Pan-European Conglomerate Club *29/09/2016*

RESPONSE TO CONSULTATION DOCUMENT “EBA GUIDELINES ON DISCLOSURE REQUIREMENTS UNDER PART EIGHT OF REGULATION (EU) 575/2013

Our comment will focus the following major issue which refers to page 27 section c. “Non-deducted insurance participations” and pages 86-87.

The EBA’s consultation paper proposes that financial conglomerates benefiting from an exemption decision under Article 49(1) of the CRR disclose (the “New Disclosure Requirements”):

(i) the amount of holdings of own funds not deducted as a consequence of using the option provided under Article 49(1) (the “Carrying Amount”); and

(ii) the total risk weighted exposure amounts associated with those exposures (the “RWA Amount”).

Pursuant to Article 49(1) of the CRR, for the purposes of calculating own funds, competent authorities may, under certain conditions, permit credit institutions to not deduct from their own funds the holdings of own fund instruments issued by insurance companies in which they have a significant investment, but instead risk-weight them. Such permission is given pursuant to a specific exemption decision (an “Exemption Decision”). National competent authorities have granted Exemption Decisions to several conglomerates, the validity of which has been recently reaffirmed by the ECB.

The legal grounds on which the EBA is proposing the New Disclosure Requirements are paragraphs (c) and (d) of Article 438 of the CRR: “*The disclosures in accordance with Template EU INS 1 are to be provided as part of the information on capital requirements from article 438(c) and (d), since non-deducted insurance participations are then risk-weighted in accordance with the CRR credit risk framework.*”

The proposed New Disclosure Requirement of the Carrying Amount raises serious legal concerns.

- **By requiring the disclosure of the Carrying Amount, the EBA would exceed the powers granted to it under Regulation (EU) No 1093/2010.**

According to Regulation (EU) No. 1093/2010, the EBA shall contribute to the consistent, efficient and effective application of the EU legislative acts referred to in Article 1 paragraph 2, which include the CRR, and to foster supervisory convergence. Pursuant to Article 1 paragraph 3 of the Regulation (EU) No 1093/2010, the EBA may also act in relation to issues not directly covered in the above-mentioned EU legislative acts including matters of financial reporting “*provided that such actions by the Authority are necessary to ensure the effective and consistent application of those acts.*”

Under Article 16 of the Regulation, the EBA “*shall, with a view to establishing consistent, efficient and effective supervisory practices within the ESFS, and to ensuring the common, uniform and consistent application of Union law, issue guidelines and recommendations addressed to competent authorities or financial institutions.*”

Consequently, the EBA explains that the objective of the draft Guidelines is “*to specify guidance and formats for disclosure requirements from Part Eight CRR in areas where these requirements have not already been specified by Regulations or other Guidelines listed* [in pp. 8 and 9]” of the Draft Guidelines. The list includes the Commission Implementing Regulation No. 1423/2013 laying down the content and format for the disclosure of own funds requirements under Article 437 of the CRR (p. 8 of the Draft Guidelines).

As mentioned above, the proposed New Disclosure Requirements would "*be provided as part of the information on capital requirements from article 438(c) and(d)*". However, since paragraphs (c) and (d) of Article 438 require that credit institutions disclose 8% of the risk-weighted exposure amounts for each exposure class specified in Article 112 or Article 147, such paragraphs only allow for disclosure of amounts of exposures, but not amounts of own funds that should have been deducted absent an Exemption Decision. Article 438 cannot therefore be a valid basis for the proposed New Disclosure Requirement of the Carrying Amount.

The New Disclosure Requirement of the Carrying Amount should rather be based on Article 437 of the CRR. However, Article 437(1)(d) of the CRR provides for an exhaustive list of items that must be subject to a separate disclosure by credit institutions: "*(i) each prudential filter applied pursuant to Article 32 to 35 of the CRR; (ii) each deduction made pursuant to Articles 36, 56 and 66 of the CRR ; and (iii) items not deducted in accordance with Articles 47, 48, 56, 66 and 79*". There is no reference to Article 49(1) of the CRR in that list, which means that insurance participations which are not deducted as a consequence of using Article 49(1) are not regarded by the CRR as requiring a separate disclosure and that the EU legislator did not intend to apply a separate disclosure requirement to the Carrying Amount. By requiring the separate disclosure of the Carrying Amount, the Draft Guidelines would add new disclosure obligations not provided for by Article 437 of the CRR.

