



EUROPEAN COMMISSION

DIRECTORATE-GENERAL FOR FINANCIAL STABILITY, FINANCIAL SERVICES AND CAPITAL
MARKETS UNION

Review of the EU Macprudential Framework

Call for advice

With this Call for Advice, the European Commission wishes to consult the European Banking Authority (EBA) and the European Systemic Risk Board (ESRB) in accordance with Article 513 of Regulation (EU) No 575/2013 (hereinafter ‘CRR’) in view of the legislative review of the EU macroprudential framework. The call for advice also seeks to obtain qualitative and quantitative evidence, including from supervisory data, as well as concrete examples or case studies and experience gathered by relevant authorities in achieving the goals of macroprudential policies. The call is therefore also addressed to the ECB, in its macroprudential capacity.

The three addressees of this call for advice are invited to submit their views and analysis by 31 March 2022.

CONTEXT AND SCOPE OF THE REVIEW

Article 513 of Regulation (EU) No 575/2013 requires the Commission to complete a review of the macroprudential provisions in the CRR and Directive 2013/36/EU (CRD)¹ by June 2022 and, if appropriate, to submit a legislative proposal to the European Parliament and to the Council by December 2022.

The mandate in Article 513 CRR offers the opportunity to review and improve the EU macroprudential framework applicable to banks. Article 513 CRR envisages a broad scope for the review, requiring the Commission to assess the effectiveness, efficiency and transparency of the macroprudential framework, listing a number of specific issues to be considered in view of a possible legislative proposal. Additional issues related to the design and use of the instruments and to the governance of macroprudential policy have become apparent over recent years and in particular during the Covid-19 pandemic – the first test of the macroprudential framework in a major economic crisis.

¹ Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

The advice should cover four broad areas:

1. overall design and functioning of the buffer framework;
2. missing or obsolete instruments;
3. internal market considerations; and
4. global risks.

These issues shall be analysed taking into account ongoing discussions at the international level and the Covid-19 crisis experience. The overall aim of the review is to improve the framework's functioning in the medium term, focusing on its effectiveness, efficiency and transparency and taking into account the impacts on other frameworks (prudential, resolution). Any suggested changes should be justified as far as possible on the basis of quantitative evidence and/or economic theory. This applies particularly to measures that would imply higher overall capital requirements. Departures from the international minimum standards set by the Basel Committee should be avoided, but the addressees could signal and justify any changes to these standards that they would regard desirable for the EU.

When proposing amendments to the framework, it is important that relevant costs and benefits of different options, including the baseline option of no change, are assessed and quantified (cost-benefit analysis or CBA hereafter).

The Commission is aware that, CBAs for some of the issues raised in this call for advice, may not be entirely feasible within the given timeframe and with the resources available. The advice should be delivered on a best-effort basis, using the latest knowledge and reflecting work that is already available.

1. OVERALL DESIGN AND FUNCTIONING OF THE BUFFER FRAMEWORK FROM THE MACROPRUDENTIAL PERSPECTIVE

Capital buffers were introduced following the Global Financial Crisis with the primary aim of increasing banks' resilience against systemic risks and vulnerabilities of various types. While the buffer requirements have contributed to higher capital levels and hence resilience, depending on the type of banks and their exposures, the functioning of the buffer framework in a crisis situation has not yet been fully tested, given that in the Covid-19 crisis (the first crisis with the macroprudential framework in place) banks have indirectly benefited from public support measures. This crisis has nevertheless triggered a discussion on whether the buffer framework is optimally designed not only to provide additional resilience, but also to act counter-cyclically when necessary and encourage banks to maintain their supply of credit to the economy also in an economic downturn.

Particular attention should be given to the appropriateness of buffers for systemically important institutions, global (G-SIIs) and other (O-SIIs). Together, these institutions are the main providers of credit in Member States and as such vital to economic performance. At the same time, the integration of G-SIIs and O-SIIs in increasingly complex financial systems makes them vulnerable to financial shocks occurring outside the banking sector and turns them into potential contagion channels for financial instability (the global dimension of this issue will be dealt with in more depth in section 4).

