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# Covered bonds – Issue and supervision, exposures

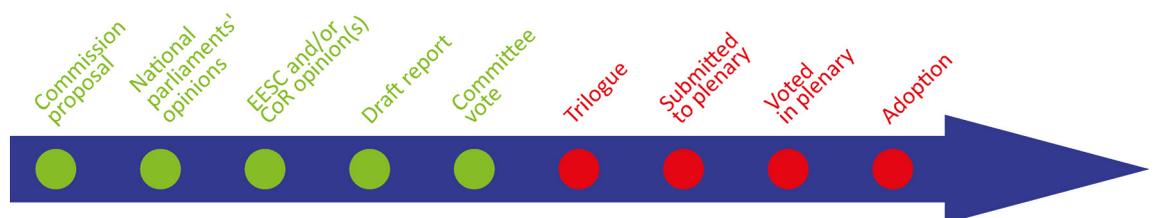
Covered bonds are debt securities issued by credit institutions and secured by a pool of mortgage loans or credit towards the public sector. They are characterised further by the double protection offered to bondholders, the segregation of assets in their cover pool, over-collateralisation, and their strict supervisory frameworks. Currently, their issuance is concentrated in five Member States. National regulatory regimes vary widely in terms of supervision and composition of the cover pool. Lastly, despite benefiting from preferential treatment under the Capital Requirements Regulation (CRR), they share no common definition, which can lead to different securities benefiting from this treatment. To remedy this, the Commission has adopted proposals for, on the one hand, a directive, which would lay down investor protection rules and provide common definitions, and on the other, a regulation, which would amend the CRR with regard to covered bond exposures. In November 2018, Parliament and Council both adopted their respective negotiating positions. The file is currently the subject of trilogue negotiations.

**Proposal for a directive of the European Parliament and of the Council on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU**

**Proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds**

COM(2018) 94, COM(2018) 93, 12.3.2018, 2018/0042 (COD), 2018/0043 (COD), Ordinary legislative procedure (COD) (Parliament and Council on equal footing – formerly 'co-decision')

Committee responsible:	Economic and Monetary Affairs (ECON)
Rapporteur:	Bernd Lucke (ECR, Germany)
Shadow rapporteurs:	Dariusz Rosati (EPP, Poland); Alfred Sant (S&D, Malta); Caroline Nagtegaal (ALDE, Netherlands); Marisa Matias (GUE/NGL, Portugal); Philippe Lamberts (Greens/EFA, Belgium); Barbara Kappel (ENF, Austria)
Next steps expected:	Trilogue negotiations



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The 'EU Legislation in Progress' briefings are updated at key stages throughout the legislative procedure. Please note this document has been designed for on-line viewing.



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## Introduction

There is no formal, universally accepted definition of 'covered bonds', just as there is no single name for them (they are called 'Pfandbriefe' in Germany, 'obligations foncières' in France, and 'cedulas' in Spain). However, they do share some characteristics that are seen as defining them. The [European Covered Bond Council](#) (ECBC) emphasises as most important:

- > the **dual recourse** – the double protection offered to bondholders: if the credit institution issuing the bond does not pay them, they have the right to turn against the institution's assets and, in case the institution goes bankrupt, they have a claim against a separate 'cover pool' of financial assets in priority to unsecured creditors;<sup>1</sup>
- > the **asset segregation** and **dynamic cover pool** – the obligation of the credit institution that issues the bond to 'ring-fence' the cover pool, and to ensure that the value of the assets making up the cover pool is equal to, or even higher than, the value of the covered bonds, at all times (also called **over-collateralisation**);
- > the **strict legal and supervisory frameworks** – to ensure asset segregation and the quality of the cover pool, public bodies must ensure both the supervision of the credit institution itself ('general' supervision), as well as the supervision of its obligations in respect of the cover pool ('special' supervision).

According to [the Commission](#), covered bonds constitute an important source of cheap and long-term funding for banks. Furthermore, they facilitate the financing of mortgage loans and public sector loans, thereby supporting lending more broadly. Also, they present the significant advantage over other kinds of bank funding sources (such as asset-backed securities) that banks retain the risk on their balance sheets and investors have claims directly with the bank. This also partially explains why they fared better, during the financial crisis, than other similar instruments. This, in turn, results in them benefiting from preferential prudential and regulatory treatment, according to Article 129 of the [Capital Requirements Regulation](#) (CRR) (e.g. banks investing in them do not have to set aside as much regulatory capital as when they invest in other assets).

