

Key issues in Banking Regulation

Key issues in Banking Regulation

1. At the European level
2. At the Basel level
3. On resolution issues

Main proposals

- Better coordination and streamlining of reporting
- New powers for ESMA on audit and accounting
- Power for EIOPA on model approval
- Power for EBA on own funds issuances approval
- Power for ESMA on CCPs
- More independence for the ESAs
- Merger of EBA/EIOPA
- Power for ESMA on consumer protection
- Funding of ESAs by the industry

ACPR largely in disagreement

European implementation of Basel 3

- Implementation of NSFR
- Leverage ratio
- Fundamental review of the trading book (FRTB)
- Interest rate risk in the banking book (IRRBB) in Pillar 2

European specificities

- Exemptions (« waivers ») at solo level
- EU parent holding undertaking
- Pillar 2 (P2R / P2G)

ACPR largely in agreement

Finalizing Basel 3 to give regulatory clarity

Main question: which **role for internal model** in the regulation?



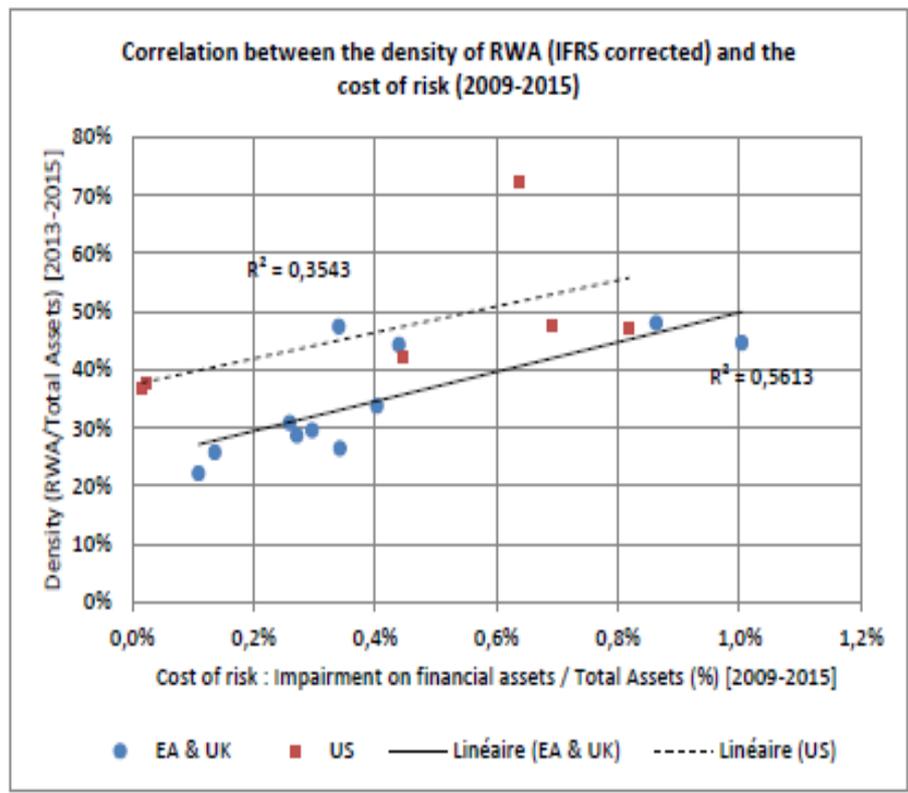
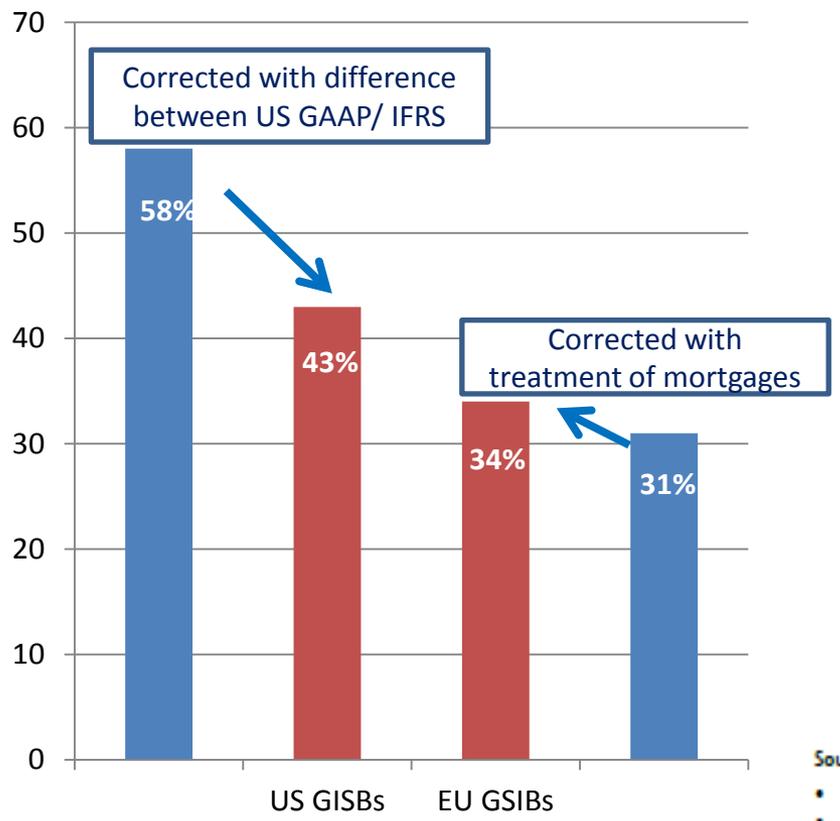
Objective for finalizing Basel 3: restore confidence in risk measurement by banks

