Committee on Economic and Monetary Affairs

2018/0042(COD)

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DRAFT REPORT

on the proposal for a regulation of the European Parliament and of the Council on amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds
(COM(2018)0093 – C8-0112/2018 – 2018/0042(COD))

Committee on Economic and Monetary Affairs

Rapporteur: Bernd Lucke

Symbols for procedures

*	Consultation procedure
***	Consent procedure
***I	Ordinary legislative procedure (first reading)
***II	Ordinary legislative procedure (second reading)
***III	Ordinary legislative procedure (third reading)

(The type of procedure depends on the legal basis proposed by the draft act.)

Amendments to a draft act

Amendments by Parliament set out in two columns

Deletions are indicated in ***bold italics*** in the left-hand column. Replacements are indicated in ***bold italics*** in both columns. New text is indicated in ***bold italics*** in the right-hand column.

The first and second lines of the header of each amendment identify the relevant part of the draft act under consideration. If an amendment pertains to an existing act that the draft act is seeking to amend, the amendment heading includes a third line identifying the existing act and a fourth line identifying the provision in that act that Parliament wishes to amend.

Amendments by Parliament in the form of a consolidated text

New text is highlighted in ***bold italics***. Deletions are indicated using either the ▌ symbol or strikeout. Replacements are indicated by highlighting the new text in ***bold italics*** and by deleting or striking out the text that has been replaced.
By way of exception, purely technical changes made by the drafting departments in preparing the final text are not highlighted.

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on the proposal for a regulation of the European Parliament and of the Council on amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds
(COM(2018)0093 – C8-0112/2018 – 2018/0042(COD))

(Ordinary legislative procedure: first reading)

The European Parliament,

– having regard to the Commission proposal to Parliament and the Council (COM(2018)0093),

– having regard to Article 294(2) and Article 114 of the Treaty on the Functioning of the European Union, pursuant to which the Commission submitted the proposal to Parliament (C8-0112/2018),

– having regard to Article 294(3) of the Treaty on the Functioning of the European Union,

– having regard to the opinion of the European Economic and Social Committee of 11 July 2018[1],

– having regard to Rule 59 of its Rules of Procedure,

– having regard to the report of the Committee on Economic and Monetary Affairs (A8-0000/2018),

1. Adopts its position at first reading hereinafter set out;

2. Calls on the Commission to refer the matter to Parliament again if it replaces, substantially amends or intends to substantially amend its proposal;

3. Instructs its President to forward its position to the Council, the Commission and the national parliaments.

Amendment 1

Proposal for a regulation
Recital 7

Text proposed by the Commission	*Amendment*
(7) Intragroup pooled covered bond structures which comply with Regulation (EU) No 575/2013, have also been used as eligible collateral in accordance with	***deleted***

[1] OJ C … of …, p …

points (d)(ii) and (f)(ii) of the first subparagraph of Article 129(1) of that Regulation. Intragroup pooled covered bond structures do not pose additional risks from a prudential perspective because they are not raising the same complexity issues as the use of loans secured by senior units issued by French Fonds Communs de Titrisation or equivalent securitisation entities securitising residential or commercial property exposures. According to EBA, collateralisation of covered bonds by pooled covered bond structures should be allowed without limits related to the amount of outstanding covered bonds of the issuing credit institution[22] . Accordingly, point (c) of the first subparagraph of Article 129(1) should be amended to remove the requirement to apply the limit of 15 % or 10 % in relation to exposures to credit institutions in intragroup pooled covered bond structures. Those intragroup pooled covered bond structures are regulated by Article 9 of Directive (EU) 20../…. [OP: Please insert reference to Directive (EU) on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU].

