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NOTE

from :	Presidency
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Subject :	Proposal for a Directive of the European Parliament and of the Council amending Directives 2006/48/EC and 2006/49/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management

Delegations will find below a compromise proposal from the Presidency following the working party meetings on 8, 21 and 30 October and 5 and 13 November 2008.

With respect to the Commission proposal changes are underlined and deletions denoted by (…).

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

amending Directives 2006/48/EC and 2006/49/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 47(2) thereof,

Having regard to the proposal from the Commission,

Having regard to the opinion of the European Economic and Social Committee,

Having regard to the opinion of the European Central Bank,

Having regard to the opinion of the Committee of the Regions,

Acting in accordance with the procedure laid down in Article 251 of the Treaty,

Whereas:

(1) Article 3 of Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions allows Member States to provide for special prudential regimes for credit institutions which are permanently affiliated to a central body since 15 December 1977, provided that those regimes were introduced in national laws no later than 15 December 1979. Those time limits prevent Member States, especially those which have acceded to the European Union since 1980, to introduce the same regimes for similar affiliations of credit institutions which have been set up later on their territories. It is therefore appropriate to remove the time limits set out in Article 3, in order to ensure equal conditions for competition between credit institutions in Member States. The Committee of European Banking Supervisors should provide for non-binding guidelines in order to enhance the convergence of supervisory practices in this regard.

(2) Hybrid capital instruments play an important role in the ongoing capital management of credit institutions. Those instruments allow credit institutions to achieve a diversified capital structure and to access a wide range of financial investors. On 28 October 1998, the Basel Committee on Banking Supervision adopted an agreement on both the eligibility criteria and limits to inclusion of certain types of hybrid capital instruments into original own funds of credit institutions.

(3) Therefore, it is important to lay down criteria for those capital instruments to be eligible for original own funds of credit institutions and to align the provisions in Directive 2006/48/EC to that agreement. The amendments to Annex XII to Directive 2006/48/EC result directly from the establishment of those criteria. (…) Original own funds referred to in Article 57(a) include all instruments that are regarded under national law as equity capital, rank after all other claims during liquidation and fully absorb losses pari passu with ordinary shares on a going concern basis. These instruments may include instruments providing preferential rights for dividend payment on a non cumulative basis, provided that they are included in Article 22 of Directive 86/635/EEC, rank after all other claims during liquidation and fully absorb losses on a going concern basis pari passu with ordinary shares. Original own funds referred to in Article 57(a) also include any other instrument under credit institutions' statutory terms taking into account the specific constitution of mutuals, co-operative societies and similar institutions and which are deemed broadly equivalent to ordinary shares. Instruments that do not rank after all other claims during liquidation or that do not absorb losses on a going concern basis pari passu with ordinary shares are included in the category of hybrids referred to in Article 57(ca).

(4) In order to avoid disruption of markets and to ensure continuity in overall levels of own funds it is appropriate to provide for specific transitional arrangements for the new regime on hybrid capital instruments.

(5) For the purpose of strengthening the crisis management framework of the Community, it is essential that competent authorities coordinate their actions with other competent authorities and where appropriate with central banks in an efficient way. In order to strengthen the efficiency of prudential supervision of parent credit institutions authorised in the Community and to allow competent authorities to better carry out the supervision of a banking group on a consolidated basis, supervisory activities should be coordinated in a more effective manner.

Therefore, Colleges of Supervisors should be established. The establishment of colleges should not affect the rights and responsibilities of the competent authorities under Directive 2006/48/EC. Their establishment should be an instrument for stronger cooperation whereby competent authorities reach agreement on key supervisory tasks. The colleges should facilitate the handling of ongoing supervision and emergency situations. The consolidating supervisor may, in association with the other members of the college, decide to organise meetings or activities that are not of general interest and therefore streamline the attendance as appropriate.

(6) The mandates of competent authorities should take into account <u>in an appropriate way</u> a Community dimension. Competent authorities should therefore <u>duly consider</u> (<u>…</u>) the effect of their decisions on the stability of the financial system in all other Member States <u>concerned</u>. <u>This principle should not bind competent authorities to achieve a specific result, but should rather be understood as a broad objective for promoting financial stability across the European Union</u>.

(7) Competent authorities should be able to participate in colleges established for the supervision of credit institutions the parent institution of which is situated in a third country. The Committee of European Banking Supervisors should provide, where necessary, for non-binding guidelines and recommendations in order to enhance the convergence of supervisory practices pursuant to Directive 2006/48/EC.

(8) Information deficits between the home and the host competent authorities may prove detrimental to the financial stability in host Member states. The information rights of host supervisors, in particular in a crisis of (<u>…</u>) <u>significant</u> branches, should therefore be reinforced. For that purpose, (<u>…</u>) <u>significant</u> branches should be defined. Competent authorities should transmit information which is essential for the pursuance of tasks of central banks and of Ministries of Finance with respect to financial crises.

(9) Excessive concentration of exposures to a single client or group of connected clients may result in an unacceptable risk of loss. Such a situation can be considered prejudicial to the solvency of a credit institution. The monitoring and control of large exposures of credit institution should therefore be an integral part of its supervision.

(10) The current large exposure regime dates back to 1992. Therefore, the existing requirements on large exposure set out in Directive 2006/48/EC and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions should be reviewed.

(11) Since credit institutions in the internal market are engaged in direct competition, the essential rules for monitoring and control of large exposures of credit institutions should be further harmonised. In order to reduce administrative burden for credit institutions the number of options for Members States as far as large exposures are concerned should be reduced.

(12) In determining the existence of a group of connected clients and thus exposures constituting a single risk, it is important to take into account also risks arising from a common source of significant funding provided by the credit institution or investment firm itself, its financial group or its connected parties.

(13) While it is desirable to base the calculation of the exposure value on that provided for the purposes of minimum own funds requirements, it is appropriate to adopt rules for the monitoring of large exposures without applying risk weightings or degrees of risk. Moreover, the credit risk mitigation techniques applied in the solvency regime were designed with the assumption of a well-diversified credit risk. In case of large exposures, dealing with single name concentration risk, credit risk is not well-diversified. Therefore effects of those techniques should be subject to prudential safeguards. In this context, it is necessary to provide for an effective recovery of the credit protection for the purposes of large exposures.

(14) Since a loss arising from an exposure to a credit institutions or an investment firm can be as severe as a loss from any other exposure, such exposures should be treated and reported as any other exposures. <u>However, an alternative quantitative limit has been introduced to alleviate disproportionate impact of such approach on smaller institutions</u>.

(15) It is important to remove misalignment between the interest of firms that 're-package' loans into tradable securities and other financial instruments (originators <u>or sponsors</u>) and firms that invest in these securities or instruments (investors).

It is therefore important for the originators or the sponsors to retain exposure to the risk of the loans in question; the exposure of the originators or the sponsors shall be to this end a net exposure after the effects of credit risk mitigation techniques so that an alignment of interest with investors is achieved by the retention. Such retention should be applicable in all situations where the economic substance of a securitisation according to the definition of the directive is applicable, whatever legal structures or instruments are used to obtain this economic substance. In particular where credit risk is transferred by securitisation, investors should make their decisions only after conducting thorough due diligence, for which they need adequate information about the securitisations. The measures to address the potential misalignment of these structures need to be consistent and coherent in all relevant financial sector regulation; the Commission intends to bring forward the appropriate legislative proposals to ensure this will be the case, after duly considering the impact.

(16) Annex III to Directive 2006/48/EC should be adapted in order to clarify certain provisions with a view to enhance convergence of supervisory practices.

(17) Recent market developments have highlighted the fact that liquidity risk management is a key determinant of the soundness of credit institutions. The criteria set out in Annex V and XI to Directive 2006/48/EC should be reinforced in order to align those provisions to the work conducted by the Committee of European Banking Supervisors and the Basel Committee on Banking Supervision.

(18) The measures necessary for the implementation of Directive 2006/48/EC should be adopted in accordance with Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission.