## Existing situation

The covered bonds market is very developed in the EU. In December 2015, the outstanding volume of covered bonds reached €2.5 trillion globally, €2.1 trillion of which were issued by EU-based institutions. This constitutes 84 % of the total at global level.

According to the most recent version of the [covered bond fact book](#), published by the European Covered Bond Council, bank treasuries remain the largest private sector buyers of covered bonds, followed by asset

<sup>1</sup> The cover pool is the pool of loans or public sector debt that secure the covered bond. In case of default, investors have a preferential claim over this pool of debt (in priority to the bank's unsecured creditors).



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managers. On the institutional side, Eurosystem central banks have become one of the main covered bond investors as a result of the three [covered bond purchase programmes](#).

The issuance of covered bonds is currently regulated at national level. Regulatory regimes differ widely across Member States in terms of supervision, disclosure requirements and the composition of the pool of assets backing covered bonds.

At the EU level, in light of their low risk, covered bonds currently benefit from preferential prudential regulatory treatment under the CRR. However, existing EU law does not comprehensively address what constitutes a covered bond. As a result, the prudential treatment under the CRR may be granted to different products, depending on the applicable national law.

In addition, covered bond markets are unevenly developed across the single market. While they are very important in some Member States – Germany (18 % of the EU outstanding volume), Denmark (18 %), France (15 %), Spain (13 %) and Sweden (11 %) – they are less developed in others.

This is why the European Commission is proposing rules that will establish common EU definitions and standards for covered bonds. The proposed new rules also aim to address specific prudential concerns, by ensuring that the features of covered bonds are in line with the risk profile underlying already existing EU-wide preferential capital treatment.

## Parliament's starting position

The European Parliament adopted a resolution in July 2017 based on an own-initiative report entitled '[Towards a pan-European covered bonds framework](#)'. After noting the positive track record and importance of covered bonds for the EU economy, Members stressed that there is a need for an EU-wide framework to be established. They added that harmonisation should respect the principle of subsidiarity and avoid a one-size-fits-all approach, as this could lead to a sharp decline in the diversity of financial products and have a negative effect on national markets.

Parliament further called for the adoption of an EU directive that clearly distinguishes between the two types of covered bonds currently in existence, namely Premium Covered Bonds (PCBs), which do not fall below the standards currently set by the CRR, and Ordinary Covered Bonds (OCBs), which do not meet the requirements set out for PCBs but do not fall below the standards currently set by the Directive on Undertakings for Collective Investment in Transferable Securities ([UCITS Directive](#)). Members noted that, under this framework, PCBs should continue to enjoy regulatory preference over OCBs, and that OCBs should enjoy regulatory preference over other forms of collateralised debts. Lastly, Parliament recommended that debt instruments covered by assets that are substantially more risky than government debt and mortgages (e.g. non-government backed infrastructure investments or credits to small- and medium-sized enterprises) should not be labelled 'covered bonds' but, possibly, 'European Secured Notes'.



## Proposal

### Preparation of the proposal

In December 2012, the European Systemic Risk Board (ESRB) issued a [recommendation](#) on the funding of credit institutions. In response to that recommendation, the European Banking Authority (EBA) issued a [report](#) on 1 July 2014 providing an overview of the EU national covered bond frameworks, identifying key features and practices in defining a prudentially sound covered bond market and providing advice on the overall conditions justifying preferential risk weight treatment of certain types of covered bond in the EU.

In 2015, in accordance with its Capital Markets Union [action plan](#), the Commission carried out a [public consultation](#) on covered bonds, summarising it thus: 'Although stakeholders agreed that a robust legal framework would help to reduce volatility and ease market access in times of distress, they did not generally regard an absence of EU-level harmonisation as the most significant factor causing market fragmentation. While respondents were concerned that harmonisation based on a one-size-fits-all approach could risk impairing well-functioning markets and reducing flexibility and product offering, at the same time they showed cautious support for targeted EU action, provided that harmonisation is principles-based, built on existing frameworks and respects the unique characteristics of national frameworks'.

Following up the aforementioned EBA report, the ESRB recommended that the EBA monitor the functioning of the covered bonds market by reference to the best practices it had identified and called on the EBA to recommend further action if necessary. In response, the EBA issued a [report on covered bonds](#) in December 2016. The report built on the previous report and, among other things, analysed regulatory developments in covered bond frameworks in individual Member States, with a particular focus on the level of alignment with the best practices identified in the previous report. Building on the results of that study, the report presented a comprehensive proposal for a 'three-step approach' to the harmonisation of covered bond frameworks in the EU.