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[22] ***Ibid.***

Or. en

Justification

Allowing the use of internally issued covered bonds (issued for sale within an intragroup) as cover pool assets for externally issued CBs may make cover pools intransparent. While the externally issued CB would be secured by a (first-layer) cover pool, the internally issued covered bonds in this first-layer cover pool would be covered by second-layer cover pools. There would be no limit to the number of second-layer cover pools contributing to the cover of the first-layer cover pool. Unless the number of internally issued CBs is very small, this may easily become an intransparent structure and may greatly exacerbate a proper risk assessment by investors. (For instance, in the case of a German Landesbank, there may be a great number of Sparkassen belonging to the same group and each of the Sparkassen could, in principle, participate in the issue of a Landesbank CB by issuing its own internal CB *secured by a second-layer cover pool.) Moreover, consistency problems arise in the case where the group sells off smaller institutions which issued internal bonds. Such a sale would generate CBs which have (external) CBs in their cover pool – which is not generally allowed under the Commission proposal for the Directive. The purpose of joint funding can be served equally well (and even better!) by Article 9 of the Directive. This Article does not entail the intransparent cover pool structure and it would provide a level playing field between small banks which belong to a group big enough to issue CBs and those which do not. The small group of (Danish) issuers which use intragroup covered bonds structures shall be given a ten year grace period in Article 129 CRR.*

Amendment 2

Proposal for a regulation
Recital 9

Text proposed by the Commission	*Amendment*
(9) Limits for Loan-To-Value ('LTV') are a necessary part of ensuring the credit quality of the covered bonds. Article 129(1) of Regulation (EU) No 575/2013 establishes the LTV limits for mortgage and ship assets but does not specify how those limits are to be applied which may lead to uncertainty. The LTV limits should be applied as soft coverage limits, meaning that while there are no limits to the size of an underlying loan, such a loan can only act as collateral within the LTV limits imposed on the assets. The LTV limits determine the percentage portion of the loan that contributes to the requirement of coverage of the liabilities. It is therefore appropriate to specify that the LTV limits ***apply to*** the portion of the loan contributing to the coverage of the covered bond.	(9) Limits for Loan-To-Value ('LTV') are a necessary part of ensuring the credit quality of the covered bonds. Article 129(1) of Regulation (EU) No 575/2013 establishes the LTV limits for mortgage and ship assets but does not specify how those limits are to be applied, which may lead to uncertainty. The LTV limits should be applied as soft coverage limits, meaning that while there are no limits to the size of an underlying loan, such a loan can only act as collateral within the LTV limits imposed on the assets. The LTV limits determine the percentage portion of the loan that contributes to the requirement of coverage of the liabilities. It is therefore appropriate to specify that the LTV limits ***determine*** the portion of the loan contributing to the coverage of the covered bond.

Or. en

Justification

The Commission text (last two sentences) is circular. What is meant is that the LTV determines how much of a loan can contribute to the cover pool.

Amendment 3

Proposal for a regulation
Recital 12 a (new)

Text proposed by the Commission	*Amendment*
	(12a) Currently, covered bonds which are not compatible with Article 129 of Regulation (EU) No 575/2013 receive the same risk weight as unsecured exposures to institutions (cf. Article 120 and Article 121 of the same Regulation). This is inappropriate, precisely because these bonds are covered and the exposures are secured. Covered bonds which are not eligible for Article 129 of Regulation (EU) No 575/2013 should henceforth receive better regulatory treatment than unsecured exposures to the same institutions. Such treatment is also appropriate because securitisations which are seen as "simple, transparent and standardised" have recently been granted special regulatory preference and, clearly, the new Directive on covered bonds and covered bond supervision also defines a simple, transparent and standardised framework. Therefore, covered bonds issued in that framework should also be granted preferential treatment.