(19) In particular the Commission should be empowered to amend Annex III of Directive 2006/48/EC in order to take account of developments on financial markets or in accounting standards or requirements which take account of Community legislation, or with regard to convergence of supervisory practice and to alter the amount (…) specified in Article 111(1) of that Directive to take account of developments on financial markets. Since those measures are of general scope and are designed to amend non-essential elements of Directive 2006/48/EC, they must be adopted in accordance with the regulatory procedure with scrutiny provided for in Article 5a of Decision 1999/468/EC.

(20) Since the objectives of the proposed action, namely the introduction of rules concerning the taking up and pursuit of the business of credit institutions, and their prudential supervision, cannot be sufficiently achieved by the Member States because it requires the harmonisation of a multitude of different rules existing in the legal systems of the various Member States and can therefore be better achieved at Community level, the Community may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary in order to achieve those objectives.

(20a) The Council, in accordance with paragraph 34 of the Interinstitutional agreement on better law-making, should encourage Member States to draw up, for themselves and in the interest of the Community, their own tables, which will, as far as possible, illustrate the correlation between the Directive and the transposition measures and to make them public.

(21) Directives 2006/48/EC and 2006/49/EC should therefore be amended accordingly,

HAVE ADOPTED THIS DIRECTIVE:

Article 1

Amendments to Directive 2006/48/EC

Directive 2006/48/EC is amended as follows:

1. Article 3(1) is amended as follows:

(a) The introductory phrase in the first subparagraph is replaced by the following:

"One or more credit institutions situated in the same Member State and which are permanently affiliated to a central body which supervises them and which is established in the same Member State, may be exempted from the requirements of Articles 7 and 11(1) if national law provides that:"

(b) The second and third subparagraphs are deleted.

2. Article 4 is amended as follows:

(a) Point (6) is replaced by the following:

"(6) 'institutions' for the purposes of Sections 2, 3 and 5 of Title V, Chapter 2, means institutions as defined in Article 3(1)(c) of Directive 2006/49/EC;"

(b) Point (45)(b) is replaced by the following:

"(b) two or more natural or legal persons between whom there is no relationship of control as set out in point (a) but who are to be regarded as constituting a single risk because they are so interconnected that, if one of them were to experience financial problems, in particular funding or repayment difficulties, the other or all of the others would be likely to encounter funding or repayment difficulties."

(c) Point (48) is added:

"(48) 'consolidating supervisor' means the competent authority responsible for the exercise of supervision on a consolidated basis of EU parent credit institutions and credit institutions controlled by EU parent financial holding companies."

3. In Article 40 the following paragraph 3 is added:

"3. The competent authorities in one Member State shall (…), in the exercise of their duties, duly consider the potential impact of their decisions on the stability of the financial system in all other Member States concerned and, in particular, in emergency situations, based on the available information."

4. The following Article 42a is inserted:

"Article 42a

1. The competent authorities of a host Member State may make a request to the consolidating supervisor where Article 129(1) applies or to the competent authorities of the home Member State, for a branch of a credit institution to be considered as significant (…).

The request shall provide reasons for considering the branch to be (…) significant with particular regard to the following:

(a) whether the market share of the branch of a credit institution in terms of deposit exceeds 2% in the host Member State;

(b) the likely impact of a suspension or closure of the operations of the credit institution on the payment and clearing and settlement systems in the host Member State;

(c) the size and the importance of the branch in terms of number of clients within the context of banking or financial system of the host Member State.

The competent authorities of the home and the host Member State, and the consolidating supervisor where Article 129(1) applies, shall do everything within their power to reach a joint decision on the designation of branches as being (…) significant.

If no joint decision is reached within two months of receipt of a request under the first subparagraph, the competent authorities of the host Member State shall take their own decision within a further period of two months on whether the branch is (…) significant. In taking its decision, the competent authorities of the host Member State shall take into account any views and reservations of the consolidating supervisor or the competent authorities of the home Member State.

The decisions referred to in the third and fourth subparagraph shall be set out in a document containing the fully reasoned decision, transmitted to the competent authorities concerned, recognised as determinative and applied by the competent authorities in the Member States concerned.

The designation of a branch as being (…) significant shall not affect the rights and responsibilities of the competent authorities under this Directive.

2. The competent authorities of the home Member State shall communicate to the competent authorities of a host Member State where a (…) significant branch is established the information referred to in Article 132(1)(c) and (d) and carry out the tasks referred to in Article 129(1)(c) in cooperation with the competent authorities of the host Member State.

If a competent authority of a home Member State becomes aware of an emergency situation within a credit institution as referred to in Article 130(1), it shall alert as soon as practicable the authorities referred to in the fourth paragraph of Article 49 and in Article 50.

3. Where Article 131a does not apply, the competent authorities supervising a credit institution with (…) significant branches in other Member States shall establish and chair a college of supervisors to facilitate the cooperation under Article 42 and paragraph 2 of this Article. The establishment and functioning of the college shall be based on written arrangements determined, after consultation with competent authorities concerned, by the competent authority of the home Member State. The competent authority of the home Member State shall decide which competent authorities participate in a meeting or in an activity of the college.

The decision of the competent authority of the home Member State shall take account of the relevance of the supervisory activity to be planned or coordinated for those authorities, in particular the potential impact on the stability of the financial system in the Member States concerned referred to in Articles 40(3) and the obligations in 42a(2).

The competent authority of the home Member State shall keep all members of the college fully informed, in advance, of the organisation of such meetings, the main issues to be discussed and the activities to be considered. The competent authority of the home Member State shall also keep all the members of the college fully informed, in a timely manner, of the actions taken in those meetings or the measures carried out."

5. The following Article 42b is inserted:

"Article 42b

1. In the exercise of their duties, competent authorities shall (…) have regard to the convergence in respect of supervisory tools and supervisory practices in the application of the laws, regulations and administrative requirements adopted pursuant to this Directive. For that purpose, Member States shall ensure that the competent authorities participate in the activities of the Committee of European Banking Supervisors and take into account its non-binding guidelines and recommendations.

2. The Committee of European Banking Supervisors shall report to the Council, the European Parliament and the European Commission on the progress made towards supervisory convergence every three years starting from 31 December 2010."

6. Article 49 is amended as follows:

(a) In the first paragraph, point (a) is replaced by the following:

"(a) central banks in the Community and other bodies with a similar function in their capacity as monetary authorities when this information is relevant for the exercise of their (…) statutory tasks, including the conduct of monetary policy, the oversight of payments and securities settlement systems, and the safeguarding of financial stability; and"

(b) The following paragraph is added at the end of the Article:

"In an emergency situation as referred to in Article 130(1), Member States shall allow competent authorities to communicate information to central banks in the Community when this information is relevant for the exercise of their (…) statutory tasks, including the conduct of monetary policy, the oversight of payments and securities settlement systems, and the safeguarding of financial stability."

7. In Article 50, the following paragraph is added:

"In an emergency situation as referred to in Article 130(1), Member States shall allow competent authorities to disclose information to the departments referred to in the first paragraph in all Member States concerned.

7 bis. Subsection 2 of Section 2 of Chapter 2 of Title V is amended as follows:

The subtitle "Calculation of requirements" is replaced by "Calculation of requirements and reporting requirements"

7 ter. In Article 74, the following paragraph is inserted after the first paragraph of point 2:

"For the communication of these calculations by credit institutions, competent authorities shall apply, by 31 December 2012, uniform formats, frequencies and dates of reporting. To facilitate this, the Committee of European Banking Supervisors shall elaborate guidelines to introduce, within the Community, a uniform reporting format at the latest by 1 January 2012."

8. Article 57 is amended as follows:

(a) Point (a) is replaced by the following:

"(a) capital within the meaning of Article 22 of Directive 86/635/EEC, in so far as it has been paid up, plus the related share premium accounts, it fully absorbs losses in going concern situations, and in the event of bankruptcy or liquidation ranks after all other claims."

(b) The following point (ca) is inserted:

"(ca) "instruments other than those referred to in point (a), which meet the requirements set out in points (a), (c), (d) and (e) of Article 63 (2) and in Article 63a;"

9. The first paragraph of Article 61 is replaced by the following:

"The concept of own funds as defined in points (a) to (h) of Article 57 embodies a maximum number of items and amounts. Member States may decide on the use of those items and on the deduction of items other than those listed in points (i) to (r) of Article 57."