Finally, the EBA does not demonstrate that such additional disclosure is necessary to ensure the effective and consistent application of the CRR (as required by Article 1(3) of Regulation (EU) No. 1093/2010) and, more generally, the Union law or the Basel Committee revised Pillar 3 framework.

As indicated in the draft Guidelines, the EBA has decided to issue "*own initiative Guidelines*" in order to "*ensure the harmonized and timely implementation*" in the EU of Pillar 3 requirements and avoid that, "*as the* [revised Pillar 3 framework] *cannot be used for disclosures by institutions in substitution of the legally applicable requirements in Part Eight CRR, market pressure might, in the absence of action by supervisors, force institutions to provide a double set of disclosures in these areas of misalignments between the CRR and the revised Pillar 3*" (p. 4 of the Draft Guidelines).

The EBA justifies the Draft Guidelines by a potential (and not actual) concern of misalignment between the Basel Committee revised Pillar 3 framework and CRD IV in respect of Pillar 3 requirements. However, the Basel Committee revised Pillar 3 framework does not require the disclosure of the amount of non-deducted holdings of own funds in insurance companies.[1]

- **Imposing the disclosure of the Carrying Amount would also legally deprive both Article 49(1) of the CRR and the Exemption Decisions of any useful effect and hurt the principle of legal certainty and legitimate expectations**.

The European Court of Justice has consistently held that "*where a provision of EU law is open to several interpretations, preference must be given to the interpretation which ensures that the provision retains its effectiveness*" and that the "*provision must be interpreted, as far as possible, in such a way as not to detract from its validity.*" Based on this EU principle of useful effect, Article 438(c) and (d) of the CRR must be interpreted in a manner consistent with the other provisions of the CRR so as not to deprive any of them of their effectiveness.

Pursuant to the EU legal principle of legal certainty, rules should also be clear and precise and their application foreseeable for all interested parties so that they may be able to ascertain unequivocally

[1] The Basel Committee revised Pillar 3 framework requires the deduction from own funds of participation in insurance companies, except in limited circumstances where such participations should be risk-weighted. In this case, the Basel Committee revised Pillar 3 framework only requires the disclosure of the risk-weighted exposure amount of non-deducted investments in insurance companies and not the amount of own funds that would have been deducted has the exception not been applicable (*See* Basel Committee on Banking Supervision Standards – Revised Pillar 3 disclosure requirements, January 2015, pp. 10 and 11).

what their rights and obligations are. It also results from this principle that individuals or companies which act in good faith on the basis of the law cannot be frustrated in their expectations. On this basis, financial conglomerates that have been authorized to not deduct their holdings of own funds instruments of insurance companies in accordance with Article 49(1) of the CRR, should legitimately expect the "full" benefit of their Exemption Decision. If credit institutions were required to disclose the Carrying Amount not deducted as a consequence of using Article 49(1) of the CRR, it is likely that the market would recalculate such institutions' CET1 capital ratios by reintegrating the RWA Amount and deducting the Carrying Amount, thereby in practice forcing such institutions to comply with stricter capital requirements than those applicable to them.

There are several examples of market pressure forcing institutions to comply with stricter capital requirements than as required under CRD IV. Institutions have been forced to calculate and publish their capital ratios on a fully loaded basis as if all CRD IV requirements were already applicable, in addition to phased-in ratios calculated in accordance with CRD IV transitional arrangements. This is also the case for TLAC: while there is no legal requirement yet, G-SIBs publish their TLAC calculated on the basis of the FSB term sheet of November 2015. In the rationale for the Draft Guidelines (as mentioned above), the EBA acknowledges that market pressure may be overwhelming. As a result, requiring the disclosure of the Carrying Amount as proposed by the EBA would in practice likely undermine the Exemption Decisions granted to financial conglomerates.

Interpreting Article 438(c) and (d) of the CRR as allowing such a requirement would deprive both the Exemption Decisions and Article 49(1) of the CRR of any useful effect and would also infringe the legitimate expectations of the concerned institutions to benefit from the full effect of the Exemption Decisions.

The EBA should therefore not require a separate disclosure of the Carrying Amount of non-deducted insurance participations

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