Or. en

Amendment 4

Proposal for a regulation
Recital 12 b (new)

Text proposed by the Commission	*Amendment*
	(12b) Extendable maturities are a new development in the field of covered bonds. They were not taken into account in the drafting of Article 129 of Regulation (EU) No 575/2013. The possibility to extend maturities makes covered bonds on the

asset side of bank balances more risky and, in times of financial distress, less liquid. This calls for increasing the risk weight. On the other hand, such bonds might be less risky if the maturity extension preserves the value of cover pool assets by avoiding fire sales. This offsets the risk of reduced liquidity. For that reason, the extendibility of the maturity by one year or less should not be penalised with an increase in the risk factor. However, if asset prices have not recovered after a year, their reduced level might in fact be persistent. Hence, covered bonds with a maturity that is extendable by more than one year should be viewed as shifting risk from the issuer to the investor. Since that type of covered bond is of higher risk than a standard fixed maturity bond, an increased risk weight is warranted.

Or. en

Amendment 5

Proposal for a regulation
Article 1 – paragraph 1 – point -1 (new)
Regulation (EU) No 575/2013
Article 4 – paragraph 1 – point 128a (new)

Text proposed by the Commission	*Amendment*
	-1. In Article 4, paragraph 1, the following point is added:
	(128a) 'extendable maturity structure' means a mechanism providing for the possibility to extend the scheduled maturity of covered bonds for a certain period of time and in the event that a specific trigger occurs;

Or. en

Justification

The CRR should also cover extendable maturity structures. Hence, the term should be *defined. The definition is taken from the Directive.*

Amendment 6

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point a – point i – indent 4
Regulation (EU) No 575/2013
Article 129 – paragraph 1 – subparagraph 1 – point f

Text proposed by the Commission	*Amendment*
- ***in*** point (f)***, point (ii) is deleted;***	- point (f) ***is replaced by the following:***
	(f) loans secured by commercial immovable property, or by non-residential immovable property held for non-profit purposes, up to the lesser of the principal amount of the liens that are combined with any prior liens and 60 % of the value of the pledged properties.

Or. en

Justification

The CRR covers residential and commercial real estate. There is no good reason why immovable property of non-profit organizations (e.g. churches, private museums, hospices) should not be eligible as well. In fact, EBA applies a broad interpretation of "commercial immovable property" so that such real estate is, in fact, currently included in some cover pools. But the examples given are clearly non-commercial and non-residential, so we should close the gap in the law and explicitly mention non-residential, non-profit property.

Amendment 7

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point a – point iii
Regulation (EU) No 575/2013
Article 129 – paragraph 1 – subparagraph 3

Text proposed by the Commission	*Amendment*
(iii) the third subparagraph is ***deleted;***	(iii) the third subparagraph is ***replaced by the following:***
	If significant concentration problems in some Member States can be documented due to the application of the credit quality step 1 requirement referred to in point (c)

	of the first subparagraph, EBA may, for all credit institutions concerned and for a period of at most three years, waive the application of the first subparagraph and allow credit quality step 2 exposures for up to 10 % of the total exposure of the nominal amount of outstanding covered bonds of the issuing institution. EBA may repeal that decision at any time, provided it grants credit institutions an adequate transition period.

Or. en

Justification

The Commission argues that credit quality step 2 should be generally allowed because it has become increasingly difficult to find credit institutions which have credit quality step 1. While this is true, legislation should not enter a race to the bottom with credit institutions. Therefore, I propose that in times of stress, EBA may temporarily allow lower credit quality, but it should be clear that, in general, the standards are upheld and it is the task of credit institutions to adapt and re-establish their creditworthiness to the highest level.

Amendment 8

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point b
Regulation (EU) No 575/2013
Article 129 – paragraph 1a – subparagraph 1 – point c

Text proposed by the Commission	*Amendment*
(c) the total exposure to ***credit*** institutions that qualify for the credit quality step 1 ***or the credit quality step 2*** shall not exceed 15 % ***of the total exposure*** of the nominal amount of outstanding covered bonds of the issuing ***credit*** institution.	(c) the total exposure to institutions that qualify for the credit quality step 1 ***as set out in this Chapter*** shall not exceed 15 % of the nominal amount of outstanding covered bonds of the issuing institution. ***Exposures to institutions in the Union with a maturity not exceeding 100 days shall not be comprised by the step 1 requirement but those institutions shall as a minimum qualify for credit quality step 2 as set out in this Chapter;***

