Mr Valdis Dombrovskis
Vice-President for the Euro and Social Dialogue
Commissioner for Financial Stability, Financial Services
and Capital Markets Union
European Commission
Rue de la Loi 200
1049 Bruxelles
Belgique

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Subject: Removal of the FRTB from the proposal of revision of the Regulation (EU) n°575/2013 and a reconsideration of the NSFR

Dear Vice-President Dombrovskis,

I would like to draw your attention to 2 elements of the proposal amending Regulation (EU) N°575/2013, published on 23 November 2016. The Risk Reduction Measures (RRM) package aspires to reduce financial risks and to consider accurately the specificities of the European economy. Also, it intends to implement a more sensitive and risk based approach. The EBF strongly supports this initiative.

A first element is **the market risk framework** which **should be applied in all jurisdictions at the same time:**

We note that the RRM proposal plans to revise the requirements for market risk. This proposal was, in our opinion, premature since the Basel agreement has not yet been finalised. Moreover, recent developments have significantly changed the situation and call into question the timeliness of the current Commission proposal on market risk:

- First, the Basel standard on market risk (BCBS 352)[1]) would lead, if not amended, to significant increases and potential instability in capital requirements as notably evidenced by the latest "Basel III Monitoring Report"[2]: The capital requirements due to the new market risk Basel methodology would already increase between 67.2% and 87.4% compared with the current approach with the optimistic assumption that all desks pass the Profit and Loss Attribution Test (PLAT) and include the Non-Modellable Risk Factor (NMRF) and remain in internal models. Industry simulations, assuming some desks fail and are switched to standard approach, provide an even much higher impact. The work re-opened by the Basel Committee aims at addressing the PLAT and NMRF. Even if those issues are satisfactorily addressed, the FRTB will still lead to a substantial capital increase, contrary to the original mandate, and at the expense of the much needed development of EU capital markets.

1 http://www.bis.org/bcbs/publ/d352.pdf
2 http://www.bis.org/bcbs/publ/d397.pdf

European Banking Federation aisbl

Brussels / Avenue des Arts 56, 1000 Brussels, Belgium / +32 2 508 3711 / info@ebf.eu
Frankfurt / Weißfrauenstraße 12-16, 60311 Frankfurt, Germany
EU Transparency Register / ID number: 4722660838-23

www.ebf.eu

- Second, the Basel Committee launched a consultation on the implementation of a "Simplified alternative to the market risk standardised approach" (BCBS 408)[3] on 29 June 2017. This new approach, applicable to small trading books, is under consultation until 27 September.

- Lastly, we would like to underline that several jurisdictions, including the United States of America, indicated either not to implement the new market risk requirements at this time or called on regulators to delay domestic implementation of the FRTB until it can be properly calibrated and assessed. As such, the "Report on Core Principles for Regulating the United States Financial System"[4] delivered by the Secretary Steven T. Mnuchin in June 2017, supports the postponement of the new requirements applicable to market risk.

If we support the principle of the revision of the current market risk framework and the introduction of more risk sensitive approaches, it is essential that this new framework is reliable, stable and compatible with the objectives of the Capital Market Union. Furthermore, **it is vital for European banks and the development of market-based financing for the European economy that Europe has the reassurance that this framework will be applied in all jurisdictions at the same time.**

A second element **to reconsider** is **the Net Stable Funding Ratio for Europe**

We would like to recall that the "Report on Core Principles for Regulating the United States Financial System"[4] delivered by the Secretary Steven T. Mnuchin also proposes to consider an adjournment of the implementation of the NSFR in the U.S. The industry is concerned about the economic impact of the Net Stable Funding Ratio (NSFR) on capital market activities, on interbank financing, as well as on end-users, due to the fact that additional costs are generally passed on to the customers.

For instance, the asymmetry applied by the NSFR between repos and reverse-repos, even when financial transactions are concluded between credit institutions, would adversely impact the liquidity of capital markets, at a time when the ECB is reconsidering its quantitative easing policy. This has recently been highlighted by the Basel Committee on the Global Financial system (CGFS) in their repo market functioning paper (N°59): "NSFR could potentially have negative implications for repo market functioning", not all intended by regulation. The CGFS is still looking for alternative measures within regulation to mitigate those impacts, which suggests that it would be premature to deploy the current Basel NSFR within Europe.

It is also important to note that on the subject of the NSFR, the Basel Committee has also decided to reopen the issue of the treatment of derivatives to address the remaining weaknesses which have been identified.

We note further that for the NSFR to be a meaningful measure for the diverse banking structures that exist in Europe it should reflect the way each banking group manages its liquidity and as such should be fulfilled on a consolidated or individual basis, accordingly to each banking group's liquidity structure. For those banking groups that manage their liquidity and funding requirements on an individual basis it is more meaningful for the NSFR to be estimated on a solo basis. However, for banking groups with a centralised liquidity management model the envisaged solo application of the NSFR creates an uneven

3 http://www.bis.org/bcbs/publ/d408.pdf
4 https://www.treasury.gov/press-center/news/Pages/Summary-of-Recommendations-for-Regulatory-Reform.aspx

playing field with other jurisdictions and should thus be reconsidered. The application of the requirement at the individual level in the EU context for banking groups that administer their liquidity in a centralised manner is overly strict considering that in the case of a lack of stable resources at the level of an entity of the group, the one-year time horizon of the NSFR would be sufficient to restore the situation through intragroup transactions. Therefore, we recommend that the European Institutions consider an application of the NSFR requirement at a consolidated level for banking groups with a centralised liquidity management model.

Finally, EU policy makers should be mindful of European specificities such as the predominance of funding via covered bonds in the absence of alternative long term funding models. The European NSFR should not disincentivise covered bond structures and other forms of covered long-term funding.

Given the current perfunctory commitment by other jurisdictions and the lack of an internationally agreed methodology for these two reforms there is a significant risk that European banks, and the economy they support, will face an **uneven playing field vis-à-vis its international competition.**

Thus, the EBF calls the European Commission for the modification of the scope of the revision of the Regulation (EU) n°575/2013 by **putting on hold the new requirements for the trading Book (FRTB)** and by **reconsidering the transposition of the Net Stable Funding Ratio (NSFR)** - at least with regard to the treatment of repos and reverse repos, derivatives, covered bonds and the application of the NSFR at the group level or solo level - **until a final agreement has been reached by the BCBS and all relevant jurisdictions have confirmed their commitment to implement**.

The EBF looks forward to your consideration and response on the above proposals and stands ready to elaborate further in the framework of a dedicated meeting if necessary.

I am sure these circumstances will be carefully evaluated by your services and hope to continue our constructive dialogue and fruitful cooperation going forward.

Yours sincerely,

Wim Mijs
Chief Executive Officer