European Parliament

CRR/CRD: The delegated act on the date of application of the own funds requirements for market risk

ECON Scrutiny Session of 23 September 2024

This briefing has been prepared to support **ECON's work on scrutiny** of delegated acts, in particular the discussion of **23 September 2024** on the Commission Delegated Regulation with regard to the date of application of the own funds requirements for market risk.

In brief

The **CRR 3/CRD 6 package** constitutes the final phase in the implementation of the internationally agreed finalised Basel 3 prudential requirements for banks into the EU financial services acquis. In particular, the CRR 3 introduces the revised market risk requirements as binding own fund requirements. These requirements were introduced in the CRR 2 only as reporting requirements[1]. However, at the time of the adoption of the CRR 3 it was not clear how and whether other major jurisdictions will apply the finalised market risk framework. Therefore, co-legislators mandated the Commission to monitor possible differences in the international implementation of the market risk framework and, in case of 'significant differences', empowered the Commission to postpone the application of the capital requirements for market risk for up to two years or to introduce temporary amendments to CRR 3 market risk requirements in the form of capital multipliers or targeted operational relief measures (Art. 461a CRR). On 24 July 2024, the Commission adopted a delegated act (DA) postponing the date of application of the market risk framework by one year to 1 January 2026.

[1] On details and further background of the first phase of the EU implementation of the market risk framework see also Scrutiny Papers PE 630.246 of February 2020.

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ITEM FOR DISCUSSION

COMMISSION DELEGATED REGULATION (EU) …/... amending Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to the date of application of the own funds requirements for market risk[2]

Background

EU Implementation: Two phase implementation of the revised international market risk standards

In the European Union, co-legislators opted for an implementation of the revised international standards for marked risk, the so-called **Fundamental Review of the Trading Book** (FRTB), in a two phase approach. In the first phase, the **CRR 2** introduced the revised market risk standards as a **reporting requirement only**. In the second phase, the **CRR 3** (Regulation (EU) 2024/1623) introduces the new Basel standards for market risk also as **binding own fund requirements**. These will become **applicable on 1 January 2025**.

Empowerment to Commission to adopt DA

In **Article 461a CRR** as amended by the CRR, 3 co-legislators task the Commission with monitoring '*the differences between the implementation of international standards on own funds requirements for market risk in the Union and in third countries, including as regards the impact of the rules in terms of own funds requirements and as regards their date of application'* (Art. 461a(1) CRR).

In case '*significant differences in such implementation are observed the Commission shall be empowered to adopt* ***delegated acts*** in *accordance with Article 462 to* ***amend*** *this Regulation* [CRR] *by postponing* '***for up to two years*** *the date from which institutions shall apply the own funds requirements for market risk set out in Part Three, Title IV, or any of the approaches to calculate the own funds requirements for market risk referred to in Article 325(1)'*(Art. 461a(2)(b) CRR).

The Commission is also empowered to apply *'[...] for up to three years, where necessary to preserve a level playing field and to offset those observed differences, targeted operational relief measures or targeted multipliers equal to or greater than 0 and lower than 1 in the calculation of the institutions' own funds requirements for market risk […].'* (Art. 461a(2)(a) CRR).

Commission Delegated Regulation postponing date of application

On 24 July 2024, the European Commission adopted a Delegated Act in accordance with Article 461a CRR, postponing the date of application of the second implementation stage by one year to **1 January 2026**.

This DA **amends** the CRR by introducing a **new Article 520a** stipulating that (i) the **own funds requirements for markets risk** (Part Three, Title IV: Arts. 325 to 377) and (ii) market risk **reporting requirements** (Arts. 430, 430b) and (iii) market risk **disclosure requirements** (Arts. 445 and 455) should be continued to be applied in the CRR version in force on 8 July 2024.