10. In Article 63(2), the following subparagraph is added:

"Instruments referred to in point (ca) of Article 57 shall comply with the requirements set out in points (a), (c), (d) and (e) of this Article."

11. The following Article 63a is inserted:

"*Article 63a*

"1. Instruments referred to in point (ca) of Article 57 shall comply with the requirements set out in paragraph 2 to 5 of this Article.

2. The instruments shall be undated or have an original maturity of at least 30 years. Those instruments may include one or more call options at the sole discretion of the issuer, but they shall not be redeemed before five years after the date of issue. If the statutory or contractual provisions governing undated instruments provide for a moderate incentive for the credit institution to redeem as determined by the competent authorities, such incentive shall not occur before ten years after the date of issue. <u>The statutory or contractual provisions governing dated instruments shall not allow for any incentive to redeem other than the maturity date</u>.

Dated and undated instruments may be called or redeemed only with the prior consent of the competent authorities. The competent authorities may grant permission provided the request is made at the initiative of the credit institution and either financial or solvency conditions of the credit institution are not unduly affected. The competent authorities may require institutions to replace the instrument by items of the same or better quality referred to in point <u>(a) or</u> (ca) of Article 57.

The competent authorities shall require the suspension of the redemption for dated instruments if the credit institution does not comply with the capital requirements set out in Article 75 <u>and may require the suspension of the redemption at other times based on the financial and solvency situation of credit institutions</u>.

The competent authority may grant permission at any time for an early redemption of dated and undated instruments in the event that there is a change in the applicable tax treatment or regulatory classification of such instruments which was unforeseen at the date of issue.

3. The statutory or contractual provisions governing the instrument shall allow the credit institution to cancel, when necessary, the payment of interest or dividends for an unlimited period of time, on a non-cumulative basis.

However, the credit institution shall cancel such payments if it does not comply with the capital requirements set out in Article 75.

The competent authorities may require the cancellation of such payments based on the financial and solvency situation of the credit institution. Any such cancellation shall not prejudice the right of the credit institution to substitute the payment of interest or dividend by a payment in the form of an instrument referred to in point (a) of Article 57, provided that any such mechanism allows the credit institution to preserve financial resources. Such substitution may be subject to specific conditions established by the competent authorities.

4. The statutory or contractual provisions governing the instrument shall provide for principal, unpaid interest or dividend to be such as to absorb losses and to not hinder the recapitalisation of the credit institution through appropriate mechanisms, as elaborated by the Committee of European Banking Supervisors under paragraph 6.

5. In the event of the bankruptcy or liquidation of the credit institution, the instruments shall rank after the items referred to in Article 63(2).

6. The Committee of European Banking Supervisors shall elaborate guidelines for the convergence of supervisory practices with regard to the instruments referred to in paragraph 1 and shall monitor their application. By 1 January 2012, the Commission shall review the application of this Article and shall report to the Parliament and the Council together with any appropriate proposals to ensure the quality of own funds.

12. In Article 65(1), point (a) is replaced by the following:

"(a) any minority interests within the meaning of Article 21 of Directive 83/349/EEC, where the global integration method is used. Any instruments referred to in point (ca) of Article 57, which give rise to minority interests shall meet the requirements under Articles 63a, 66, and points (a), (c), (d) and (e) of Article 63(2);"

13. Article 66 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. The items referred to in points (d) to (h) of Article 57 shall be subject to the following limits:

(a) the total of the items in points (d) to (h) of Article 57 may not exceed a maximum of 100 % of the items in points (a) to (ca) minus (i), (j) and (k) <u>of</u> that Article; and

(b) the total of the items in points (g) to (h) of Article 57 may not exceed a maximum of 50 % of the items in points (a) to (ca) minus (i), (j) and (k) of that Article."

(b) The following paragraph 1a is inserted:

"1a. Notwithstanding paragraph 1, the total of the items in point (ca) of Article 57 shall be subject to the following limits:

(a) instruments that must be converted during emergency situations <u>and may be converted at the initiative of the competent authority, at any time, based on the financial and solvency situation of the issuer</u> into items referred to in point (a) of Article 57 within a pre-determined range (<u>…</u>) shall in total not exceed a maximum of 50% of the items in points (a) to (ca) minus (i), (j) and (k) of Article 57;

(b) within the limit referred to in point (a) of this paragraph, all other instruments shall not exceed a maximum of 35% of the items in points (a) to (ca) minus (i), (j) and (k) of Article 57;

(c) within the limits referred to in points (a) and (b) of this paragraph, dated instruments and any instrument, whose statutory or contractual provisions provide for an incentive for the credit institution to redeem shall not exceed a maximum of 15% of the items in points (a) to (ca) minus (i), (j) and (k) of Article 57;

(d) the amount of items exceeding the limits set out in points (a), (b) and (c) shall be subject to the limit set out in paragraph 1."

(c) Paragraph 2 is replaced by the following:

"2. The total of the items in points (l) to (r) of Article 57 shall be deducted half from the total of the items (a) to (ca) minus (i), (j) and (k) of that Article, and half from the total of the items (d) to (h) of that Article, after application of the limits laid down in paragraph 1 of this Article. To the extent that half of the total of the items (l) to (r) of Article 57 exceeds the total of the items (d) to (h) of that Article, the excess shall be deducted from the total of the items (a) to (ca) minus (i), (j) and (k) of that Article. Items in point (r) of Article 57 shall not be deducted if they have been included in the calculation of risk-weighted exposure amounts for the purposes of Article 75 as referred to in Annex IX, Part 4."

(d) Paragraph 4 is replaced by the following:

"4. The competent authorities may authorise credit institutions to exceed the limits laid down in paragraphs 1 and 1a temporarily during emergency situations."

14. Article 87 is amended as follows:

(a) Paragraph 11 is replaced by the following:

"11. Where exposures in the form of a collective investment undertaking (CIU) meet the criteria set out in Annex VI, Part 1, points 77 and 78 and the credit institution is aware of all or parts of the underlying exposures of the CIU, the credit institution shall look through to those underlying exposures in order to calculate risk-weighted exposure amounts and expected loss amounts in accordance with the methods set out in this Subsection. Paragraph 12 shall apply to the part of the underlying exposures of the CIU the credit institution is not aware of (…) or could not reasonably be aware of. In particular, paragraph 12 shall apply where it would be unduly burdensome for the credit institution to look through the underlying exposures in order to calculate risk-weighted amounts and expected loss amounts in accordance with methods set out in this section.

Where the credit institution does not meet the conditions for using the methods set out in this Subsection for all or parts of the underlying exposures of the CIU, risk weighted exposure amounts and expected loss amounts shall be calculated in accordance with the following approaches:

(a) for exposures belonging to the exposure class referred to in point (e) of Article 86(1), the approach set out in Annex VII, Part 1, points 19 to 21;

(b) for all other underlying exposures, the approach set out in Articles 78 to 83, subject to the following modifications:

(i) for exposures subject to a specific risk weight for unrated exposures or subject to the (…) credit quality step yielding the highest risk weight for a given exposure class, the risk weight shall be multiplied by a factor of 2 but cannot be higher than 1250%;

(ii) for all other exposures, the risk weight shall be multiplied by a factor of 1.1 and subject to a minimum of 5%.

If, for the purposes of point (a), the credit institution is unable to differentiate between private equity, exchange-traded and other equity exposures, it shall treat the exposures concerned as other equity exposures. Without prejudice to Article 154(6), where these exposures, taken together with the credit institution's direct exposures in this exposure class, are not material within the meaning of Article 89(2), paragraph 1 of that Article may be applied subject to the approval of the competent authorities."

(b) In paragraph 12, the second subparagraph is replaced by the following:

"Alternatively to the method described in the first subparagraph, credit institutions may calculate themselves or may rely on a third party to calculate and report the average risk weighted exposure amounts based on the CIU's underlying exposures in accordance with the approaches referred to in points (a) and (b) of paragraph 11, provided that the correctness of the calculation and the report is adequately ensured."

