EUROPEAN COMMISSION
Directorate General Financial Stability, Financial Services and Capital Markets Union

Director General

Brussels,
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Mr. Jóse Manuel CAMPA
Chairperson
European Banking Authority
France

Sent by e-mail

Subject: Call for Advice to the EBA on the final elements of the Basel III framework

Dear Mr. Campa,

As part of the preparatory work for the implementation of the final Basel III reforms, on 4 May 2018 the Commission services sought technical advice from the European Banking Authority (EBA) on the potential impact of these reforms on the EU banking sector and the wider EU economy, and on possible implementation challenges which would arise for institutions established in the EU. The EBA was furthermore asked to opine on whether, looking at the EU banking sector as a whole, any significant shifts to or from certain types of activities, exposures, business lines or business models would be expected following the introduction of any of the reforms.

I understand the EBA is currently finalising its advice on the final Basel III reforms in the area of credit risk, operational risk, output floor, and securities financing transactions whereas the response concerning the reforms related to market risk and credit valuation adjustment risk is expected to follow at end of September this year, owing to the later completion of these elements of the Basel III framework.

I would like to thank you and your staff for all your efforts to prepare a truly comprehensive analysis of the revised Basel standards. Nevertheless, as my services already indicated at different occasions, there are still a few areas where further work is considered necessary to inform our decision-making. This work could be undertaken after the publication of the first advice, and ideally be delivered as part of the second advice. In particular, I consider that further analysis is needed on the following issues:

- **Quantitative assessment of the impacts resulting from the application of the output floor at all levels**. According to your analysis, which mainly relies on consolidated level data, the output floor is going to be the main driver behind the capital impacts of the Basel III reforms. While the draft advice highlights that applying the floor at each level may lead to higher overall requirements, depending on the group structures, and to notable impacts on subsidiaries with specific business models, the potential impacts have not been comprehensively assessed. As more light on this aspect is crucial to inform decision-making, I reiterate our earlier request –

echoed by major supervisors – for complementing the quantitative assessment with impact estimates at the sub-consolidated and individual levels, taking into account the particular data quality and resource constraints you may face.

- **Additional analysis to increase risk sensitivity in the equity exposure class**. The Basel III revisions in this area are one of the biggest drivers behind the increase in capital requirements for credit risk – and this without taking into account likely further increases for intra-group exposures. Yet, the current analysis falls short of assessing the impact on intra-group equity exposures nor does it explore possible ways to increase the risk sensitivity of the framework, as requested in our CfA. I would therefore invite you to analyse the consequences of the increased risk weights on existing group structures and business models and to provide recommendations on how to enhance risk sensitivity in this area.

- **Additional analysis to increase the risk sensitivity for specialised lending**. Capital requirements would appear to increase significantly in this area but there is no good understanding whether this is actually warranted from a risk perspective. More concretely, I would invite the EBA to carry out a more granular analysis that considers possible criteria for differentiating between different qualities of specialised lending exposures, and that reviews the appropriateness of the input floors provided by the Basel III standards for own-estimated loss given default.

- **Estimation of TLAC/MREL shortfalls**. I finally reiterate our request in the CfA for an estimation of the potential TLAC/MREL shortfalls that the changes to the calculation of risk-weighted assets (RWAs) would trigger – this as an essential element to have the full picture of the impact of the reform package. I understand that the EBA will soon publish a report on MREL, which should provide for sufficiently reliable data to discuss the impact of the increase in RWAs expected to result from the final Basel III standards on banks' capability to meet their TLAC/MREL requirements.

I cannot stress enough the importance of the abovementioned analysis. My services stand ready to support the EBA in completing the technical advice as efficiently as possible – please do not hesitate to contact the Head of Unit D1, Nathalie Berger, to this effect. The invaluable input from the EBA will be instrumental in informing the Commission's decision.

Thank you in advance for your cooperation and I look forward to receiving the EBA's advice.

Yours sincerely,

Olivier GUERSENT