European Parliament

Covered bonds: Issue and supervision, exposures

The Commission has proposed a directive and a regulation to create a unified European framework for covered bonds. Parliament is due to vote in April on the texts agreed in interinstitutional negotiations.

Background

Covered bonds are debt securities issued by credit institutions, and usually secured by a pool of mortgage loans or public sector debt. They are further characterised by the double protection offered to bondholders, the segregation of assets in their cover pool, over-collateralisation, and strict supervisory frameworks. Although they have a long-established tradition in Europe, and their volume on EU markets is considerable, issuance is mainly concentrated in five Member States. In addition, national regulatory regimes vary considerably in terms of supervision and composition of the cover pool. Lastly, despite benefiting from regulatory preferences, as well as – for the highest quality bonds – preferential capital treatment under the Capital Requirements Regulation (CRR), covered bonds share no common definition across national regulatory regimes, which can lead to different types of securities benefiting from this treatment.

European Commission proposal

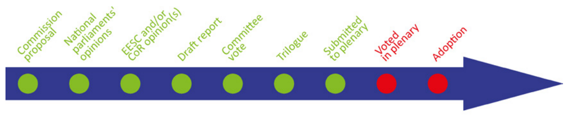
To remedy this, the Commission adopted proposals for, on the one hand, a directive, to define the features of the instrument, identify which assets can be considered as eligible in the pool backing the debt obligations, and lay down investor protection rules; and, on the other, a regulation, to amend, in the CRR, the conditions for covered bonds on banks' balance sheets benefiting from lighter capital treatment.

European Parliament position

In the compromise text for the directive, two labels for ordinary and premium covered bonds frame the issuance of covered bonds. The article on eligible cover assets is now more detailed, adding particular requirements for collateral assets, as well as public undertakings securing or guaranteeing covered bonds (10 % over-collateralisation). Intragroup pooled covered bond structures will be subject to specific requirements, while rules on joint funding are simplified. Furthermore, the obligations in terms of composition of the cover pool remain flexible. The requirement on the Commission to submit a report on third-country equivalence has been brought forward from three to two years after the provisions come into force. Lastly, the amended text includes the obligation for the Commission to submit a report to Parliament and Council after three years, covering implementation of the directive with regard to the level of investor protection and developments regarding the issue of covered bonds in the Union. The Commission has also to procure a study and consult the European Banking Authority and the European Central Bank on the possibility of introducing 'European Secured Notes'.

With regard to the proposed regulation amending the CRR, the agreed text modifies Article 129(1)(c) to include exposures in the form of derivative contracts and short-term deposits with a maturity not exceeding 100 days. Furthermore, for exposures in the form of short-term deposits and derivative contracts to credit institutions that qualify for credit quality step 3, the exposure must not exceed 8 % of the total exposure of the nominal amount of outstanding covered bonds of the issuing credit institution.

First-reading reports: 2018/0042 (COD) & 2018/0043 (COD); Committee responsible: ECON; Rapporteur: Bernd Lucke (ECR, Germany). For further information see our 'EU Legislation in progress' briefing.



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