The Commission proposal built on the EBA's analysis and advice.

In its [impact assessment](#), the Commission considered a number of policy options for developing covered bond markets and addressing prudential concerns. The retained option is minimum harmonisation based on national regimes, which builds on the recommendations contained in the 2016 EBA report. For analysis of the Commission's impact assessment, see the EPRS [initial appraisal](#).



## The changes the proposal would bring

### The directive

#### Subject matter, scope and definitions (title 1)

The proposal for a [directive](#) lays down investor protection rules concerning (i) requirements for issuing covered bonds; (ii) the structural features of covered bonds; (iii) covered bond public supervision; (iv) publication requirements for competent authorities in relation to covered bonds. It would apply to covered bonds issued by banks<sup>2</sup> established in the EU (articles 1 and 2). It would further provide common definitions of terms such as 'covered bonds',<sup>3</sup> 'cover pool', 'over-collateralisation', or 'acceleration of a covered bond' (article 3).

#### Structural features of covered bonds (title 2)

#### Dual recourse and bankruptcy remoteness (chapter 1)

The proposal provides that Member States would lay down rules to safeguard the dual recourse and also would ensure the bankruptcy remoteness<sup>4</sup> of covered bonds (articles 4 and 5).

#### Cover pool and coverage (chapter 2)

The proposal provides that Member States would require that covered bonds are at all times collateralised by high quality assets (pointing to CRR for more details) and that banks issuing them have in place procedures to ensure that assets are insured against the risk of damage (article 6). Those requirements would also apply to assets located outside the EU; if a bank complies with them, a Member State would have the possibility to allow it to include those assets in the cover pool (article 7).

Article 8 provides that Member States would have the possibility to lay down rules regarding the use, by way of an intragroup transaction, of covered bonds issued by a bank belonging to a group as collateral for the external issue of covered bonds by another bank belonging to the same group. Article 9 deals with joint funding, i.e. the use of collateralised loans by a bank as assets in the cover pool for the issue of covered bonds by another bank.<sup>5</sup>

2 The Commission explains that the fact that the directive allows only banks to issue covered bonds is coherent with the inherent nature of the instrument (i.e. to provide funding for loans) and with the facts that banks (i) have the necessary knowledge and management capability of credit risk in relation to the loans in the cover pool and (ii) are subject to sound capital requirements.

3 'A debt obligation issued by a credit institution and secured by a cover pool of assets which covered bond investors have direct recourse to as preferred creditors'.

4 Bankruptcy remoteness would mean that covered bonds' maturity cannot be shortened automatically upon the issuer's insolvency or resolution. Bankruptcy remoteness would be directly linked to the dual recourse mechanism and would a core feature of the covered bond framework.

5 The European Commission notes in the detailed explanation of the specific provisions of the proposal for a Directive that, as covered bonds are issued mainly by large banks, their benefits are often beyond the reach of smaller institutions. The proposal for a directive would allow issuers to pool cover assets by several credit institutions under certain conditions. This would be intended to encourage issuance by smaller institutions and give them access to covered bonds funding.



Articles 10 to 12 deal with the composition of the cover pool, the requirements for the segregation of assets in the cover pool and the presence of derivative contracts (under specific requirements) in the cover pool.

Article 14 states that Member States would ensure that banks issuing covered bonds provide information on the programmes that is sufficiently detailed to allow investors to assess the profile and risks of that programme and to carry out their due diligence. It further provides for the minimum portfolio information that must be made available.

Article 15 sets minimum coverage requirements (e.g. all liabilities of the covered bonds would be covered by the assets in the cover pool) that Member States would need to ensure covered bond programmes meet.

Specifically to address liquidity risk, Article 16 provides that Member States would require that the cover pool includes at all times a liquidity buffer composed of specific liquid assets available to cover the net liquidity outflow of the programme for 180 calendar days.

Article 17 sets conditions for extendable maturity structures so as to ensure investor protection.

Lastly, article 13 of the proposal provides that Member States would have the possibility to require that issuing credit institutions appoint a cover pool monitor to perform ongoing monitoring of the pool with regard to articles 6 to 12 and 14 to 17.