15. In Article 89, the introductory phrase of point (d) is replaced by the following:

"(d) exposures to central governments of the Member States and their regional governments, local authorities and administrative bodies provided that"

16. Article 106 is amended as follows:

(a) Paragraph 2 is replaced by the following:

"2. Exposures shall not include any of the following:

(a) in the case of foreign exchange transactions, exposures incurred in the ordinary course of settlement during the 48 hours following payment;

(b) in the case of transactions for the purchase or sale of securities, exposures incurred in the ordinary course of settlement during the five working days following payment or delivery of the securities, whichever is the earlier; or

(c) in the case of the provision of money transmission or (…) financial instruments clearing, (…) settlement and custody services to clients, delayed receipts in funding and other exposures arising from client activity, which do not last longer than the following business day."

(b) Paragraph 3 is added:

"3. In order to determine the existence of a group of connected clients, in respect of exposures referred to in points (m), (o) and (p) of Article 79(1), where there is an exposure to underlying assets, a credit institution shall assess the scheme (…) or its underlying exposures, or both. For that purpose, a credit institution shall evaluate the economic substance and the risks inherent in the structure of the transaction."

17. Article 107 is replaced by the following:

"Article 107

For the purposes of calculating the value of exposures in accordance with this Section, the term 'credit institution' shall also cover any private or public undertaking, including its branches, which meets the definition of 'credit institution' and has been authorised in a third country."

18. Article 110 is replaced by the following:

"Article 110

1. A credit institution shall report the following information about every large exposure to the competent authorities, including large exposures exempted from the application of Article 111(1):

(a) the identification of the client or the group of connected clients to which a credit institution has a large exposure;

(b) the exposure value before taking into account the effect of the credit risk mitigation, when applicable (…);

(c) where used, the type of funded or unfunded credit protection;

(d) the exposure value after taking into account the effect of the credit risk mitigation calculated for the purpose of Article 111(1).

If a credit institution is subject to Articles 84 to 89, its 20 largest exposures on a consolidated basis, excluding those exempted from the application of Article 111(1), shall be made available to the competent authorities.

2. Member States shall provide that reporting is to be carried out at least twice a year.

3. Member States shall require credit institutions to analyse, to the extent possible, their exposures to collateral issuers, (…) providers of unfunded credit protection and underlying assets pursuant to Article 106(3) for possible concentrations and where appropriate take action and report any significant findings to their competent authority."

19. Article 111 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. A credit institution may not incur an exposure, after taking into account the effect of the credit risk mitigation in accordance with Articles 112 to 117, to a client or group of connected clients the value of which exceeds 25% of its own funds.

Where that client is an institution or where a group of connected clients includes one or more institutions, this value may not exceed 25% of the credit institution's own funds or the amount of EUR 150 million, whichever is higher, provided that the sum of exposure values, after taking into account the effect of the credit risk mitigation in accordance with Articles 112 to 117, to all connected clients that are not institutions does not exceed 25% of the credit institution's own funds.

Where the amount of EUR 150 million is higher than 25% of the credit institution's own funds, the value of the exposure, after taking into account the effect of credit risk mitigation in accordance with Articles 112 to 117, shall not exceed a reasonable limit in terms of the credit institution's own funds. This limit shall be determined by credit institutions, consistently with the policies and procedures referred to in Annex V, point 5, to address and control concentration risk, and shall not be higher than 100% of the credit institution's own funds.

Member States may set a lower limit than EUR 150 million and shall inform the Commission."

(b) Paragraphs 2 and 3 are deleted.

(c) Paragraph 4 is replaced by the following:

"4. A credit institution shall at all times comply with the limit laid down in paragraph 1. If in an exceptional case exposures exceed this limit, the value of the exposure shall be reported without delay to the competent authorities which may, where the circumstances warrant it, allow the credit institution a limited period of time in which to comply with the limit.

<u>Where the amount of EUR 150 million referred to in paragraph 1 is applicable, the competent authorities may allow on a case by case basis that the 100% limit in terms of the credit institution's own funds can be exceeded</u>."

20. Article 112 is amended as follows:

(a) Paragraph 2 is replaced by the following:

"2. Subject to paragraph 3, where, under Articles 113 to 117, the recognition of funded or unfunded credit protection is permitted, this shall be subject to compliance with the eligibility requirements and other minimum requirements, set out in Articles 90 to 93."

(b) The following paragraph 4 is added:

"4. For the purpose of this Section, a credit institution shall not take into account the collateral referred to in Annex VIII, Part 1, points 20 to 22, unless permitted under Article 115."

21. Article 113 is amended as follows:

(a) Paragraphs 1 and 2 are deleted.

(b) Paragraph 3 is amended as follows:

(i) The introductory phrase is replaced by the following:

"3. The following exposures shall be exempted from the application of Article 111(1):"

(ii) Points (e) and (f) are replaced by the following:

"(e) asset items constituting claims on regional governments and local authorities of Member States where those claims would be assigned a 0 % risk weight under Articles 78 to 83 and other exposures to or guaranteed by such governments and authorities claims on which would be assigned a 0 % risk weight under Articles 78 to 83;

(f) exposures to counterparties referred to in paragraph 7 or paragraph 8 of Article 80 if they would be assigned a 0% risk weight under Articles 78 to 83; exposures that do not meet these criteria, whether exempted from Article 111(1) or not, shall be treated as exposures to a third party."

(iii) Point (i) is replaced by the following:

"(i) exposures arising from undrawn credit facilities that are classified as low risk off-balance sheet items in Annex II and provided that an agreement has been concluded with the client or group of connected clients under which the facility may be drawn only if it has been ascertained that it will not cause the limit applicable under Article 111(1) to be exceeded."

(iv) Points (j) to (t) are deleted.

(c) The third, fourth and fifth subparagraphs are deleted.

(d) The following paragraph 4 is added:

"4. Member States may fully or partially exempt the following exposures from the application of Article 111(1):

(a) covered bonds falling within the terms of Annex VI, Part 1, points 68, 69 and 70;

(b) asset items constituting claims on regional governments and local authorities of Member States where those claims would be assigned a 20% risk weight under Articles 78 to 83 and other exposures to or guaranteed by such governments and authorities claims on which would be assigned a 20% risk weight under Articles 78 to 83;

(c) notwithstanding point (f) of paragraph 3 of this Article, exposures incurred by a credit institution to its parent undertaking, to other subsidiaries of that parent undertaking or to its own subsidiaries, in so far as those undertakings are covered by the supervision on a consolidated basis to which the credit institution itself is subject, in accordance with this Directive or with equivalent standards in force in a third country; exposures that do not meet these criteria, where exempted from Article 111(1) or not, shall be treated as exposures to a third party;

(d) asset items constituting claims on and other exposures (…) including participations or other kind of holdings (…), to regional or central credit institutions with which the lending credit institution is associated in a network in accordance with legal or statutory provisions and which are responsible, under those provisions, for cash-clearing operations within the network;

(e) asset items constituting claims on and other exposures to credit institutions incurred by credit institutions operating on a non-competitive basis providing loans under legislative programmes or their statutes to promote specified sectors of the economy under some form of government oversight and restrictions on the use of the loans provided that the respective exposures arise from such loans that are passed on to the beneficiaries via other credit institutions;

(f) asset items constituting claims on and other exposures to institutions, provided that these exposures do not constitute such institutions' own funds, do not last longer than the following business day and are denominated in a currency of the Member State exercising this option, provided that such currency is not the euro or the sterling;

(g) 50% of medium/low risk off-balance sheet documentary credits and of medium/low risk off-balance sheet undrawn credit facilities referred to in Annex II and subject to the competent authorities' agreement, 80% of guarantees other than loan guarantees which have a legal or regulatory basis and are given for their members by mutual guarantee schemes possessing the status of credit institution;

(h) asset items constituting claims on central banks in the form of required minimum reserves held at these central banks, and which are denominated in the national currencies of the borrowers."