In practice, finalizing Basel 3:

- **Credit risk measurement:** revised standardized approach and limitation to the use of internal model
- **Operational risk measurement:** review all the framework (new standardized approach and end of advanced method)
- Introduce an overall floor (**capital output floor**) between the internal model and the standardized approach
- Introduce a specific **leverage requirement for systemic banks (G-SIBs)**, in addition to the 3 % Tier 1.

Variability is in question but has good explanations

Risk Weighted Assets/Total balance sheet (end June 2016)



Sources: The raw data comes from:

- FDIC Global Capital Index for the Total Assets (TA) and the Total RWA.
- SNL for the Cost of Risk (Impairment on Financial Assets over Total Assets) for the year 2009-2013

Need not to underestimate main issues

Variability may have multiple causes:

- Banks' business models
- Composition of portfolios
- Risk management (very different share and types of exposures kept in banks' balance sheets and securitized respectively)



Work is needed to clarify expectations in terms of supervision and validation of internal models

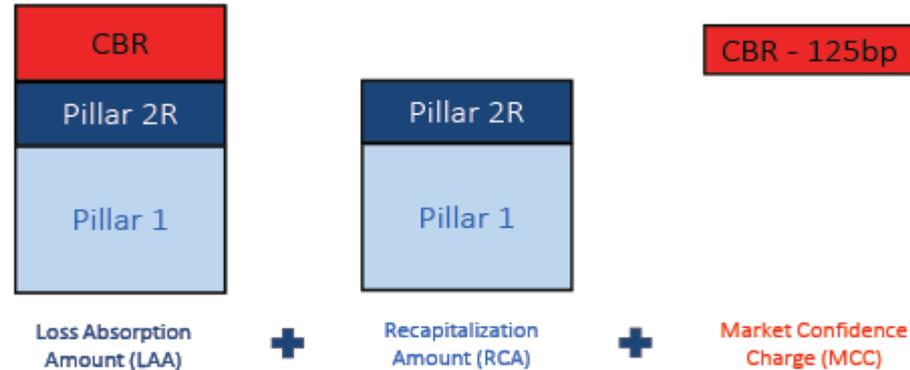
Our proposals

- Developing guidelines regarding the validation of internal models
- Full control of portfolios for which a bank may apply to use the A-IRB or F-IRB
- More transparent and standardized back testing tools should be put in place by banks
- Annual benchmarking exercises should be performed on internal models with peer reviews
- Complete and regular credit-risk-focused stress-testing exercises should be performed by supervisory authorities
- An output floor could thus be considered as only an optional measure

The Single Resolution Board (SRB) is considering informative MREL targets

- "Industry dialogue of 28th November 2016 " on the new indicative MREL target based on the MREL delegated act (EBA RTS) and taking into account the new SREP methodology for 2016 (but not the revised regulation)

- Informative MREL Targets in 2016 = Mechanical sum of three amounts



- Possible changes to take into account the proposed EU changing rules
 - distinction between MREL Requirement and MREL Guidance
 - possible adjustments to be made by the resolution authority, with the supervisory authority, to take into account the business model and the risk profile

The Commission's legislative proposal to implement TLAC in the EU ("BRRD2")

1. MREL remains in principle required for each individual institution.
2. Internal MREL would be required and could be constituted of 50% of collateralized guarantees.
3. Can be fully waived but under strict conditions, including that both the resolution entity and the subsidiary be subject to « supervision by the same Member State » (?). No Single Market perspective as in the EBA Report? Not even a reference to the Banking Union?
4. The resolution authority may impose more stringent requirements.

❑ **A fast-track revision of article 108 BRRD on creditor hierarchy, in order to harmonize creditor hierarchy across Europe.**