### Covered bond public supervision (title 3)

The Commission proposal notes that covered bond public supervision is a core feature of many national covered bond frameworks; the proposal for a directive would therefore harmonise the components of such supervision and specify the tasks and responsibilities of the national competent authorities performing it.

Article 18 would task Member States with providing that the issue of covered bonds is subject to public supervision, and to designate one or more competent authorities to monitor the issue of covered bonds. Member States would further require banks to obtain permission (under specific minimum requirements) for their programmes before they can issue covered bonds under those programmes (article 19).

Article 20 provides that, in the event of the *resolution* of a bank issuing covered bonds, national competent authorities would cooperate with the resolution authority, in order to ensure that the rights and interests of the covered bond investors are preserved. By contrast, in the case of the *insolvency* of a credit institution issuing covered bonds, Member States would have the possibility to provide for a special administrator to be appointed for the same reasons. In both of these cases, they would ensure the coordination and exchange of information between the competent authorities, the special administrator and the resolution authority.

Member States would also require banks issuing covered bonds to report at least information on specific requirements of the programme to competent authorities on a regular basis and upon request. Member States would lay down rules on the frequency of the regular reporting (article 21).

Competent authorities would be given all supervisory, investigatory and sanctioning powers that are necessary to perform the task of covered bond public supervision (and at least those mentioned in article 22).



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In addition, Member States would lay down rules establishing appropriate effective, proportionate and dissuasive administrative penalties and remedial measures, applicable at least in the situations provided in article 23. Member States would make sure that those penalties and measures are effectively implemented. When determining their type and amount, competent authorities would take into account specific circumstances enumerated in paragraph 4 of article 23. Member States would also make sure that administrative sanctions and remedial measures are published without undue delay on the official website of the competent authorities. Those authorities would be further required to inform the European Banking of Authority (EBA) of any administrative sanctions and remedial measures imposed, and the EBA would maintain a central database of those communicated sanctions and remedial measures (article 24).

Member States would ensure that competent authorities cooperate closely with the authorities performing general bank supervision, with each other, as well as with the EBA (article 25).

Lastly, article 26 states that Member States would ensure that competent authorities publish, on their official website, their national regulations relative to the issue of covered bonds; the list of banks permitted to issue covered bonds; and the list of covered bonds allowed to use the European Covered Bonds label (see next point).

#### Labelling (title 4)

Under the provisions of the directive, Member States would allow banks to use the label 'European Covered Bonds' in respect of covered bonds which meet the requirements laid down in the provisions transposing the directive. It would not regulate national denominations and labels, which would continue to be used.

#### Amendments to other directives (title 5)

The proposed directive would amend Article 52(4) of the UCITS Directive (possibility for Member States to raise the 5 % limit on a UCITS asset invested in transferable securities or money market instruments) to replace the definition of covered bonds. It would also amend Article 2(1) of the Bank Recovery and Resolution Directive to add the definition of 'covered bond' to its list of definitions.

## The regulation

With regard to Article 129(1) – on exposures in the form of covered bonds – of [Regulation \(EU\) No 575/2013](#) (often referred to as the CRR), the proposed [regulation](#) would:

- > replace the introductory phrase of paragraph 1 with a new one, so that the reference to covered bonds in Directive 2009/65/EC (UCITS) would be replaced with a reference to the new directive (see above);
- > replace Article 129(1) point (c) 'institutions' with 'credit institutions';