22. Article 114 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. Subject to paragraph 3, for the purposes of calculating the value of exposures for the purposes of Article 111(1) a credit institution may use the 'fully adjusted exposure value' as calculated under Articles 90 to 93, taking into account the credit risk mitigation, volatility adjustments, and any maturity mismatch (E*)."

(b) Paragraph 2 is amended as follows:

(i) The first subparagraph is replaced by the following:

"Subject to paragraph 3, a credit institution permitted to use own estimates of LGDs and conversion factors for an exposure class under Articles 84 to 89 shall be permitted, where it is able to the satisfaction of the competent authorities to estimate the effects of financial collateral on their exposures separately from other LGD-relevant aspects, to recognise such effects in calculating the value of exposures for the purposes of Article 111(1)."

(ii) The fourth subparagraph is replaced by the following:

"Credit institutions permitted to use own estimates of LGDs and conversion factors for an exposure class under Articles 84 to 89 which do not calculate the value of their exposures using the method referred to in the first subparagraph may use the Financial Collateral Comprehensive Method or the approach set out in Article 117(1)(b) for calculating the value of exposures."

(c) Paragraph 3 is amended as follows:

(i) The first subparagraph is replaced by the following:

"A credit institution that makes use of the Financial Collateral Comprehensive Method or is permitted to use the method described in paragraph 2 in calculating the value of exposures for the purposes of Article 111(1), shall conduct periodic stress tests of their credit-risk concentrations, including in relation to the realisable value of any collateral taken."

(ii) The fourth subparagraph is replaced by the following:

"In the event that such a stress test indicates a lower realisable value of collateral taken than would be permitted to be taken into account while making use of the Financial Collateral Comprehensive Method or the method described in paragraph 2 as appropriate, the value of collateral permitted to be recognised in calculating the value of exposures for the purposes of Article 111(1) shall be reduced accordingly."

(iii) In the fifth subparagraph, point (b) is replaced by the following:

"(b) policies and procedures in the event that a stress test indicates a lower realisable value of collateral than taken into account while making use of the Financial Collateral Comprehensive Method or the method described in paragraph 2; and"

(d) Paragraph 4 is deleted.

23. Article 115 is replaced by the following:

"*Article 115*

1. For the purpose of this Section, a credit institution may reduce the exposure value by up to 50% of the value of the residential property concerned, if either of the following conditions is met:

(a) the exposure is secured, by mortgages on residential property or by shares in Finnish residential housing companies, operating in accordance with the Finnish Housing Company Act of 1991 or subsequent equivalent legislation;

(b) the exposure relates to a leasing transaction under which the lessor retains full ownership of the residential property leased for as long as the lessee has not exercised his option to purchase.

The value of the property shall be calculated, to the satisfaction of the competent authorities, on the basis of (…) prudent valuation standards laid down by law, regulation or administrative provisions. (…)

Residential property shall mean a residence to be occupied or let by the owner.

2. For the purpose of this Section, a credit institution may reduce the exposure value by up to 50% of the value of the commercial property concerned, only if the competent authorities concerned in the Member State where the commercial property is situated allow the following exposures (…) to receive a 50% risk weight (…) in accordance with Articles 78 to 83:

(a) exposures secured by mortgages on offices or other commercial premises, or by shares in Finnish housing companies, operating in accordance with the Finnish Housing Company Act of 1991 or subsequent equivalent legislation, in respect of offices or other commercial premises; or

(b) exposures related to property leasing transactions concerning offices or other commercial premises.

The value of the property shall be calculated, to the satisfaction of the competent authorities, on the basis of prudent valuation standards laid down by law, regulation or administrative provisions.

Commercial property shall be fully constructed, (…) leased and produce appropriate rental income."

24. Article 116 is deleted.

25. Article 117 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. Where an exposure to a client is guaranteed by a third party, or secured by collateral issued by a third party, a credit institution may:

(a) treat the portion of the exposure which is guaranteed as having been incurred to the guarantor rather than to the client provided that the unsecured exposure to the guarantor would be assigned an equal or lower risk weight than a risk weight of the unsecured exposure to the client under Articles 78 to 83;

(b) treat the portion of the exposure collateralised by the market value of recognised collateral as having been incurred to the third party rather than to the client, if the exposure is secured by collateral and provided that the collateralised portion of the exposure would be assigned an equal or lower risk weight than a risk weight of the unsecured exposure to the client under Articles 78 to 83.

The approach referred to in point (b) shall not be used by a credit institution where there is a mismatch between the maturity of the exposure and the maturity of the protection.

For the purpose of this Section, a credit institution may use both the Financial Collateral Comprehensive Method and the treatment provided for in point (b) of the first subparagraph only where it is permitted to use both the Financial Collateral Comprehensive Method and the Financial Collateral Simple Method for the purposes of Article 75(a)."

(b) In paragraph 2, the introductory phrase is replaced by the following:

"Where a credit institution applies point (a) of paragraph 1:"

26. Article 119 is deleted.

27. The following Section 7 is added to Chapter 2:

"Section 7

Exposures to transferred credit risk

Article 122a

1. A credit institution, other than an originator, a sponsor or original lender, shall only be exposed to the credit risk of a securitisation position in its trading book or non-trading book (…) if the originator, sponsor or original lender:

(…)

(…)

has (…) explicitly disclosed (…) to the credit institution that it will retain, on an ongoing basis, a material net economic interest (…) which, in any event shall not be less than 5 per cent (…).

For this purpose, retention of net economic interest shall mean either:

a) retention of not less than 5 % of the nominal value of each of the tranches sold or transferred to the investors; or

b) in the case of securitisations of revolving exposures, retention of originator's interest of not less than 5% of the nominal value of the securitised exposures; or

c) retention of randomly selected exposures, equivalent to not less than 5% of the nominal amount of the securitised exposures, where these would otherwise have been securitised in the securitisation provided that the number of potentially securitised exposures is not less than 100 at origination; or

d) retention of the first loss tranche and, if necessary, other tranches having the same or more severe risk profile than those transferred or sold to investors, so that the retention equals in total not less than 5% of the nominal value of the securitised exposures.

Net economic interest is measured at the origination and shall be maintained on an on-going basis. It shall not be subject to any credit risk mitigation or any short positions or any other hedge. The net economic interest shall be determined by the notional value for off-balance sheet items.

For the purpose of this Article, "on-going basis" shall mean that retained positions, interest or exposures shall not be hedged or sold.

1 bis. Where an EU parent credit institution or an EU financial holding company, or one of its subsidiaries, as an originator or a sponsor, securitises exposures from several institutions or financial institutions which are included in the scope of supervision on a consolidated basis, the requirement referred to in the first subparagraph may be satisfied on the basis of the consolidated situation of the related EU parent credit institution or EU financial holding company. This paragraph shall only apply where institutions or financial institutions which created the securitised exposures have committed themselves to adhere to the requirements set out in paragraph 5 and deliver, in a timely manner, to the originator or sponsor and to the EU parent credit institution or an EU financial holding company the information needed to satisfy the requirements referred to in paragraph 6.

2. Paragraph 1 shall not apply when the securitised exposures are (…) claims or contingent claims on or guaranteed by:

(a) central governments or central banks;

(b) regional governments, local authorities and public sector entities of Member States;

(c) institutions to which a 50% risk weight or less is assigned under Articles 78 to 83; and

(d) multilateral development banks.

Paragraph 1 shall not apply to:

(a) transactions based on an index, where the underlying reference entities are identical to those that make up an index of entities that is widely traded, or are other tradeable securities other than securitisation positions;

(b) syndicated loans, purchased receivables or credit default swaps where these instruments are not used to package and/or hedge a securitisation that is covered by paragraph 1.

