

The text of the Annex I which was approved by the European Parliament on 25 April 2024 could be considered as confusing on the treatment of some Trade Finance instruments as some of them, namely guarantees, are now mentioned twice in Bucket 2 and Bucket 4.

In the text of the Regulation 575/2013 (CRR) which was published on 26 June 2013,

- Bucket 2 (Medium risk) which required a 50% CCF included
 - (a) *trade finance off-balance sheet items, namely documentary credits issued or confirmed (see also 'Medium/low risk');*
- Bucket 3 (Medium/low risk) which required a 20% CCF included
 - (a) *trade finance off-balance sheet items:*
 - (i) *documentary credits in which underlying shipment acts as collateral and other self-liquidating transactions;*
 - (ii) *warranties (including tender and performance bonds and associated advance payment and retention guarantees) and guarantees not having the character of credit substitutes;*
 - (iii) *irrevocable standby letters of credit not having the character of credit substitutes*

Warranties and guarantees not having the character of credit substitutes deserved then a 20% CCF.

In the proposal issued by FISMA in 2021 to amend the CRR,

- the Bucket 2 which required a 50% CCF included
 - ✓ *Performance bonds, bid bonds, warranties and stand-by letters of credit related to particular transactions and*
 - ✓ *Off-balance sheet items not constituting a credit substitute where not explicitly included in any other category*
 - ✓ *Other off-balance sheet items carrying similar risk, as communicated to EBA*
- the Bucket 4 which required a 20% CCF included only
 - ✓ *Short-term, self-liquidating trade letters of credit arising from the movement of goods, in particular documentary credits collateralised by the underlying shipment, in case of an issuing institution or a confirming institution;*
 - ✓ *Other off-balance sheet items carrying similar risk, as communicated to EBA.*

Warranties and guarantees not having the character of credit substitutes were then moved from Bucket 4 to Bucket 2, deserving a 50% CCF.

The ICC published then studies which confirmed that a 20% CCF would adequately cover the risks attached to guarantees, such as performance bonds. The historical data on performance bonds issued on behalf of non-performing debtors show that the empirical CCF derived from the claim pay-out ratio is at 10%.

In the text approved at the Trilog in December 2023, warranties were then reintroduced in Bucket 4 but not deleted from Bucket 2.

In the text which was approved by the Parliament in April 2024

- the Bucket 2 which requires a 50% CCF includes
 - ✓ *Performance bonds, bid bonds, warranties and standby letters of credit related to particular transactions and similar transaction-related contingent items, excluding trade finance off-balance sheet items referred to in bucket 4;*
 - ✓ *Other off-balance sheet items carrying similar risk, as communicated to EBA.*

- the Bucket 4 which requires a 20% CCF includes
 - ✓ *Trade finance off-balance sheet items:*
 - *documentary credits in which underlying shipment acts as collateral and other self-liquidating transactions;*
 - *warranties (including tender and performance bonds and associated advance payment and retention guarantees) and guarantees not having the character of credit substitutes;*
 - *irrevocable standby letters of credit not having the character of credit substitutes;*
 - ✓ *Other off-balance sheet items carrying similar risk, as communicated to EBA.*

Then warranties (including tender and performance bonds and associated advance payment and retention guarantees) and guarantees not having the character of credit substitutes are mentioned twice, in Buckets 2 and 4, while the intention could have been to maintain them in Bucket 4, deserving a 20% CCF, as it was the case in 2013.

Would it be possible to take advantage of an amendment to the text of the CRR, as it occurred 15 times between 2015 and 2022, to clarify the treatment of these warranties, mentioning them only in Bucket 4 and deleting them from Bucket 2?

In the meantime, could the EBA confirm that these warranties carry a similar risks to instruments listed in Bucket 4 ?