Preparation of the proposal

The changes the proposal would bring

- > delete Article 129(1) points (d) ii) and (f) ii), which relate to loans secured by senior units issued by French 'Fonds communs de titrisation' or equivalent securitisation entities governed by the laws of a Member State securitising residential property exposures. Similarly, it would delete the reference to those points from the second sub-paragraph;<sup>6</sup>
- > delete Article 129(1) third sub-paragraph and inserts instead new paragraphs 1a, 1b and 1c. Paragraph 1a details that exposures to banks that qualify for credit quality step 1 (see Articles 114 and onwards of the CRR) would not exceed 15 % of the nominal amount of outstanding covered bonds of the issuing credit institution, while exposures to those that qualify for step 2 would not exceed 10 % of the total exposure of the nominal amount of outstanding covered bonds. Also, the total exposure to banks that qualify either for step 1 or 2 would not exceed 15 % of the total exposure of the nominal amount. Paragraph 1a would, lastly, provide that it would not apply to the use of covered bonds as eligible collateral as permitted pursuant to article 9 of the proposed directive (i.e. joint funding – see above). Paragraph 1b relates to paragraph 1 point (d)(i) (loans secured by residential property) and would provide that the limit of 80 % in that point would refer to the portion of the loan that contributes to the coverage of liabilities attached to the covered bond. Finally, paragraph 1c would relate to points (f)(i) (loans secured by commercial immovable property) and (g) (loans secured by maritime liens on ships) and provide, similarly, that the limit of 80 % in that point would refer to the portion of the loan that would contribute to the coverage of liabilities attached to the covered bond;
- > insert two new paragraphs (3a and 3b) with regard to immovable property collateralising covered bonds, according to which covered bonds would be subject to a minimum of 5 % over-collateralisation<sup>7</sup> (although competent authorities designated according to the directive would be able to decide to impose a lower minimum level of over-collateralisation, provided specific conditions stipulated in the article would be met) and eligible assets in paragraph 1 would be included in the cover pool as substitution assets;
- > amend paragraph 6 so that covered bonds issued before 31 December 2007 would not be subject to the requirements of (also) the new paragraphs 3a and 3b. It would also amend paragraph 7 so that covered bonds issued before the regulation is applied are not subject to the requirements of paragraphs 3a and 3b.

It would amend Article 416(2) so as to include covered bonds in the meaning of the proposal for a directive on covered bonds to the list of liquid assets. For the same reason, it replaces point 6(c) of Annex III (Items subject to supplementary reporting of liquid assets).

It would amend Article 425(1) so as to exempt covered bonds from the 75 % inflow limit, in the meaning of the directive on covered bonds.

6 The European Commission notes in the detailed explanation of the specific provisions of the proposal for a Regulation that this possibility is repealed because only a few national covered bond frameworks allow the inclusion of residential or commercial mortgage-backed securities.

7 The Commission notes that 'this level is in line with the advice of the EBA and with the results of the ICF study. While lower than the new Basel standards, it would make the product safer and would raise the level for the majority of Member States where the required minimum level is currently lower'.



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In point (b) Article 427(1), it would amend point (x) to add covered bonds, in the meaning of the new directive on covered bonds, to the liabilities that need to be reported to the competent authorities. For the same reason, it would amend point (h) (iii) of Article 428(1).

It would delete Article 496, as that article relates to Article 129(1) (1)(d)(ii) and (f)(ii), which have also been deleted.



Advisory committees

National parliaments

Stakeholders' views

## Views

### Advisory committees

Neither committee has yet adopted an opinion on the matter.

### National parliaments

The deadline for the submission of reasoned opinion on the grounds of subsidiarity was 16 May for the [proposed regulation](#) and 17 May 2018 for the [proposed directive](#). No reasoned opinion was adopted.

### Stakeholders' views<sup>8</sup>

The European Mortgage Federation – European Covered Bond Council (EMF-ECBC) [welcomed](#) the adoption of the European Commission's package on covered bonds, appreciating 'the long and careful consideration given by the European Institutions in preparing the draft framework for the key qualitative characteristics of the covered bond asset class, and to maintaining its fundamental role in the long-term funding strategies of European lenders'.

<sup>8</sup> This section aims to provide a flavour of the debate and is not intended to be an exhaustive account of all different views on the proposal. Additional information can be found in related publications listed under 'EP supporting analysis'.



## Legislative process

### Parliament's report on the proposed directive

In Parliament, the ECON committee appointed Bernd Lucke (ECR, Germany) as rapporteur for both files - directive and regulation. The draft report for the proposed directive on issue and public supervision was published on 17 August, and the [report](#) was adopted on 20 November 2018.

### Subject matter, scope and definitions (title 1)

In article 3, the main amendments concern the definitions of 'covered bond'<sup>9</sup> and 'cover pool',<sup>10</sup> as well as the introduction of a definition for 'resolution'.

### Structural features of covered bonds (title 2)

An important addition proposed is the creation of two classes of covered bonds, namely covered bonds (premium) and ordinary covered bonds. Parliament would amend the Commission proposal's article 6, which now relates to covered assets for covered bonds (premium) (i.e. those which also comply with the requirements set in Article 129 of the Capital Requirements Regulation), whereas a new article 6a would deal with cover assets for ordinary covered bonds. The article stipulates that in case Member States allow the issuance of covered bonds secured by high quality covered assets, they must require that cover assets provide the issuing institution with claims for the payment of a clearly determined amount of money (which must meet specific legal requirements, laid out in point 2) and are secured by collateral assets (which must meet the requirements of point 3). Furthermore, they must impose specific requirements (point 4) to ensure risk mitigation.