Commission reasoning for postponement

According to the Commission the postponement is necessary because of *'[...] delays in the implementation of the Basel III standards by major jurisdictions [...]'* in order *'[...] to preserve a level playing field with third countries in terms of own funds requirements [...].'*[3] In the explanatory memorandum to the DA the Commission stipulates in particular that the *'[...] monitoring of the FRTB's implementation across jurisdictions shows that, while some jurisdictions have recently implemented the standards (Canada and Japan for example), other jurisdictions, for which level playing field considerations are very relevant, are lagging behind and significant uncertainty remains about the timelines and possible deviations in implementation in those jurisdictions. Most significantly, as of June 2024, the US has not yet implemented the FRTB standards or been sufficiently clear about when or how it would be ready to do so. The Commission's assessment is that given the current regulatory developments in the US, the Basel standard will likely not be implemented by US agencies*

[2] Commission Delegated Regulation (EU) …/... of 24.7.2024 amending Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to the date of application of the own funds requirements for market risk, C(2024)5139.
[3] See summary in DA Register.

before 2026. As a result, the European Commission considers it necessary, in order to preserve a level playing field with third countries in terms of own funds requirements and the impact of those requirements, to use the co-legislators' empowerment and postpone by a year the application of the FRTB standards.'

Commission addresses operational issues

The publication of the Delegated Act was accompanied by a set of **Questions and Answers**[4]. These Q&As also clarify some related operational and technical details, '*so that banks and supervisors have a consistent approach to the implementation of the requirements.*' These details address inter alia methodologies to be used for the calculation of the own funds requirements for market risks, the ramifications of the postponement on the disclosure requirements, the procedure to follow for the calculation of the output floor, capital requirements for credit valuation adjustment (CVA) risk; and profit and loss attribution test (PLAT).

Concerning the trading book/non-trading book boundary requirements, the Commission referred to additional EBA guidance.

European Banking Authority (EBA) Response to the Delegated Act

On 12 August 2024 the European Banking Authority (EBA) published its response[5] to the Commission Delegated Act. This response consists of (i) an EBA Opinion[6] in the form of a 'no-action letter' and further technical clarifications in the form of (ii) EBA considerations[7].

EBA Opinion - no-action letter

EBA summarised in its press statement the opinion as follows: *'In the no-action letter, the EBA recommends that competent authorities should not prioritise any supervisory or enforcement action in relation to the amendments to the provisions setting the boundary between the banking and trading books, or those defining internal risk transfers between books.'* The EBA also clarified *'that the points it made in another no-action letter on the same topic issued in 2023 should remain applicable.*

The EBA is of the opinion that the front-loaded application of the revised provisions on the boundary and internal risk transfers, compared to the rest of the FRTB framework, which is not yet implemented in the Union for capital purposes, would subject institutions to an operationally complex, fragmented and costly two-step implementation. In addition, there are no jurisdictions at the global level that envisage such a two-step implementation of the FRTB framework. This means that a front-loaded application of the boundary provisions would lead to global institutions being subject to very different regulatory requirements depending on where the risk management is performed, thus resulting in a fragmentation of the regulatory framework.'[8]

Background - Legal Basis of EBA Opinion: The EBA Opinion in form a no-action letter is based on Art. 9c of the EBA Regulation[9].

EBA considerations - making the postponement operational

According to the same EBA press statement: '*The EBA also shares some considerations on a set of technical questions and implementation issues arising from the postponement, that were deemed material and relevant with a view to achieving a harmonised implementation of the market risk framework across institutions during the postponement period. [...]*'.

[4] Question and Answers, Banking Package: Moving Forward with the implementation of the Basel Standards, while preserving the international level playing field. Link here.
[5] See EBA Press Release of 12 August 2024, Link: here.
[6] Opinion of the European Banking Authority on the application of the provisions relating to the boundary between trading book and banking book, and on the internal risk transfer between books as referred to Article 1, points (34), (35) and (38) of Regulation (EU) No 2024/1623: EBA/Op/2024/05.
[7] EBA consideration on the postponement of the application of the FRTB in the EU.
[8] EBA Press Release of 12 August 2024.
[9] Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010. Link here.