Or. en

Justification

The Commission wants to replace today's CRR text "c) exposures to institutions that qualify for the credit quality step 1 as set out in this Chapter". The Commission's text would allow exposures to credit institutions even for credit quality step 2. These exposures would not necessarily be backed by collateral. The limits of 15%, 10% and 15% of the nominal amount of total outstanding bonds set in the new paragraph 1a are sizable and they would not apply at all to those banks which use covered bonds of other institutions as collateral. The Commission argues that this is necessary to allow for unlimited use of internal covered bonds by an external CB issuer. But the Commission text goes much farther since collateral requirements are generally waived within the above limits. Essentially, credit institutions with credit quality step two would be put on equal footing with governments, even though the former do not have tax raising power. It seems advisable to keep the well-tested text which is currently in the CRR. The change would be unnecessary in any case if, as suggested, Article 8 on internal bonds, is deleted from the Directive.

Amendment 9

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point b
Regulation (EU) No 575/2013
Article 129 – paragraph 1a – subparagraph 2

Text proposed by the Commission	*Amendment*
This paragraph shall not apply to the use of covered bonds as eligible collateral ***as permitted pursuant to Article 9 of Directive (EU) 20xx/xxxx [OP: Please insert reference to Directive (EU) on the issue of*** covered bonds ***and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU]***.	***For a period of ten years after ... [the date of entry into force of this Regulation],*** this paragraph shall not apply to the use of covered bonds as eligible collateral ***for issuers which have had, prior to January 1, 2018, an established practice of using*** covered bonds ***of credit institutions belonging to the same group as eligible collateral***.

Or. en

Justification

This gives the Danish issuers using this model plenty of time to adapt their business model to the joint funding possibilities provided for in Article 9 of the CB Directive.

Amendment 10

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point b
Regulation (EU) No 575/2013
Article 129 – paragraph 1b

Text proposed by the Commission	*Amendment*
1b. For the purposes of point (d)(i) of the first subparagraph of paragraph 1, the limit of 80 % shall ***refer to*** the portion of the loan contributing to the coverage of liabilities attached to the covered bond and be applicable throughout the entire maturity of the loan.	1b. For the purposes of point (d)(i) of the first subparagraph of paragraph 1, the limit of 80 % shall ***determine*** the portion of the loan contributing to the coverage of liabilities attached to the covered bond and be applicable throughout the entire maturity of the loan.

Or. en

Justification

The meaning of "refer to" is unclear. The corresponding Recital 9 also uses "determine".

Amendment 11

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point b
Regulation (EU) No 575/2013
Article 129 – paragraph 1c

Text proposed by the Commission	*Amendment*
1c. For the purposes of point (f)(i) and point (g) of the first subparagraph of paragraph 1, the limit of 60 % shall ***refer to*** the portion of the loan contributing to the coverage of liabilities attached to the covered bond and be applicable throughout the entire maturity of the loan.***;***	1c. For the purposes of point (f)(i) and point (g) of the first subparagraph of paragraph 1, the limit of 60 % shall ***determine*** the portion of the loan contributing to the coverage of liabilities attached to the covered bond and be applicable throughout the entire maturity of the loan.

Or. en

Justification

The meaning of „refer to" is unclear. The corresponding Recital 9 also uses „determine".

Amendment 12

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point d
Regulation (EU) No 575/2013
Article 129 – paragraph 3a – subparagraph 3

Text proposed by the Commission	*Amendment*
The assets contributing to a minimum level of overcollateralisation shall ***not*** be subject to the limits on exposure size as set out in points (b) and (c) of the first subparagraph of paragraph 1 and shall ***not*** count towards those limits.	The assets contributing to a minimum level of overcollateralisation shall be subject to the limits on exposure size as set out in points (b) and (c) of the first subparagraph of paragraph 1 and shall count towards those limits.