With regard to the joint funding of covered bonds by several credit institutions (article 9), Parliament would amend the Commission proposal so that funding is allowed if the jointly funded covered bond is issued by a single credit institution – 'the lead institute', and adds obligations for Member States (such as limiting joint funding, or direct recourse in the case of insolvency or resolution of the lead institute).

Article 10 (composition of the cover pool) would also be amended, so as to specify that, for the cover pool in article 6 to be considered sufficiently homogeneous, all of its primary assets must comply with the eligibility criteria set in points (a) to (g) of [Article 129\(1\) of the CRR](#) (concerning exposures in the form of covered bonds).

9 'A debt obligation issued under public supervision ... by a credit institution or by a specialised mortgage credit institution and which is a dual recourse instrument ..., which is bankruptcy remote ..., for which the assets in the cover pool are segregated ..., and which is collateralised by eligible assets.'

10 'A clearly defined set of identifiable assets securing the payment obligations of the covered bond issuer until maturity of the covered bond and subject to legal arrangements ensuring that those assets will be segregated from other assets held by the credit institution issuing covered bonds at the latest when resolution or insolvency proceedings have been opened in respect of the covered bond issuer.'



### Covered bond public supervision (title 3)

In article 23 relative to administrative penalties, Parliament would add that Member States may decide not to lay down rules on such penalties or measures, if they already provide for criminal penalties in their national law.

### Labelling (title 4)

Parliament would amend article 27 so that the labelling requirements for Member States also apply to European covered bonds (premium).

### Final provisions (title 6)

The proposal would not amend title V, but create two new articles within title VI of the Commission proposal (final provisions). The first one concerns equivalence (Article 31) and empowers the Commission to adopt delegated acts, while the other (Article 31a) deals with reviews and reports, and sets the obligation for the Commission to submit a report to Parliament and Council on the implementation of the directive after three years, as well as to procure a study and to consult the EBA and ECB on the possibility of introducing 'European Secured Notes'.

### Parliament's report on the proposed regulation

The committee draft report for the proposed regulation on exposures was published on 21 August and [adopted](#) on 20 November 2018. Parliament would amend Article 4(1) of the CRR to add the definition of 'extendable maturity structure'.<sup>11</sup>

Parliament would also amend Article 129 CRR:

Paragraph 1(c) would be amended to include exposures in the form of short-term deposits with a maturity not exceeding 100 days, and 1(f) to include loans secured by commercial immovable property or non-residential immovable property held for non-profit purposes.

(New) point (ba) of newly inserted paragraph 1a would stipulate that, for exposures in the form of short-term deposits and derivative contracts to credit institutions that qualify for the credit quality step 3, the exposure must not exceed 5 % of the total exposure of the nominal amount of outstanding covered bonds of the issuing credit institution.

The Commission's proposed paragraph 1b would be amended. Under the new paragraph, the values of the properties pledged must be monitored on a regular basis and updated annually by the issuer, using an indexation method based on market prices of immovable property.

11 'A mechanism providing for the possibility, upon the occurrence of a trigger event, of extending the scheduled maturity of covered bonds for a certain period of time.'

The Commission's proposed paragraph 1c would also be amended. Under the new paragraph, the full loan amount, irrespective of the limit set out in the first subparagraph, must be subject to the segregation of assets in the cover pool.

In paragraph 3a, Parliament would add as a condition for lower level of collateralisation the regular (public) disclosure by the credit institution issuing covered bonds of the level of over-collateralisation.

Lastly, the new paragraph 7a would state that for the purposes of points (d)(i), (e), (f) and (g) of the first subparagraph of paragraph 1 (loans secured by e.g. residential property, commercial immovable property, or maritime [liens](#)), Member States would be able to decide to apply a higher limit referring to the portion of the loan contributing to the coverage of liabilities, provided that specific conditions are met.

### Council position on the proposed directive

In the Council the Working Party on Financial Services discussed the two proposals at eight meetings under the Bulgarian and Austrian Presidencies. On 23 November 2018, delegations agreed on the texts of the negotiating mandates.

On the proposed directive on [issue and supervision](#), the Council proposed – among other things – the following amendments to the Commission proposal.