The Commission seeks advice on the following questions:

Based on the evaluation of the current buffer framework, is there scope for optimising the overall design and use of the buffer framework to prevent and mitigate financial stability risks and to reduce the pro-cyclicality of the financial system? In particular:

- Is there scope for making the buffer framework more effective in ensuring sufficient resilience against different types of systemic risks in all Member States and for different types of banks and exposures, and if so, what changes would be needed?
- Is there scope for making the buffer framework more effective in smoothening financial and economic cycles, and if so, how could this be achieved through buffer calibration and the modalities for restoring buffers after a buffer release or buffer depletion?
- Is there need and scope for redesigning the macroprudential buffer framework in view of its interaction with other capital requirements (leverage ratio minimum requirements, minimum requirements for own funds and eligible liabilities (MREL)), and if so, how?
- Is the systemic importance of banks appropriately and adequately covered by G-SII and O-SII buffer requirements, and should the leverage ratio buffer requirement that applies to G-SIIs be extended to O-SIIs and, if so, should the calibration be different from the calibration for G-SIIs?

Supporting analysis should focus primarily on the following issues:

Compare the level of macroprudential buffer requirements across Member States, types of banks and types of exposures and assess their consistency, taking into account differing levels of systemic risk.

Check whether there is sufficient clarity as to which buffer should be used for which risk and how buffers should be calibrated for a given risk (taking into account differences in risk weights across banks), notably as regards the sectoral application of systemic risk buffers. If necessary, make proposals, based on a CBA, for achieving more consistency (e.g. through amendments of existing legal provisions, guidance, governance arrangements).

Assess in a comprehensive manner the buffer requirements for SIIs, their appropriateness in view of their market shares, their specific activities and the risk their failure would pose to financial stability, and the consistency of O-SII buffer requirements across Member States and also in comparison with G-SIIs. When it comes to excluding banks' activities across the euro area from the category of cross-border activities, evidence should be provided on the relevance of this issue for O-SIIs, in comparison to the existing provisions for G-SIIs. Assess, based on a CBA whether a leverage ratio buffer requirement similar to the one for G-SIIs should be extended to O-SIIs, and, if that is the case, in what manner the calibration should be tailored to the specific features of those institutions and what implications the possible introduction of a leverage ratio buffer requirement for O-SIIs would have in terms of additional capital demand and on the resolution framework.

Analyse how pro-cyclical behaviour of banks can be mitigated through the use of macroprudential tools and how banks might respond to countercyclical buffer rate adjustments under different scenarios and conditions. Explore in particular the main motivations behind banks' behaviour as they get close to their combined buffer requirements (CBR) or dip into their buffers (e.g. avoid market stigma, continue to remunerate investors, maintain prudent safety margins). In light of this, discuss the costs and benefits of different options for reforming the buffer framework or developing new guidance for its application over the cycle. The options to be considered should cover

buffer releasability, replenishment pathways and distribution restrictions; they should be assessed based on a CBA and under different crisis scenarios, taking also into account the broader market implications for banks' debt instruments. If the evidence and analysis points to a need to increase the share of releasable buffers (for instance, in the form of a positive neutral CCyB rate over the cycle), it should be explored whether and how this could be achieved in a capital-neutral way that is also consistent with international standards and the resolution framework and its objectives. Appropriate governance and coordination arrangements for the calibration of buffers, the timing of their release and replenishment and the use of distribution restrictions to avoid premature distributions if buffers are released before banks have fully absorbed a shock) should also be discussed.

As regards overlapping capital requirements, review evidence of how important the overlaps are, based on the applicable prudential and resolution frameworks, and assess the likely evolution of these overlaps over the coming years. Assess the implications of these overlaps for achieving the goals of macroprudential policy and estimate the costs and benefits of options for reducing these overlaps, if these are deemed necessary.

2. MISSING OR OBSOLETE INSTRUMENTS

While the EU has a broad range of capital buffers, other tools may still need to be added to the EU legal framework, while some existing ones may be or may become obsolete.