Or. en

Justification

The Commission proposes a minimum level of overcollateralisation requirement in order for a covered bond to be eligible for preferential capital treatment. But the Commission does not require that CRR-eligible assets contributing to the minimum level of overcollateralisation are subject to the limits on exposure size set out in point (b) and (c) of Article 129(1).This approach conflicts with the EBA recommendation made in 2016. If the limits are not enforced the cover pool assets used to arrive at the level of overcollateralisation could include a share of lower quality exposures greater than deemed prudent as an 'eligible asset'. This could create clear financial stability risks.

Amendment 13

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point d
Regulation (EU) No 575/2013
Article 129 – paragraph 3a – subparagraph 4

Text proposed by the Commission	*Amendment*
Competent authorities designated pursuant to Article 18(2) of Directive (EU) 20xx/xxx [OP: Please insert reference to Directive (EU) on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU] ***may decide to apply a lower minimum level of overcollateralisation to covered bonds*** provided that the following conditions are met:	***Member States may decide to apply a lower minimum level of overcollateralisation to covered bonds or may authorise their*** competent authorities designated pursuant to Article 18(2) of Directive (EU) 20xx/xxx[OP: Please insert reference to Directive (EU) on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU] ***to do so,*** provided that the following conditions are met:

Or. en

Justification

There is more democratic scrutiny if Member States lay out the OC requirements in legislative acts rather than leave the decision to the discretion of a competent authority. While the latter may be advantageous in terms of flexibility, the former approach also has its merits and should therefore be allowed.

Amendment 14

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point ea (new)
Regulation (EU) No 575/2013
Article 129 – paragraph 7a (new)

Text proposed by the Commission	*Amendment*
	(ea) after paragraph 7, the following paragraph is inserted:
	7a. Covered bonds failing to comply with paragraph 1 but complying with the requirements of Directive (EU) 20XX/XX of the European Parliament and of the Council on covered bonds and covered bond supervision shall be assigned a risk weight equal to a factor of 0,7 multiplied by the risk weight applicable to an unsecured exposure to a rated institution or an unrated institution according to Articles 120 and 121 of this Regulation, respectively.

Or. en

Justification

Currently, covered bonds which are not Article 129-compatible receive the same risk weight as unsecured exposures to institutions, cf. Article 120 and Article 121 CRR. This is inappropriate precisely because these bonds are covered and the exposures secured. Covered bonds which are not eligible for Article 129 (1) CRR should henceforth receive better preferential treatment than unsecured exposures. This is even more appropriate since STS securitizations have recently been granted special regulatory preference and, clearly, the new Directive on Covered Bonds and Covered Bond Supervision also defines a simple, transparent and standardized framework in which these covered bonds are issued.

Amendment 15

Proposal for a regulation
Article 1 – paragraph 1 – point 1 – point eb (new)
Regulation (EU) No 575/2013
Article 129 – paragraph 7b (new)

Text proposed by the Commission	*Amendment*
	(eb) after paragraph 7, the following paragraph is inserted:
	7b. The risk weights provided for in paragraphs 4, 5 and 7a shall be increased if the covered bond was issued with an extendable maturity structure under which its maturity can be extended by more than one year. The increase of the risk weight shall be equal to
	- 5 percentage points if the maturity can be extended by at most three years.
	- 10 percentage points if the maturity can be extended by at most five years.
	- 15 percentage points if the maturity can be extended by at most ten years.
	- 20 percentage points if the maturity can be extended by more than ten years.
	For the purpose of this Article, the length of a possible maturity extension is always the possible extension at the date of issue.

Or. en

Justification

Extendable maturities are a new development in the covered bond universe. They have not been taken into account when Article 129 of the CRR was devised. The possibility of maturity extensions makes covered bonds on the asset side of bank balances more risky - and less liquid in times of financial distress. This calls for increasing the risk weight. On the other hand, these bonds may be less risky if the maturity extension serves at preserving the value of cover pool assets by avoiding fire sales. This is an offsetting factor to the risk of reduced liquidity and it is the reason why extendable maturities of one year or less shall not be penalized with an increase in the risk factor. However, if asset prices have not recovered after a year, their reduced level may actually be persistent. Hence, covered bonds with maturity extensions of more than a year should be viewed as shifting risk from the issuer to the investor. Since this type of covered bond is of higher risk than a standard fixed maturity bond, an increased risk weight is warranted.