(…)

3. deleted

3. (…) Credit institutions, other than originators or sponsors or original lenders, shall be able to demonstrate, from the moment they invest on, (…) to the competent authorities for each of their individual securitisation positions that they have a comprehensive and thorough understanding of and have implemented formal policies and procedures appropriate to their trading book and non-trading book and commensurate with the risk profile of their investments in securitised positions for analysing and recording (…):

(a) (…) information disclosed under paragraph 1, (…) by originators (…) or sponsors to specify the (…) net economic interest that they maintain, on an on-going basis, in the securitisation (…);

(b) the risk characteristics of the individual securitisation position;

(c) the risk characteristics of the exposures underlying the securitisation position;

(d) the reputation and loss experience in earlier securitisations of the originators or sponsors in the relevant exposure classes underlying the securitization position;

(e) the statements made by the originator or sponsor, or its agent or advisor, about (…) its due diligence to ensure the quality of the securitised exposures (…) and, where applicable, on the collateral quality of the securitised exposures (…);

(f) where applicable, the methodologies and concepts on which the valuation of collateral supporting the securitised exposures (…) is based and the policies adopted by the originator or sponsor to ensure the independence of the valuer; and

(g) all the structural features of the securitisation that can materially impact the performance of the credit institution's securitisation position. (…) Credit institutions shall (…) regularly (…) perform (…) their own stress tests appropriate to their securitisation positions. To this end, credit institutions shall not only rely on stress tests performed by an ECAI. (…).

4. Credit institutions, other than originators or sponsors or original lenders, shall establish formal procedures appropriate to their trading book and non-trading book and commensurate with the risk profile of their investments in securitised positions to monitor on an ongoing basis and in a timely manner performance information on the exposures underlying their securitisation positions. Where appropriate (…), this shall include (…): the exposure type, (…) the percentage of loans more than 30, 60 and 90 days past due, default rates, prepayment rates, loans in foreclosure, collateral type and occupancy, frequency distribution of credit scores or other measures of credit worthiness across underlying exposures, industry and geographical diversification, frequency distribution of loan to value ratios with band widths that facilitate adequate sensitivity analysis. Where the underlying exposures are themselves securitisation positions, credit institutions shall have the above listed information not only on the underlying securitisation tranches, such as the issuer name and credit quality, but also on the characteristics and performance of the pools underlying securitisation tranches (…).

Credit institutions shall have a thorough understanding of all structural features of a securitisation transaction that would materially impact the performance of their exposures to the transaction such as the contractual waterfall and waterfall related triggers, credit enhancements, liquidity enhancements, market value triggers, and deal-specific definition of default.

Where the requirements in paragraph 3 and in this paragraph are not met in any material respect, and by reason of negligence or omission, credit institutions shall apply a risk weight of 1250% to these securitisation positions under Annex IX, part 4 except where competent authorities have decided to temporarily suspend the requirements referred to in paragraphs 1 and 2 during periods of general market liquidity stress.

5. (…) Originator credit institutions shall apply the same sound and well-defined criteria for credit-granting in accordance with the requirements of Annex V, point 3 to exposures to be securitised as they apply to exposures to be held on their (…) book. To this end the same processes for approving and, where relevant, amending, renewing and re-financing credits shall be applied by the originator (…) credit institutions. Credit institutions shall also apply the same standards (…) to securitisation positions (…) purchased from third parties (…). The same standards of analysis should be applied to the underwriting of securitisation positions as applied to other underwritings undertaken by the credit institution.

6. Sponsor and originator credit institutions shall disclose to investors the (…) net economic interest that they maintain in the securitisation. Sponsor and originator credit institutions shall ensure that investors and prospective investors have readily available access to all materially relevant data on the (…) securitisation exposure, such as the credit quality and performance of the individual underlying exposures, or the credit quality and performance of underlying pools of exposures where these exposures are assigned to the retail exposure class, and (…) information that is necessary to conduct (…) appropriate stress tests (…). Where these requirements and those in paragraph 5 are not met, by an originator credit institution in any material respect, Article 95(1) shall not be applied by an originator credit institution which will not be allowed to exclude the securitised exposures from the calculation of its capital requirements under this Directive.

7. Paragraphs 1 to 6 (…) shall apply to securitisations issued from (…) 31 December 2010. (…) To existing securitisations where new underlying exposures are added or substituted after that date, paragraphs 1 to 6 shall apply from 31 December 2012. Competent authorities may decide to temporarily suspend the requirements referred to in paragraphs 1 and 2 during periods of general market liquidity stress.

8. Competent authorities shall disclose the following information (…):

(a) the general criteria and methodologies adopted to review the compliance with paragraphs 1 to 7 at 31 December 2010;

(…)

(b) (…) without prejudice to the provisions laid down in Chapter 1, Section 2, a summary description of the outcome of the supervisory review and description of the measures imposed in cases of non-compliance with paragraphs 1 to 6 identified on an annual basis starting from December 2011 (…).

This requirement is subject to the second subparagraph of Article 144.

9. The Committee of European Banking Supervisors (…) shall report every two years to the Commission about the application of (…) this Article, including on potential evidence of other risk transfer mechanisms and financial innovation with adverse incentives and on the implementation of paragraph 1 bis. (…)"

28. Article 129 is amended as follows:

(a) Paragraph 1 is amended as follows:

(i) Point (b) is replaced by the following:

"(b) planning and coordination of supervisory activities in going concern situations, including in relation to the activities referred to in Articles 123, 124, 136, in Chapter 5 and in Annex V, in cooperation with the competent authorities involved;

(ii) The following point (c) is added:

(c) planning and coordination of supervisory activities in cooperation with the competent authorities involved, and if necessary with central banks, in preparation of and during emergency situations, including adverse developments in credit institutions or in financial markets using, where possible, existing defined channels of communication for facilitating crisis management.

The planning and coordination of supervisory activities (…) shall include exceptional measures referred to in Article 132(3)(b), the preparation of joint assessments, the implementation of contingency plans and communication to the public."

(b) The following paragraph 3 is added:

"3. The consolidating supervisor and the competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company in a Member State shall (…) do everything within their power to reach a joint decision on the application of Articles 123 and 124 to determine the adequacy of the consolidated level of own funds held by the group with respect to its financial situation and risk profile and (…) the required level of own funds for the application of Articles 136(2) to each entity within the banking group and on a consolidated basis.

(…) The joint decision shall be reached at the very latest six months after submission by the consolidating supervisor of a report containing the risk assessment of the group in accordance with Articles 123 and 124 to the other relevant competent authorities. The joint decision shall also duly consider the risk assessments of subsidiaries performed by (…) relevant competent authorities under Articles 123 and 124 in accordance with the level of application of this directive.

(...)

The joint decision (…) shall be set out in a document containing the fully reasoned decision which shall be provided to the EU parent credit institution by the consolidating supervisor. In case of disagreement, the consolidating supervisor shall at the request of any of the other competent authorities concerned consult the Committee of European Banking Supervisors. The consolidating supervisor may consult the Committee of European Banking Supervisors on its own initiative.

In the absence of such a joint decision between the competent authorities within six months, (…) the decision on the application of Articles 123, 124 and 136(2) shall be taken on a consolidated basis by the consolidating supervisor after duly considering the risk assessment of subsidiaries performed by relevant competent authorities. The decision on the application of Articles 123, 124 and 136(2) shall be taken by the respective competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company on an individual or sub-consolidated basis in accordance with the level of application of this Directive after duly considering the views and reservations expressed by the consolidating supervisor during the six months period.

The decisions shall be set out in a document provided by the consolidating supervisor to all competent authorities concerned and to the EU parent credit institution.

Where the Committee of European Banking Supervisors has been consulted, all competent authorities shall consider such advice, and explain in their decision any significant deviation therefrom.

The joint decision referred to in the first subparagraph and the decisions referred to in the fourth subparagraph shall be recognised as determinative and applied by the competent authorities in the Member State concerned.

The joint decision referred to in the first subparagraph and the decisions referred to in the fourth subparagraph shall be updated on an annual basis or, in exceptional circumstances, where a competent authority responsible for the supervision of subsidiaries of an EU parent credit institution or, an EU parent financial holding company makes a written and fully reasoned request to the consolidating supervisor to update the decision on the application of Article 136(2). In the latter case, the update may be addressed on a bilateral basis between the consolidating supervisor and the authority making the request.

The Committee of European Banking Supervisors shall elaborate guidelines for the convergence of supervisory practices with regard to the joint decision process referred to in this paragraph and with regard to application of Articles 123, 124 and 136(2) with a view to facilitating the joint decision referred to in the first subparagraph."