Many Member States are using borrower-based measures (BBMs) in addition to capital-based and other measures to prevent credit-fuelled overheating in the residential real estate sector. In principle, borrower-based measures could also target non-financial corporates (NFCs), but very few Member States have developed such tools for NFCs, typically focusing on commercial real estate.

Macroprudential policy has so far been mainly of a preventive and longer-term nature. The Covid-19 shock has tested the framework's suitability for crisis management. Article 459 CRR empowers the Commission to take short-term measures in response to changes in the intensity of micro- or macroprudential risks (under very restrictive conditions), but it is difficult to imagine a scenario where the conditions for using this article would be met, and where the tools provided for in the article would be appropriate. There was a consensus in the current crisis on the need to impose restrictions on the distribution of capital to investors and staff even before the CBR is breached, but there are no clearly defined powers for national or EU authorities to apply such restrictions on a system-wide basis. The Commission was therefore given a mandate to assess whether competent authorities should be empowered by EU law to impose restrictions on such distributions in exceptional circumstances (Article 518b CRR).

The review should also seek to identify instruments that may be obsolete. Having multiple prudential tools that can target similar risks would create unwarranted complexity and may contribute to a more fragmented internal market. In particular, forthcoming legal changes due to the finalisation of Basel III reforms may have implications for macroprudential instruments that directly or indirectly affect risk-weights such as those provided under Articles 164 and 458 CRR.

The Commission seeks advice on the following questions:

Based on the evaluation of the current framework, are there any tools that are missing in the current macroprudential framework or that have or may soon become obsolete, and if so, which ones? In particular:

- Should certain instruments be added to the EU macroprudential toolkit? Specifically, how could the EU macroprudential framework support and ensure a more comparable and effective use of borrower-based measures across MS to target potentially unsustainable borrowing by households and non-financial corporates?
- Is there a need to enhance the crisis management capacity of macroprudential policy, at the Union and/or national level, in particular to impose system-wide restrictions on distributions in exceptional circumstances?
- Have certain instruments become obsolete or could they become obsolete over the coming years? In particular, to what extent should provisions be maintained that allow the adjustment of risk weights or risk weight determinants for real estate exposures on macroprudential grounds once Basel III input and output floors apply?

Supporting analysis should focus primarily on the following issues:

Review evidence on the use and effectiveness of borrower-based measures and assess, based on a CBA, how their optimal use could be supported via the macroprudential framework in EU law, for instance by (i) introducing harmonised definitions and indicators in the area of BBMs; (ii) enhancing the availability of data (for instance from credit registers) needed for the effective application of BBMs; and (iii) introducing a minimum, harmonised BBM toolkit for residential real estate, commercial real estate, and/or for non-financial corporations. Assess the costs and benefits of different options not only from a financial stability perspective, but also with regard to the functioning of the internal market (market fragmentation, reciprocation) and possibly social impacts (access to home ownership) and administrative burdens.

Assess, based on a CBA and taking into account the effectiveness of authorities' use of existing tools to reduce distributions during the Covid-19 crisis, whether and how additional powers to restrict system-wide distributions should be introduced for macroprudential authorities and specified in EU law. Review evidence on the impact of system-wide distribution restrictions on banks' overall resilience, on the integrity of intragroup transferability of resources within cross-border groups, and on banks' access to market funding and ability to raise additional capital. If it is concluded that system-wide distribution restrictions are needed, propose criteria that could govern the activation of system-wide distribution restrictions at the EU group level (or at the individual level where the financial institution is not part of an EU group), including possibly at sub-consolidated or individual level, and the potential interactions of such discretionary restrictions with automatic distribution restrictions pursuant to Articles 141 and 141b CRD, as well as other relevant microprudential measures. Present any other crisis management tools (new tools or coordination of existing ones) that should be considered in the macroprudential sphere, together with the costs and benefits thereof.

Assess, based on a CBA, whether certain macroprudential instruments may become obsolete or should be reviewed (notably Article 164 and certain provisions of Article 458 CRR) and explore options for possible adaptations thereof, taking into account the experience so far with macroprudential policies and recent and upcoming changes in the broader context (notably the introduction of sectoral systemic risk buffers and the forthcoming Basel III finalisation with the introduction of input and output floors).