EXPLANATORY STATEMENT

The European Parliament, in its resolution 2017/2005(INI) 'Towards a pan-European covered bonds framework' of 4 July 2017, supported the creation of a principles-based European covered bonds framework, aiming at

(i) a clear distinction between covered bonds (CB) which comply with Article 129 CRR ('premium covered bonds' (PCB)) and those which do not ('ordinary covered bonds' (OCB)).

(ii) regulatory preference of PCBs over OCBs.

(iii) regulatory preference of OCBs over other forms of collateralized debt.

(iv) PCBs and OCBs being highly liquid and close to risk-free assets.

(v) a 'European Secured Notes' (ESN) framework as a third tier after PCBs and OCBs.

(vi) transparency of covered bond structures to facilitate risk assessment.

The Commission proposals make good progress towards some of these objectives. They ensure (ii), but fail to address (i), (iii) and (v). There are good proposals for (iv) and (vi), but there is also room for improvement.

As for (i), the Commission proposals do not distinguish between PCBs and OCBs. Your rapporteur proposes to split Article 6 of the proposed directive (on eligible assets) into Articles 6 and Article 6a, where the former defines assets eligible for PCBs and the latter assets eligible for OCBs. Moreover, the label 'European Covered Bond' laid down in Article 27 should apply to OCBs, while PCBs are distinguished from OCBs by an additional designation, i. e. 'European Covered Bond (Premium)'.

As for (iii), there is no Commission proposal and OCBs would receive the same risk weight as unsecured exposures to institutions, cf. Articles 120 and 121 of the CRR. This seems inappropriate, since a secured exposure is safer than an unsecured exposure. Also, STS securitisations have recently been granted preferential treatment in the CRR, so it is hard to understand why OCBs compliant with a simple, transparent and standardized European Covered Bonds framework would be treated like unsecured exposures. Your rapporteur suggests to amend Article 129 of the CRR by a new paragraph 8 specifying the risk weights of covered bonds which fail to comply with Article 129, paragraph 1, but qualify for the (ordinary) 'European Covered Bonds' label. Specifically, my suggestion is to grant those covered bonds (which, technically, are 'exposures to institutions') a risk weight equal to 70% of the risk weight for which the exposure would qualify if it were unsecured (Articles 120 and 121 of the CRR).

The issues of (iv) and (v) should be dealt with jointly, since the Commission has not made a proposal which would allow certain types of assets to be relegated to an ESN framework. Your rapporteur therefore suggests the following approach:

(a) There should be no positive (or negative) list of possible asset types for OCBs. Rather, all types of assets (even those which Parliament had in mind for ESNs) may, in principle, be eligible for OCB cover pools[1]. This allows innovation, growth and development in the OCB segment of the European covered bond market.

(b) However, OCBs should be liquid and almost risk-free assets. Their cover assets must be of high quality. Given no restrictions on the nature of the cover assets, their quality shall be ensured by requiring strict adherence to the well-tested structural properties of CB cover pool assets in terms of legal requirements (enforceability of claims), asset valuation (not surpassing market or mortgage lending value), and risk mitigation (prudent loan-to-value ratios and sufficient diversification), cf. the proposed Article 6a of the Directive. These requirements protect the covered bond label.

As for (vi), the Commission proposals are generally well suited to enhance transparency and facilitate investors‘ risk assessment. However, your rapporteur feels that the proposed Article 8 of the Directive (Intragroup pooled CB structures) undermines these objectives and should therefore be deleted. Article 8 would allow cover pools to contain internally issued covered bonds of other banks belonging to the same group as cover assets. The internally issued covered bonds would be covered by second-layer cover pools and there would be no limit to the number of second-layer cover pools contributing to the cover of the first-layer cover pool. Unless the number of internally issued CBs is very small, this may easily become an intransparent structure and may greatly impair a proper risk assessment by investors.