SSM - Statement by the Chair of Supervisory Board of the ECB

Asked during a public hearing in ECON on 2 September 2024 on the supervisory perspective of this postponement, the Chair of the Supervisory Board of the ECB replied the following: *'[...] So in that spirit I would also answer your question on the FRTB. So I thought it would have also been a good decision to keep it within the package, not to isolate it. I know that for political reasons that decision has been taken, but I don't think that's my reading. It wasn't absolutely necessary to delay this. Banks compete on many different grounds. There are many factors that have an impact on how present banks are in certain markets, and this is one element of it. I'm not sure that the European banks would have significantly lost ground on markets, in any case not affecting that many banks – that they wouldn't have lost that much ground vis-à-vis their international competitors. There's just a broader spectrum of things that needs to be taken into account. So again, implementation, what has been agreed, there's been a lot of discussion. I think that for me would be the best way forward.'*[10]

Basel Implementation in major jurisdictions - State of play

UK - Basel 3.1 standards - implementation date moved to 1 January 2026 and four year transitional[11]: The Prudential Regulation Authority (PRA) published in November 2022 its proposed rules for implementing the finalised Basel III framework (Basel 3.1 standards) for consultation. The consultation period ended on 31 March 2023. On 12 September, the PRA published its 'near-final' standards. At the same time the PRA updated the implementation timeline: *'To support a smooth implementation of the package and having considered feedback from the consultation as well as the implementation timelines of other jurisdictions, the PRA has decided to move the implementation date for the Basel 3.1 standards by a further six months to 1 January 2026 with a four-year transitional period ending on 31 December 2029.'*[12][13]

US - '**Basel III endgame proposal':** The implementation of the finalised Basel 3 rules are also called in the US 'Basel 3 endgame'. On 27 July 2023, the three bank regulatory agencies in the US, the Board of Governors of the Federal Reserve System (**Fed**), the Federal Deposit Insurance Corporation (**FDIC**) and the Office of the Comptroller of the Currency (**OCC**) published their proposed rules[14] and requested comments.[15] These proposed rules triggered strong opposition by the banks concerned. In a speech given on 10 September 2024, the Fed Vice-Chair of Supervision outlined that the US agencies' recent work on the comments received during the consultation period led them to conclude that *'broad and material changes to the proposals are warranted'*. He also mentioned several potential elements of a '**re-proposal'**.[16]

Procedural Issues

Under Article 290 TFEU, the Parliament may object to the above mentioned delegated act, but cannot amend it. The Commission has informed Parliament that the deadline for objections by Parliament and Council is three months from the date of notification, i.e. until **24 October 2024**. In accordance with Article 462(6) CRR, the scrutiny deadline may be extended once by another three months. If the ECON Committee considers it appropriate, it may table a reasoned motion for a resolution to plenary objecting to the delegated act within the scrutiny period, stating the reasons for Parliament's objections to the above-mentioned delegated act and possibly incorporating a request to the Commission to submit a new delegated act taking into account Parliament's recommendations (Rule 114(3) of the Rules of Procedure).

[10] Public Hearing with Claudia Buch, Chair of the Supervisory Board of the European Central bank, Monday, 02 September 2024. Link here.
[11] BoE, News Release, 27 September 2023: Timings of implementation. Link here.
[12] BoE, News Release, 12 September 2024: The PRA publishes the second policy statement on Basel 3.1 and proposals on the strong and simple capital regime for smaller firms. Link: here.
[13] The four-year transitional period concerns only the phasing-in of the output floor and has an impact only to banks that use internal models, in part or in full. Banks fully under standardised approach do not benefit from the four-year transitional period.
[14] On the content of the proposal see official Fact Sheet on the proposed rules: Link here.
[15] Board of Governors of the Federal Reserve System, Joint Press Release, 27 July 2023: Agencies request comment on proposed rules to strengthen capital requirements for large banks. Link here.
[16] Speech, September 10, 2024, The Next Steps on Capital, Vice Chair for Supervision Michael S. Barr, At the Brookings Institution, Washington, D.C.; link: here.

State of play: The DA, as adopted by the Commission, is currently under scrutiny by the European Parliament and the Council.

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