### Subject matter, scope and definitions (title 1)

In article 3 (definitions), the Council changes the term defined from 'acceleration of a covered bond' to 'automatic acceleration of a covered bond' and provides a definition for that automatic acceleration.<sup>12</sup>It also deletes the term and definition of 'residential property'. It amends the definition of 'match funding requirement' to include counterparties of derivative contracts, and to add that amounts received from borrowers and counterparties of derivative contracts must be placed in the cover pool in assets, until the payments are due to the covered bond investors and counterparties of derivative contracts. Lastly, it defines the term 'group' (of undertakings).

### Structural features of covered bonds (title 2)

Article 6 (eligible cover assets) is significantly amended. The proposal would set the obligation for covered bonds to be secured at all times either by assets eligible under Article 129 of the CRR or by high quality covered assets, ensuring a claim for payment (which must meet the requirements of point 2) and secured by collateral assets (which must meet the requirements of point 3). Member States would have to lay down rules on the valuation methodology and process for physical assets used as collateral. They would also have to require that credit institutions issuing covered bonds have procedures in place to monitor that assets used as collateral are adequately insured against the risk of damage, and document the cover assets.

<sup>12</sup> 'A situation in which a covered bond upon insolvency or resolution of the issuer automatically becomes immediately due and payable and in respect of which the covered bond investors have an enforceable claim to be repaid earlier than the original maturity date.'



In article 9 (joint funding), Council would add that Member States may allow for cover assets to be originated by an undertaking that is not a credit institution. If they do so, however, they must require that the issuing credit institution either performs its own assessment of the creditworthiness of the obligor, or verifies that the originating undertaking has effective processes in order to ensure that credit-granting is based on a thorough assessment of the creditworthiness of the obligor and (for cover assets that are loan claims), assesses the credit-granting standards of that undertaking.

The amended version of article 10 (composition of the cover pool) would change the role of Member States. Instead of them having to ensure investor protection by providing for a sufficient level of homogeneity of the assets in the cover pool, they would instead have to lay down rules on the composition of cover pools, as well as rules on the level of homogeneity required from assets in the cover pool.

In article 13, relative to the cover pool monitor, Council would add the possibility for Member States to allow a cover pool monitor that is not separate from the credit institution, under specific conditions.

In article 15 (requirements for coverage), point 1b of the Commission proposal (calculation of the level of coverage) would become a new point 2 and would be significantly more detailed compared to the Commission proposal. A derogation to this paragraph would be introduced in paragraph 3. Ultimately, points 1c (list of assets in the cover pool that can contribute to the coverage requirement) and 1d (stipulating that uncollateralised claims, where a default is considered to have occurred, do not contribute to the cover pool) of the Commission proposal would be deleted.

### Covered bond public supervision (title 3)

In article 21 (reporting to competent authorities) point 2, information relative to dual recourse, bankruptcy remoteness of the covered bond and investor information requirements, would no longer have to be provided.

In article 23 (administrative penalties and remedial measures), point 6 would provide the possibility of exceptions to the right to be heard for a period of time, when urgent action is needed in order to prevent significant losses to third parties or significant damage to the financial system.

### Final provisions (title 6)

Two new points would be added to proposed article 30 relative to transitional measures. With the first one, Member States would have to ensure that competent authorities supervise the compliance of covered bonds issued before a specific date with the requirements laid down in Article 52(4) of the UCITS Directive (i.e. the maximum amount a UCITS can invest in bonds issued by a credit institution registered in a Member State). With the second one, it would give them the possibility to allow the first paragraph also to apply to tap issues of covered bonds for which the opening of the [ISIN code](#) is prior to that date, provided the issues comply with specific requirements.



## Council position on the proposed regulation

On [exposures](#), the Council would amend the Commission's amendment to Article 129(1) point c of the CRR. The amended text would add, to exposures to credit institutions that qualify for credit quality steps 1 and 2, those exposures that are in the form of short-term deposits and are used to fulfil the cover pool liquidity buffer requirement, as well as derivative contracts, where they are permitted by the competent authorities. Accordingly, it would also add a new sub-paragraph (b1), according to which, exposures in the form of short-term deposits and derivative contracts to credit institutions that qualify for credit quality step 3, must not exceed 10 % of the total exposure of the nominal amount of outstanding covered bonds of the issuing credit institution.



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[Exposures in the form of covered bonds](#), European Parliament, Legislative Train Schedules.

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