3. INTERNAL MARKET CONSIDERATIONS

The EU macroprudential framework also seeks to preserve the integrity of the internal market while leaving it mostly to Member State authorities to address adequately

systemic risks, which tend to be specific to individual Member States (although this may change with deeper economic and financial integration). The largely decentralised use of macroprudential instruments is therefore framed by provisions in CRR and CRD, which require an EU-level authorisation for certain measures. Moreover, the effectiveness of national macroprudential measures in the internal market depends on being able to prevent, through reciprocation by other Member States, circumvention and regulatory arbitrage, an issue which may arise not only in relation to other Member States, but possibly other parts of the financial sector to the extent that they can provide similar services as banks. It is important to assess, also in light of the recent crisis experience, whether the current framework offers not only the appropriate macroprudential tools to national authorities, but also ensures their effectiveness in the internal market, and whether it provides for adequate safeguards for the integrity of the internal market. The review should therefore also consider whether provisions related to the internal market achieve their goals without undue complexity. It should therefore be assessed, based on a CBA, whether there is scope for simplifying and streamlining procedures while maintaining necessary safeguards.

The Commission seeks advice on the following questions:

Based on an assessment of the current framework, does the macroprudential framework strike the right balance between national decision-making and a well-functioning internal market? In particular:

- Is there evidence to suggest that macroprudential measures go beyond what is appropriate to address systemic risks, despite the safeguards in the framework to prevent this? Or, on the contrary, is there evidence that macroprudential measures fall short of appropriately addressing systemic risk due to governance issues or the applicable authorisation procedures?
- Are the provisions to prevent inappropriate uses of macroprudential tools proportionate and effective? Is there scope for simplification or streamlining of procedures? If so, which ones and how would you evaluate them?
- Are the provisions on reciprocation adequate to maintain a level playing field and to prevent the circumvention of national macroprudential measures through regulatory arbitrage? Is there scope for simplification or streamlining of the reciprocation framework and procedures? If so, which options do you see and how would you evaluate them?
- Is there a need for measures that could mitigate the risk of circumvention through a shift of activities to non-bank financial services providers? If so which ones, and how would you evaluate them?
- Are the hard- and soft-law instruments (such as the ECB's power to top up buffers, the Commission empowerment in Article 459, ESRB warnings and recommendations) adequate to ensure that national authorities take sufficient and appropriate action to address systemic risks? If not, which additional measures would you see and how would you evaluate them?

Supporting analysis should focus primarily on the following issues:

Assess whether disparities in the implementation of national macroprudential policies create undue fragmentation of the internal market, going beyond what would be justified by systemic risks and vulnerabilities that can be observed in the Member States. Advise whether there is a need to adapt the current EU oversight powers, rules and procedures, not only to make them more effective, but also to reduce complexity and administrative

burdens while retaining the effectiveness of the safeguards, and, if appropriate, make proposals based on a CBA. Focus in particular on the systemic risk buffer (Art 133 CRD) and its interaction with O-SII buffers to propose possible alternative designs of the thresholds defined in Article 133(10)-(12) and in Article 131, particularly when systemic risk buffers are sectoral. Explore streamlined and consistent authorisation procedures for national macroprudential measures, including those notified in accordance with Article 458 CRR and advise on appropriate analytical methodologies for judging whether such measures entail disproportionate adverse effects on the whole or parts of the financial system of other Member States or of the Union as a whole or create an obstacle to the proper functioning of the internal market.

Review evidence of circumvention of national macroprudential measures either through a shift of services to other Member States (and cross-border provision of such services to the country applying the macroprudential measure) or through shifts of such activities towards non-banks. Propose options based on a CBA for preventing such circumvention and for ensuring the effectiveness of national macroprudential measures. Determine the appropriate scope for mandatory reciprocity. Propose ways of integrating the consideration of reciprocity needs in the assessment of the national measure, avoiding further assessments of reciprocity measures.

