



## Prudential Regulation Review

May 2018

May saw the sustainable finance agenda moving up the list of priorities of the European Union (EU), with the European Commission (EC) publishing its first set of legislative proposals on sustainable finance, including the development of an EU taxonomy for climate change, environmentally and socially sustainable activities.

This note is produced for information only on a best effort basis, and does not constitute advice of any kind.

## Capital (including stress testing and macro prudential)

The European Banking Authority (EBA) published the [results of its 2016 Credit Valuation Adjustment \(CVA\) risk monitoring exercise](#), which assessed the impact on own funds requirements of the reintegration of transactions currently exempted from the scope of the CVA risk charge under the CRR. The exercise found that the median bank would see its current CVA risk charge multiplied by 3.06 when reintegrating exempted transactions.

The EBA announced that, by summer 2019, it will provide technical advice and policy recommendations on the [implementation of Basel 3](#) in order to support the Commission in drafting a "CRD6/CRR3" legislative proposal. The EBA further plans to launch an EU-wide bank data collection exercise in July to inform this work.

The European Commission (EC) consulted on a proposal for a regulation on [sovereign bond-backed securities](#) (SBBSSs). SBBSSs are proposed new financial instruments backed by pools of Eurozone government bonds, which the EC hopes will help to diversify sovereign portfolios and reduce risks in the EU banking sector. The proposal seeks to remove regulatory obstacles in the development of SBBSSs.

The EC welcomed the general approach reached by the Council on the [risk reduction package \(CRD V/CRR II\)](#). The package will implement international standards into EU law while taking European specificities into account. EC Vice-President Dombrovskis, speaking at an ECOFIN press conference, noted several [key components of the package, including the 3% binding leverage ratio and the Net Stable Funding Ratio \(NSFR\)](#), and called upon the European Parliament to define its negotiating position as soon as possible.

The Basel Committee on Banking Supervision (BCBS) and the International Organisation of Securities Commissions (IOSCO) published the [criteria for identifying short-term "simple, transparent and comparable" \(STC\) securitisations](#), and in conjunction, also issued a [standard setting out their capital treatment](#). The BCBS and IOSCO publication extended the scope of the STC criteria to short-term securitisations, particularly exposures related to asset-backed commercial paper conduits, and also set out amendments to the previous short-term STC criteria. The standard included new guidance on the short-term STC criteria around initial and ongoing data, full support for investors, redemption cash flow, and documentation disclosure and legal review.

## Crisis management (including special resolution, systemically important firms, and business continuity)

The EBA and ESMA issued a joint statement on the treatment of [retail holdings of liabilities eligible for bail-in](#). The statement found that there may be significant consumer protection issues relating to the sale of liabilities eligible for bail-in to retail investors. It further found that retail holdings of liabilities eligible for bail-in may be an impediment to resolvability.

## Rethinking the domestic and international architecture for regulation

Ignazio Angeloni, Member of the Supervisory Board of the ECB, spoke on the [strategic direction of the Single Supervisory Mechanism \(SSM\)](#). He explained that, in the future, the ECB will seek to enhance the quality of supervision further; strengthen its focus on market risks and macroprudential linkages; and further develop crisis management and prevention frameworks.

Yves Mersch, Member of the Executive Board of the ECB, delivered a speech noting that [ring-fencing measures may be needed to safeguard financial markets, firms, investors and consumers from the risks posed by virtual currencies \(VC\)](#). He highlighted four areas that will require particular attention from the regulators, including VCs themselves; VC exchanges and wallet providers; financial market infrastructures; and the banking sector.

## Disclosure, valuation and accounting

The EC published its first set of legislative proposals targeting [sustainable finance](#), which included a [proposal](#) on a unified EU classification system for determining whether an economic activity is environmentally-sustainable; a [proposal](#) amending the EU Benchmark Regulation to create low-carbon benchmarks and positive-carbon impact benchmarks; a [proposal](#) for a regulation on disclosures relating sustainable investments and sustainability risks; and [amendments to MiFID II](#) and [amendments to IDD](#) to assess how best to include environmental, social and governance considerations into financial advice. The proposals set out that firms offering financial products as environmentally sustainable and financial advice for environmentally sustainable products will have to disclose information on how, and to what extent, the criteria set out by the EU are used to determine their environmental sustainability.

