



*Process and structure of the new
supervisory framework*
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I. CRD IV – contents recap

How does the CRD IV affect provisions and requirements?

1. Basel III has been implemented in the CRD
2. Basel I and II remain relevant
3. CRD IV includes the modifications from CRD II and III
4. CRD IV includes other initiatives like
 - European Single rulebook, Maximum harmonization
 - Basel/FSB buffers, e.g. the “SIB” buffer
 - Governance rulebook, Revised sanctions regime

-> The CRD IV is a complete revision of all provisions

II. CRD IV – legal recap

Word by word the CRD has changed dramatically:

1. Many details of the CRD have changed (a bit, or more)
2. The legal form of much of the CRD has changed:
 - one Directive (“CRD”)
 - one Regulation (“CRR”)
 - 100+ Binding Technical Standards by EBA (also Regulations)
 - dozens of other mandates to EBA or the Commission
 - COREP harmonization broader, deeper and more relevant

-> The CRD IV is an important change to European law

III. CRD IV Changes to European law

The transition to a regulation has broad implications:

- Directly applicable
- Legally binding to anyone
- (hence) no implementation in national law
- (hence) no/few national options and discretions
- (hence) most options are options to institutions
- (hence) almost no national law

-> The CRR implies a massive change to national law

IV. National impact of a Regulation

Consequences of a Regulation:

- A Regulation prevails over national law
- National law should not contain similar provisions
- National law ought to arrange only anything that has not been set out in Regulations
- Specific macro-prudential provisions are excluded

-> Much of our national law has to be modified

V. Changes to national legislation

How does national legislation change?

- New provisions in the Directive are implemented in Wft
 - Higher level legislation (Wft and Bpr) are becoming references guides to details in the CRR
 - Lower level legislation (DNB toezichthouderregelingen) are withdrawn unless they concern Directive areas
 - Some waivers are void and must be reconsidered
- > DNB and institutions must verify compliance with the CRR, even in areas where Basel III has no impact

VI. How to approach a Regulation

How do we apply a Regulation?

- European regulations are generally interpreted literally
- The EBA is mandated to interpret the Regulation
- Forget about national traditions

“**Animal farm principle**” the CRR is equal in all languages but the English language version is slightly more equal

-> Ask questions to the EBA

VII. CRD IV – where to find what

CRR (R = regulation):

- Definitions
- Scope of application
- Definition of capital
- Solvency requirements
- Large exposures
- Retention requirements
- Liquidity
- Leverage ratio
- Disclosure (“Pillar III”)
- Transitional arrangements

CRD (D = directive):

- Authorisation
- Competences of supervisors
- Sanctions
- Governance
- Remuneration
- Consolidated supervision
- Pillar II
- Capital buffer provisions

A directive has to be transposed into national law. Hence these subjects are to found in the Wft.

VIII. CRD IV - structure

How could I use the order of the CRD en CRR?

1. CRD / CRR – separate subject matters
2. Parts – themes
3. Titles – formal segments
4. Chapters – formal segments
5. Sections – logical segments
6. Subsections – logical segments
7. Articles – separate provisions
8. Paragraphs – usually exemptions to the main rule
9. Sub-paragraphs – usually exemptions to the main rule