Your rapporteur suggests to delete Article 8 and simultaneously modify Article 9 (Joint funding) such that it serves the same purpose as Article 8 without entailing the same detriments. (A generous transition phase should be granted to the very small number of (Danish) banks which currently use intragroup pooled CB structures.) Under the proposed new wording of Article 9, any number of banks may jointly fund a covered bond issue. All these banks would contribute assets to just one cover pool under the responsibility of a ’lead institution’ which issues the covered bond. This would ensure transparency and simplified risk assessment. It would, unlike Article 8, also provide a level playing field between small banks which belong to a group big enough to issue CBs and those which do not.

Other issues:

Homogeneity of cover pools (Article 10 of the proposed directive)

Surpassing Parliament’s demands, the Commission text required cover pool homogeneity. This wording should be softer, since some degree of heterogeneity is indispensable for risk diversification and liquidity management. Since it is impossible to define the optimal degree of homogeneity in a legal text, Article 10 gives examples of the admissible degree of heterogeneity for CRR-eligible assets.

Extendable maturities (new in Article 129 CRR via Article 1(1) of the proposed regulation)

Soft bullet and conditional pass-through structures are a new development in the covered bond universe. They have not been taken into account when Article 129 of the CRR was

[1] This is in line with the very broad approach to CBs taken in the UCITs Directive. Moreover, a positive or negative list of asset types may be hard to reconcile with a principles-based legislation.

devised. Parliament emphasized that regulatory preference should be granted corresponding to the safety of assets. In terms of risk there are pros and cons of extendable maturities, but clearly the longer the possible maturity extension, the more risk is shifted to the investor. Therefore, your rapporteur proposes to amend Article 129 CRR by a new paragraph 7b which gradually increases the risk weight for covered bonds whose maturity can be extended by more than a year.

Liquidity buffer (Article 16 of the proposed directive)

Parliament demanded that the cover pool contain a liquidity buffer for half a year. The Commission has transposed this demand in Article 16 of the Directive. However, there is an open contradiction between the requirement in paragraph 1 (cover pool includes ”at all times“ a liquidity buffer) and the derogation the Commission foresees in paragraph 4 (liquidity buffer is not necessary for the 30 days where the bank has liquidity from LCR requirements). While this derogation is motivated from the legitimate intent to eliminate double-counting claims against the bank, it overlooks the fact that upon insolvency or resolution of the credit institution the cover pool is segregated from the bank. Since in this case, LCR liquidity remains with the bank, the cover pool would be without liquidity reserves for the first 30 days. Your rapporteur finds this unacceptable and has proposed a different solution which also eliminates double-counting but preserves, even under insolvency of the issuer, the liquidity of the cover pool for 180 days and the LCR reserve of the bank for 30 days under stress.

3rd country equivalence (Article 31 of the proposed directive)

The Commission proposes to wait for more than three years before possibly submitting a legislative initiative on the recognition of third-country equivalence. Such a long delay is at odds with Parliament’s aim of establishing the EU covered bonds framework as a benchmark model for developing covered bonds markets worldwide since a long delay signals a reluctance to open the EU market to non-EU competitors. This said, introducing an equivalence regime now does not necessarily mean that equivalence will be granted to third countries immediately. Instead, it would just provide the framework for which equivalence can be granted if the Commission decides that third countries provide equivalent levels of investor protection. The absence of even a framework for recognizing equivalence would clearly not incentivise third countries to duplicate the EU model. In addition, there is no reason to wait for details of how Member States have implemented the Directive. The nature of the Commission’s minimum harmonising approach is that the standard is based on a common set of principles to be interpreted and developed individually by Member States. This framework is sufficient to allow for equivalence assessments of similar measures enacted by third countries.