision of the leverage ratio regime, the Regulation should contain provisions that provide for automatic migration of the leverage ratio to "Pillar I", after revision of the leverage ratio regime (i.e. no further legislative action would be needed in this respect, once the leverage ratio calibration is completed).

Collaboration between competent authorities in cases of branch supervision

14. Overall, the Presidency is in a position to note an agreement on the principle that supervision of branches of credit institutions should at all times remain efficient and effective. In this regard, Member States show a high level of flexibility towards finding a workable solution which would streamline supervision procedures between the competent authorities of the "home" and the "host" Member State, as well as further rationalising an exchange of information and contributing to the overall efficiency of supervision of, inter alia, liquidity requirements (Articles 41, 51 and 52 of the proposed Directive).
Further work

15. Following the discussions at the Working Party, the Presidency notes that some of Member States have concerns about definition of own funds, in particular the treatment of significant investments in insurers and the "substance over form" approach on Common Equity Tier I capital, and more work is required in this area. They consider that the proposals of the Commission do not fully transpose the Basel III requirements, while other Member States do not agree with this view. Moreover, the Presidency is of the view that further work is also needed on, inter alia, countercyclical buffers, the sanctioning regime, requirements linked to corporate governance, etc.

16. The Presidency intends to continue scrutiny of these legislative proposals, with the particular aim of identifying other issues of key importance to Member States, as well as attempting to collect the views of Member States on the scope, procedure and timing for the adoption of secondary legislation (including binding technical standards) related to this package. With this future work, the Presidency intends to contribute towards answering the call of the European Council for a swift agreement on these legislative proposals.

III. CONCLUSION

17. Against this background, the Permanent Representatives' Committee is invited to recommend that the Council:

- takes note of progress achieved with regard to the above-mentioned legislative proposals; and
- invites the incoming Presidency and Member States to continue work, with a view to reaching an agreement on a compromise text to advance towards negotiations with the European Parliament, in order to reach an agreement by June 2012.