IX. CRD IV and the SSM

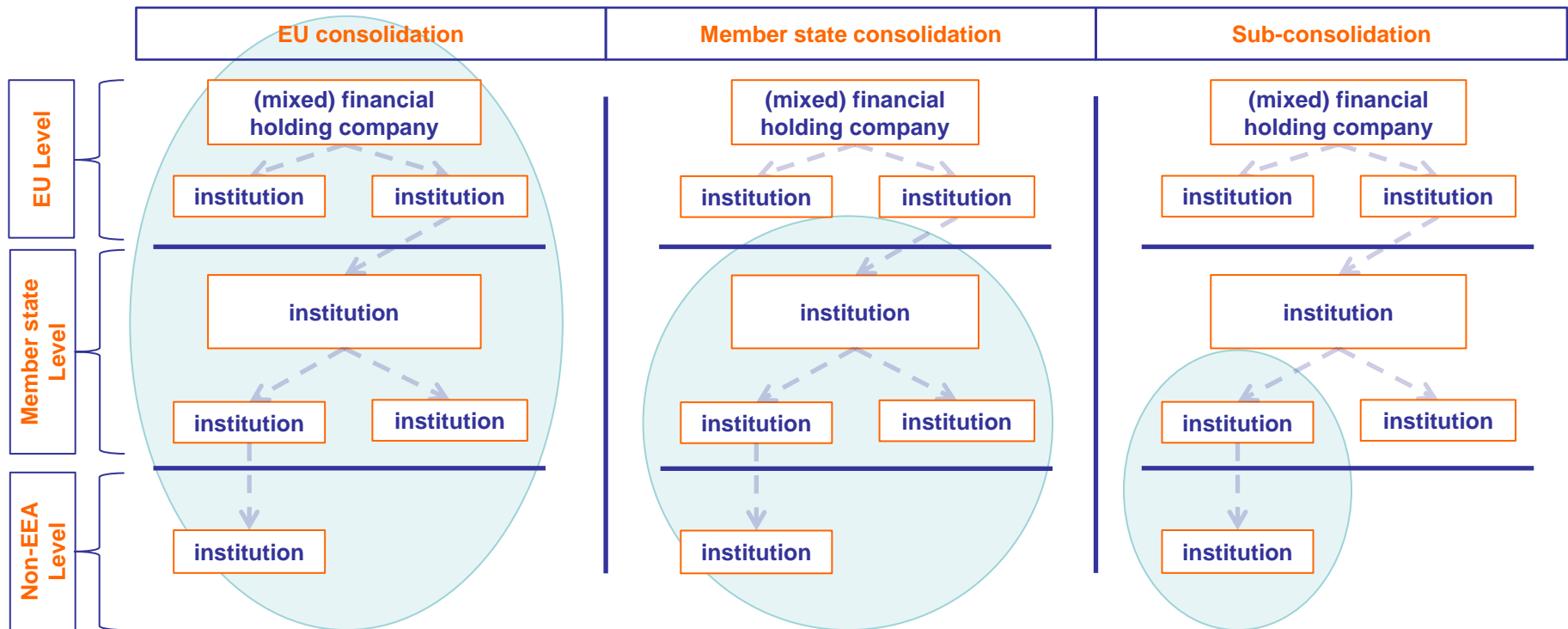
- In essence the SSM Regulation (SSMR) is “only” a re-assignment of the *competent authority* in the CRD
- On significant institutions ECB becomes the supervisor, while other institutions remain under imminent supervision by DNB, subject to SSM policies
- The application of the CRD by the SSM might differ from current supervisory practices, in areas such as:
 - Options, discretions and application of waivers
 - Pillar II and SREP / RAS
 - Reporting
 - Consolidated supervision on top level
- Many more details to be filled in, until 01-10-2014

X. Increased importance of reporting

How do we expect to use data in the next five year?

- Basel III migration monitoring requires data
- Dominant role of EBA increases focus on reporting
- Increased international cooperation demands data
- Prospect of the SSM intensifies data usage
- Review and reports (e.g. on the LR and LCR) will be based on reporting, while our arguments need data
- Dutch tradition in reporting has to develop

XI. Consolidated basis



XII. Consolidated requirements

EU consolidation	Member state consolidation	Sub-consolidation
<p>Consolidated requirements</p> <ul style="list-style-type: none">• Own Funds,• Capital Requirement,• Large Exposures,• Leverage• Liquidity• Disclosure• Exposures to Transferred Credit Risk• CRD requirements<ul style="list-style-type: none">• Governance• Pillar II• Buffer	<p>Consolidated requirements</p> <ul style="list-style-type: none">• Own Funds,• Capital Requirement• Large Exposures• Leverage.• Exposures to Transferred Credit• CRD requirements<ul style="list-style-type: none">• Governance• Pillar II• Buffer	<p>Consolidated requirements</p> <ul style="list-style-type: none">• Capital requirement• Qualified Holdings• Exposures to Transferred Credit Risk• CRD requirements<ul style="list-style-type: none">• Governance• Buffer ?

Reference guide – main provisions

Where can I find CRD IV's main provisions?