29. Article 130 paragraph 1 is replaced by the following:

"1. Where an emergency situation, including adverse developments in financial markets, arises, which potentially jeopardises the stability of the financial system in any of the Member States where entities of a group have been authorised or where (…) significant branches as referred to in Article 42a are established, the consolidating supervisor shall, subject to Chapter 1, Section 2, alert as soon as is practicable, the authorities referred to in the fourth paragraph of Article 49 and in Article 50, and shall communicate all information that is essential for the pursuance of their tasks. These obligations shall apply to all competent authorities under Articles 125 and 126 and to the competent authority identified under Article 129(1).

If the authority referred to in the fourth paragraph of Article 49 becomes aware of a situation described in the first subparagraph of this paragraph, it shall alert as soon as is practicable the competent authorities referred to in Articles 125 and 126.

Where possible, the competent authority and the authority referred to in the fourth paragraph of Article 49 shall use existing defined channels of communication."

30. The following Article 131a is inserted:

"Article 131a

1. The consolidating supervisor shall establish colleges of supervisors to facilitate the exercise of the tasks referred to in Articles 129 and 130(1).

Colleges of supervisors shall provide a framework for the consolidating supervisor and the other competent authorities concerned to carry out the following tasks:

(a) exchange information <u>including with third countries' competent authorities subject to the requirements of this paragraph and compatibility with Community law</u>;

(b) agree on voluntary entrustment of tasks and <u>voluntary</u> delegation of responsibilities <u>where appropriate</u>;

(c) determine supervisory examination programmes based on a risk assessment of the group in accordance with Article 124;

(d) increase the efficiency of supervision by removing unnecessary duplication of supervisory requirements, including in relation to the information requests referred to in Articles 130(2) and 132(2);

(e) consistently apply the prudential requirements under this Directive across all entities within a banking group <u>without prejudice to the options and discretions available in Community legislation</u>;

(f) apply 129(1)(c) taking into account the work of other forums that may be established in this area.

The competent authorities participating in the college of supervisors shall cooperate closely. The confidentiality requirements under Chapter 1, Section 2 shall not prevent competent authorities from exchanging confidential information within colleges of supervisors. The establishment <u>and functioning</u> of colleges of supervisors shall not affect the rights and responsibilities of the competent authorities under this Directive.

2. The establishment and functioning of the college shall be based on written arrangements referred to in Article 131, determined after consultation with competent authorities concerned by the consolidating supervisor.

The Committee of European Banking Supervisors shall elaborate guidelines for the operational functioning of colleges, including in relation to Article 42a(3).

The competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company and the competent authorities of a host country where (…) significant branches as referred to in Article 42a are established, and third countries' competent authorities where appropriate and subject to confidentiality requirements that are equivalent, in the opinion of all competent authorities, to the requirements under Chapter 1 Section 2, may participate in colleges of supervisors.

The consolidating supervisor shall chair the meetings of the college and shall decide which competent authorities participate in a meeting or in an activity of the college. The consolidating supervisor shall keep all members of the college fully informed, in advance, of the organisation of such meetings, the main issues to be discussed and the activities to be considered. The consolidating supervisor shall also keep all the members of the college fully informed, in a timely manner, of the actions taken in those meetings or the measures carried out.

The decision of the consolidating supervisor shall take account of the relevance of the supervisory activity to be planned or coordinated for those authorities, (…) in particular the potential impact on the stability of the financial system in the Member States concerned referred to in Articles 40(3) and the obligations in 42a(2).

The consolidating supervisor, subject to the confidentiality requirements under Chapter 1, Section 2, shall inform the Committee of European Banking Supervisors of the activities of the college of supervisors, including in emergency situations, and communicate to that Committee all information that is of particular relevance for the purposes of supervisory convergence."

31. Article 132 is amended as follows:

(a) In point (d) of paragraph 1 the reference to Article 136 is replaced by the reference to Article 136(1).

(b) In point (b) of paragraph 3 the reference to Article 136 is replaced by the reference to Article 136(1).

32. Article 150 is amended as follows:

(a) Paragraph 1 is amended as follows:

(ii) Points (k) and (l) are replaced by the following:

"(k) the list and classification of off-balance sheet items in Annexes II and IV;

(l) adjustment of the provisions in Annexes III and V to XII in order to take account of developments on financial markets (in particular new financial products) or in accounting standards or requirements which take account of Community legislation, or with regard to convergence of supervisory practice; or"

(ii) the following point (m) is added:

"(m) alteration of the amount of EUR 150 million (…) specified in Article 111(1) (…)."

(b) In paragraph 2, point (c) is replaced by the following:

"(c) clarifications of exemptions provided for in Article 113;"

33. In Article 154, the following paragraphs 8 and 9 are added:

"8. Credit institutions which do not comply by 31 December 2010 with the limits set out in Article 66(1a) shall develop strategies and processes (…) on the necessary measures to resolve this situation before the dates set out in paragraph 9.

These measures shall be reviewed under Article 124.

9. Instruments that by 31 December 2010, according to national law were deemed equivalent to the items referred to in points (a), (b) and (c) of Article 57 but do not fall within point (a) of Article 57 or do not comply with the criteria set out in Article 63a, shall be deemed to fall within point (ca) of Article 57 (…) until 31 December 2040, subject to the following limitations (…):

(a) up to 20% of the sum of points (a) to (ca) of Article 57, less the sum of points (i), (j) and (k) of Article 57 between 10 and 20 years after 31 December 2010;

(b) up to 10% of the sum of points (a) to (ca) of Article 57, less the sum of points (i), (j) and (k) of Article 57 between 20 and 30 years after 31 December 2010.

The Committee of European Banking Supervisors shall monitor, until 31 December 2010, the issuance of these instruments."

33 bis. Article 156 is amended as follows:

(a) The third paragraph is replaced by the following:

"By 1 January 2012 the Commission shall review and report on the application of this Directive with particular attention to all aspects of Articles 68 to 73, 80(7), 80(8), 113(4)(c) and 129, and shall submit this report to the Parliament and the Council together with any appropriate proposals."

(b) The following paragraphs are added at the end of the Article:

"By 1 January 2011, the Commission shall review the progress made by the Committee of European Banking Supervisor towards uniform formats, frequencies and dates of reporting referred to in Article 74(2). In light of that review, the Commission shall report to the Parliament and the Council together with any appropriate proposals.

By 1 January 2012, the Commission shall report to the European Parliament and the Council on the application and effectiveness of Article 122a in the light of international market developments."

34. Annex III is amended as follows:

(a) In part 1, point 5, the following text is added:

"Under the method set out in Part 6 of this Annex (IMM), all netting sets with a single counterparty may be treated as single netting set if negative simulated market values of the individual netting sets are set to 0 in the estimation of expected exposure (EE)."

(b) In part 2, point 3 is replaced by the following:

"3. When a credit institution purchases credit derivative protection against a non-trading book exposure, or against a CCR exposure, it may compute its capital requirement for the hedged asset in accordance with Annex VIII, Part 3, points 83 to 92, or subject to the approval of the competent authorities, in accordance with Annex VII, Part 1, point 4 or Annex VII, Part 4, points 96 to 104.

In these cases, and where the option in the second sentence of point 11 in Annex II of Directive 2006/49/EC is not applied, the exposure value for CCR for these credit derivatives is set to zero.

However, an institution may choose to consistently include for the purposes of calculating capital requirements for counterparty credit risk all credit derivatives not included in the trading book and purchased as protection against a non-trading book exposure or against a CCR exposure where the credit protection is recognised under this Directive."