Examine whether there is evidence of inaction bias (regarding both the build-up and reduction/release of buffers), identify circumstances under which it is likely to occur, and assess how effective EU instruments are in overcoming such inaction bias and whether there is a need for adapting those EU instruments, such as Article 459 CRR.

4. GLOBAL RISKS, INCLUDING CLIMATE CHANGE

Financial stability in the EU does not only depend on limiting systemic risks and vulnerabilities within the EU. There are contagion risks from outside the EU, often also involving non-bank financial intermediation, that also need to be addressed. While financial intermediation through non-banks is growing in importance, banks continue to play a pivotal role in the global financial system. Large banks provide crucial services for non-bank financial intermediaries. Moreover, new developments happening at a global scale can represent growing threats to financial stability. The financial stability implications of climate change are already widely acknowledged and studied and should receive special attention in this review. Other important topics could be cyber security threats, the entry of big tech firms in financial services and the rise of crypto assets.

The Commission seeks advice on the following questions:

Based on your evaluation, does the current macroprudential framework provide sufficient and appropriate tools to protect financial stability in the EU against adverse developments in third countries and other challenges? In particular:

- Are macroprudential tools (notably Articles 138 and 139 CRD) appropriate and sufficient to prevent and mitigate financial stability risks arising from banks' exposure to third countries, notably taking into account compliance with global prudential standards? If not, which tools could be added and how would you evaluate them?
- Is there a need to enhance the tools for monitoring and mitigating banks' risk exposures to other financial institutions, notably through derivatives, margin debt and securities financing transactions? If so, which tools could be added and how would you evaluate them?

- Given the increasing importance of market-based finance and trading, is there a need to enhance the tools for monitoring and mitigating banks' risk exposures, while at the same time strengthening the resilience of banks' market making functions and the provision of market liquidity in crisis situation? If so, which tools could be added and how would you evaluate them?
- Are macroprudential tools appropriate and sufficient to prevent and mitigate financial stability risks arising from the changing nature of systemic risks (including due to climate change, new global providers of financial services, cybersecurity and crypto assets)? If not, which tools could be added and how would you evaluate them?

Supporting analysis should focus primarily on the following issues:

Assess, based on a CBA, the main risks for EU financial stability emanating from material third countries' financial systems and whether the EU's existing prudential tools and notably capital requirements are sufficient to mitigate those risks and have been used in an adequate way by national authorities; review the effectiveness of the powers and procedures enshrined in Articles 138 and 139 CRD and consider possible improvements or alternatives (e.g. coordinated use of microprudential tools).

Assess, based on a CBA, the interconnectedness between the banking and the non-banking financial sectors and analyse how this has developed since the Global Financial Crisis and what financial stability risks arise therefrom, paying particular attention to the role of banks as market makers and providers of funding and services for market participants. Explore, based on a CBA, possible changes to the macroprudential toolkit to mitigate these risks, taking into account the existing entity- and activity-based regulations covering the markets for derivatives and securities financing transactions, the asset management sector and the insurance sector in the EU, and, where relevant, in other jurisdictions from which financial instability could spill over into the EU.

Explore plausible scenarios for the materialisation of new global risks and assess, based on a CBA, what policy tools could be used or developed to counter such risks, both at EU level and in global fora. Review the approaches for, and experience with, stress tests that have been developed for such new global risks, notably climate change, and consider designs for further stress tests. Discuss how stress test results could be used for the choice and calibration of possible macroprudential measures.

FINAL CONSIDERATIONS

To avoid overlaps and duplication of effort and to ensure consistency, particularly in the cost-benefit analysis approach, the Commission proposes to establish an informal liaison group with experts designated by the addressees and the Commission. Its task would be to make choices on what evidence and methodologies to consider in answering the questions, and possibly to allocate tasks among the addressees; this should be without prejudice to the right of each addressee to draw its own conclusions from the analysis.

The Commission recalls that the advice provided will not prejudice the Commission's final decision on a legislative proposal.

The addressees are invited to deliver their advice to the Commission services by 31 March 2022.