Governance	CRD 88	Bpr H3
Risk management + Pillar II	CRD 73 - 87	Bpr H4
ICAAP + ILAAP	CRD 73 + 86	Bpr H4
Definition of capital	CRR 25-88	
Initial own funds	CRD 12+ 29-33	Bpr 48
Capital requirement	CRR 92	
Buffer	CRD 128 -142	Wft + Bpr
Reporting	CRR 99	Bpr + Reg Staten (temp)
Leverage ratio	CRR Part 7	
Liquidity	CRR Part 6	Bpr + Reg. Liquiditeit (temp)
Large exposures	CRR Part 4	
Disclosure	CRR Part 8	

Reference guide – own funds

Provisions concerning the capital requirement

Own funds definition	CRR Part 2: 25 - 88
Capital requirement	CRR Part 3: 92
Credit risk	CRR Part 3: 102 - 300
CR_SA	CRR Part 3: 114 - 141
CR_IRB	CRR Part 3: 142 - 191
CR_CRM	CRR Part 3: 192 - 241
CR_SEC	CRR Part 3: 242 - 270
CR_CCR	CRR Part 3: 271 - 311
Operational risk	CRR Part 3: 312 – 324
Market risk	CRR Part 3: 325 – 379
Settlement risk	CRR Part 3: 380
CVA risk	CRR Part 3: 381 - 384

Reference guide – Dutch law

What happens to DNB's Toezichthouderregelingen?

Regeling beheerst beloningsbeleid	Remains in force
Regeling hybride instrumenten banken en andere financiële ondernemingen	Will be withdrawn
Regeling hybride instrumenten verzekeraars	Remains in force
Regeling liquiditeit	Remains in force for now
Regeling securitisaties	Will be withdrawn
Regeling solvabiliteitseisen kredietrisico	Will be withdrawn
Regeling solvabiliteitseisen marktrisico	Will be withdrawn
Regeling solvabiliteitseisen operationeel risico	Will be withdrawn
Regeling staten financiële ondernemingen	Amendements
Beleidsregels	Will be withdrawn



How to make sense of it?

I. Capital ratio - CRD's key concept

Definition of capital conceptual:

- I. solidity / loss absorption capacity
- II. "distance to default" (measurement)
- III. public disclosure (comparability)
- IV. going and gone-concern concepts

Capital requirements conceptual:

- I. level of public's risk acceptance
- II. demands / expectations
- III. base for public disclosure
- IV. base to compare institutions

$$\frac{\text{Definition of Capital}}{\text{Total Risk Exposure Amount}} \geq \text{Capital Requirement}$$

TREA conceptual:

- I. all risk types managed, measured and quantified in one quantity
- II. proportionate with size and risk
- III. institutions' own risk assessment captured via internal models + ICAAP

Thoughts on solvency supervision:

- I. solvency is primary objective of prudential supervision
- II. own funds requirement is the core of prudential supervision
- III. but not the only means of achieving supervisory goals

II. Basel III and the capital ratio

- Modifications to the definition of capital
- Reclassifications of capital instruments
- Reclassifications of deductions

- Higher requirements (2->4,5% CET1)
- Formalisation of the CET1 requirement
- Addition of capital buffer expectations

$$\frac{\text{Definition of Capital}}{\text{Total Risk Exposure Amount}} \geq \text{Capital Requirement}$$

- Adjustments to risks weights
- Introduction of CVA risk for OTC derivatives
- Modification of the CRR approach to CCP's

- Other changes to Basel III / CRD IV
 - Leverage ratio
 - LCR + NSFR
 - Governance rulebook
 - Enhanced disclosure

III. Elements of the capital ratio

Capital requirements:
Pillar I (4,5/6/8/8%*) + Pillar II

Buffer expectation level:
Buffer on top of Pillar I + Pillar II

Definition of Capital
$$\frac{\text{Total Risk Exposure Amount}}{\geq \text{Capital Requirement}}$$

Pillar I requirements

Elements of Total Risk Exposure Amount (TREA)

- Credit risk – banking book.
- Position risk and LE risk – trading book.
- FX, commodities and settlement risk.
- CVA risk for OTC derivatives.
- Operational risk.
- Counterparty credit risk.

Pillar II risks

Measured and quantified in TREA, at least risk concepts:

- Stress testing (including market risks)
- Concentration risk
- Residual risks from credit risk mitigation
- Securitisation risk
- Liquidity risk
- Diversification (including geographical location)
- Business model risk
- System risk

IV. Two approaches to the ratio

CRD IV hierarchy of requirements

CRD IV capital quality hierarchy