(c) In part 5, point 15 is replaced by the following:

"15. There is one hedging set for each issuer of a reference debt instrument that underlies a credit default swap. 'Nth to default' basket credit default swaps shall be treated as follows:

(a) the size of a risk position in a reference debt instrument in a basket underlying an 'nth to default' credit default swap is the effective notional value of the reference debt instrument, multiplied by the modified duration of the 'nth to default' derivative with respect to a change in the credit spread of the reference debt instrument;

(b) there is one hedging set for each reference debt instrument in a basket underlying a given 'nth to default' credit default swap; risk positions from different 'nth to default' credit default swaps shall not be included in the same hedging set;

(c) the CCR multiplier applicable to each hedging set created for one of the reference debt instruments of an 'nth to default' derivative is 0.3% for reference debt instruments that have a credit assessment from a recognised ECAI equivalent to credit quality step 1 to 3 and 0.6% for other debt instruments."

35. Annex V is amended as follows:

(a) Point 14 is replaced by the following:

"14. Robust strategies, policies, processes and systems shall exist for the identification, measurement, (…) management and monitoring of liquidity risk over an appropriate set of time horizons, including intra-day, so as to ensure that credit institutions maintain adequate levels of liquidity buffers. These strategies, policies, processes and systems shall be tailored to business lines, currencies and (…) entities and shall include adequate allocation mechanisms of liquidity costs, benefits and risks (…)."

(e) The following point 14a is inserted:

"14a. The strategies, policies, processes and systems referred to in point 14 shall be proportionate to the complexity, risk profile, scope of operation of the (…) credit institution and risk tolerance set by the management body and reflect the credit institution's (…) importance in each Member State, in which it carries on business. Credit institutions shall communicate risk tolerance to all relevant business lines."

(f) Point 15 is replaced by the following:

"15. Credit institutions shall develop methodologies for the identification, measurement, management and monitoring of funding positions (…). These shall include the current and projected material cash-flows in and arising from assets, liabilities, off-balance-sheet items, including contingent liabilities and the possible impact of reputational risk."

(g) The following points 16 to 22 are added:

"16. Credit institutions shall distinguish between pledged and unencumbered assets that are available at all times, in particular during emergency situations. They shall also take into account the legal entity in which assets reside, <u>the country where assets are legally recorded either in a register or in an account</u> as well as their eligibility and <u>shall monitor how assets can be mobilised in a</u> timely <u>manner</u> (<u>…</u>).

17. Credit institutions shall also have regard to existing legal, regulatory and operational limitations to potential transfers of liquidity and unencumbered assets amongst (<u>…</u>) entities, both within and outside the EEA.

18. A credit institution shall consider different liquidity risk mitigation tools, including <u>a system of limits and</u> liquidity buffers in order to be able to withstand a range of different stress events and an adequately diversified funding structure and access to funding sources. These arrangements shall be reviewed regularly.

19. Alternative scenarios on liquidity positions and on risk mitigants shall be considered and the assumptions underlying decisions concerning the funding position shall be reviewed regularly. For these purposes, alternative scenarios shall address, in particular, off-balance sheet items and other contingent liabilities, including those of SSPEs or other special purpose entities, in relation to which the credit institution acts as sponsor or provides material liquidity support.

20. Credit institutions shall consider the potential impact of institution-specific, market-wide and combined alternative scenarios. Different time horizons and varying degrees of stressed conditions shall be considered.

21. Credit institutions shall adjust their strategies, internal policies and limits on liquidity risk and develop effective contingency plans, taking into account the outcome of the alternative scenarios referred to in point 19.

22. In order to deal with liquidity crises, credit institutions shall have in place contingency plans setting out adequate strategies and proper implementation measures in order to address possible liquidity shortfalls. These plans shall be regularly tested, updated on the basis of the outcome of the alternative scenarios set out in point 19, be reported to and approved by senior management, so that internal policies and processes can be adjusted accordingly."

36. Annex XI is amended as follows:

(a) Point 1(e) is replaced by the following:

"(e) the exposure to, measurement and management of liquidity risk by the credit institutions, including the development of alternative scenario analyses, the management of risk mitigants (in particular the level, composition and quality of liquidity buffers) and effective contingency plans;

(b) The following point 1a is inserted:

"1a. For the purposes of point 1(e), the competent authorities shall regularly carry out a comprehensive assessment of the overall liquidity risk management by credit institutions and promote the development of sound internal methodologies. While conducting these reviews, the competent authorities shall have regard to the role played by credit institutions in the financial markets. The competent authorities in one Member State shall (…) duly consider the potential impact of their decisions on the stability of the financial system in all other Member States concerned."

37. Annex XII, part 2, points 3 (a) and (b) are replaced by the following:

"(a) summary information on the terms and conditions of the main features of all own funds items and components thereof, including instruments referred to in point (ca) of Article 57, instruments the statutory or contractual provisions of which provide an incentive for the credit institution to redeem them, and instruments subject to Article 154(8) and (9);

(b) the amount of the original own funds, with separate disclosure of all positive items and deductions; the overall amount of instruments referred to in point (ca) of Article 57 and instruments the statutory or contractual provisions of which provide an incentive for the credit institution to redeem them, shall also be disclosed separately; those disclosures shall each specify instruments subject to Article 154(8) and (9);

Article 2

Amendments to Directive 2006/49/EC

Directive 2006/49/EC is amended as follows:

(1) In Article 12, the first subparagraph is replaced by the following:

"'Original own funds' means the sum of points (a) to (ca), less the sum of points (i), (j) and (k) of Article 57 of Directive 2006/48/EC."

(2) Article 28 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. Institutions, except investment firms that fulfil the criteria set out in paragraph (2) or (3) of Article 20 of this Directive, shall monitor and control their large exposures in accordance with Articles 106 to 118 of Directive 2006/48/EC."

(b) Paragraph 3 is deleted.

(3) Article 30(4) is replaced by the following:

"4. By derogation from paragraph 3 competent authorities may allow assets constituting claims and other exposures on recognised third-country investment firms and recognised clearing houses and exchanges to be subject to the same treatment as laid down in Article 111(1) of Directive 2006/48/EC and in point (c) of Article 106(2) of Directive 2006/48/EC respectively."

(4) Article 31 is amended as follows:

(a) In the first paragraph, points (a) and (b) are replaced by the following:

"(a) the exposure on the non-trading book to the client or group of clients in question does not exceed the limit laid down in Article 111(1) of Directive 2006/48/EC, this limit being calculated with reference to own funds as specified in that Directive, so that the excess arises entirely on the trading book;

(b) the institution meets an additional capital requirement on the excess in respect of the limit laid down in Article 111(1) of Directive 2006/48/EC, that additional capital requirement being calculated in accordance with Annex VI to this Directive;"

(b) In the first paragraph, point (e) is replaced by the following:

"(e) institutions shall report to the competent authorities every three months all cases where the limit laid down in Article 111(1) of Directive 2006/48/EC has been exceeded during the preceding three months."

(c) The second paragraph is replaced by the following:

"In relation to point (e), in each case in which the limit has been exceeded, the amount of the excess and the name of the client concerned shall be reported."

(5) In Article 32(1), the first subparagraph is replaced by the following:

"1. The competent authorities shall establish procedures to prevent institutions from deliberately avoiding the additional capital requirements that they would otherwise incur, on exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC once those exposures have been maintained for more than 10 days, by means of temporarily transferring the exposures in question to another company, whether within the same group or not, and/or by undertaking artificial transactions to close out the exposure during the 10-day period and create a new exposure."

(5 bis) In Article 35, the following paragraph is added:

"6. Investment firms shall be covered by the uniform formats, frequencies and dates of reporting referred to in Article 74(2) of Directive 2006/48/EC."

(6) In Article 38, the following paragraph is added:

"3. Article 42a, with the exception of point 1(a) of Directive 2006/48/EC shall apply mutatis mutandis to the supervision of investment firms unless the investment firms fulfil the criteria set out in Article 20(2), 20(3) or 46(1) of this Directive."

(7) In Article 45(1) the date "31 December 2010" is replaced by "31 December 2012".

(8) In Article 48(1) the date "31 December 2010" is replaced by "31 December 2012".

Article 3

Transposition

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by (…) 31 October 2010 at the latest. (…)

   They shall apply those provisions from (…) 31 December 2010.

   When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 4

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Article 5

Addressees

This Directive is addressed to the Member States.

Done at Brussels,

For the European Parliament	*For the Council*
The President	*The President*