Danièle Nouy, Chair of the Supervisory Board of the ECB, [wrote](#) to Marco Zanni, Member of the European Parliament (MEP) about non-performing loans and Level 3 assets. She stated that the ECB has intensified its review of [banks' valuation and classification approaches](#) and will continue to focus on the effectiveness and reliability of banks' control processes, such as classification under the fair value hierarchy.

## Central Bank of Ireland

Sharon Donnery, Deputy Governor, Central Banking, has argued that the case in favour of [setting a positive Countercyclical Capital Buffer](#) (CCyB) sufficiently early in the economic cycle, to build in resilience and mitigate pro-cyclicality in a downturn, is compelling. The Deputy Governor was speaking at Maynooth University where she lectured in economics before joining the Central Bank of Ireland.

An Economic Letter examines [the ratio of new mortgage lending to household disposable income](#) for the purpose of monitoring cyclical systemic risk in the residential real estate lending market in Ireland.

An Economic Letter examines [the effects of European Central Bank \(ECB\) policy announcements on sovereign yields in pre-crisis, crisis and post-crisis periods](#). The paper measures ECB policy changes by movements in market expectations and the analysis focuses on Germany, France, Italy and Spain.

An Economic Letter considers whether the [toolbox currently in use at central banks might not prove sufficient to deal with another severe depression if long-run real interest rates remain at their current low levels](#), limiting the room available to cut short-term rates in the future. The research compares different monetary policy regimes according to how strongly they stimulate the economy during recessions, when policy rates could be constrained by the zero lower bound.

## Other

Sabine Lautenschläger, Member of the Executive Board of the ECB and Vice-Chair of the Supervisory Board of the ECB, indicated her belief that [macroprudential policy, rather than monetary policy, is a better tool to address financial stability concerns](#), and that monetary policy should be focused on ensuring price stability.

# Contact Us

Our firm's website, [www.deloitte.ie](http://www.deloitte.ie) provides world-leading continuously updated information source on international and local topics such as [Risk Advisory](#).

For more details on the above please contact your client service partner or our Irish Risk Advisory contacts:

**Sean Smith**  
Partner – Regulatory Risk  
T: +353 1 417 2306  
E: [seansmith1@deloitte.ie](mailto:seansmith1@deloitte.ie)

**John Kernan**  
Director – Regulatory Risk  
T: +353 1 417 8983  
E: [jkernan@deloitte.ie](mailto:jkernan@deloitte.ie)

**Olumuyiwa John Farayibi**  
Manager – Regulatory Risk  
T: +353 1 417 3096  
E: [ofarayibi@deloitte.ie](mailto:ofarayibi@deloitte.ie)

**Senan Ryan**  
Consultant - Regulatory Risk  
T: +353 1 417 8630  
E: [senryan@deloitte.ie](mailto:senryan@deloitte.ie)

# Deloitte.

Deloitte refers to one or more of Deloitte Touche Tohmatsu Limited, a UK private company limited by guarantee ("DTTL"), its network of member firms, and their related entities. DTTL and each of its member firms are legally separate and independent entities. DTTL (also referred to as "Deloitte Global") does not provide services to clients. Please see [www.deloitte.com/about](http://www.deloitte.com/about) for a more detailed description of DTTL and its member firms.

At Deloitte, we make an impact that matters for our clients, our people, our profession, and in the wider society by delivering the solutions and insights they need to address their most complex business challenges. As one of the largest global professional services and consulting networks, with over 220,000 professionals in more than 150 countries, we bring world-class capabilities and high-quality services to our clients. In Ireland, Deloitte has over 2,000 people providing audit, tax, consulting, and corporate finance services to public and private clients spanning multiple industries. Our people have the leadership capabilities, experience, and insight to collaborate with clients so they can move forward with confidence.

This communication contains general information only, and none of Deloitte Touche Tohmatsu Limited, its member firms, or their related entities (collectively, the "Deloitte Network") is, by means of this communication, rendering professional advice or services. Before making any decision or taking any action that may affect your finances or your business, you should consult a qualified professional adviser. No entity in the Deloitte Network shall be responsible for any loss whatsoever sustained by any person who relies on this communication.

**CENTRE for**  
**REGULATORY**  
**STRATEGY**  
**EMEA**