



**BANK ĊENTRALI TA' MALTA**  
EUROSISTEMA  
**CENTRAL BANK OF MALTA**

## **Consultation Document**

**Consultation on the proposed amendments to  
Directive no.11 on 'Macro-prudential policy'**

**7 December 2020**

**Closing date: 14 December 2020**

*Note: The documents circulated by the CBM for the purposes of consultation are in draft form and consist of proposals. Accordingly, these proposals are not binding and are subject to changes and revisions following representations received from License Holders and other interested parties. It is important that persons involved in the consultation process bear these considerations in mind.*

## **Executive Summary**

The aim of this consultation paper is to consult on amendments proposed to Directive no.11 on 'Macroprudential Policy' issued in terms of the Central Bank of Malta Act (Cap. 204) to transpose elements of the revised Capital Requirements Directive (CRD V) falling under the responsibility of the Central Bank of Malta (CBM).

As per Legal Notice 29 of 2014 (Appointment of Designate Authority to implement Macroprudential Instruments), the CBM is the authority responsible for setting the systemic risk buffer and for identifying the institutions to which it applies; periodically setting the countercyclical capital buffer rate for Malta to be applied by institutions on domestic exposures when calculating their institution-specific countercyclical capital buffer; and for identifying, jointly with the competent authority, global and other systemically important institutions authorised in Malta and the respective applicable capital buffer.

In this regard, with the entry into force of the fourth Capital Requirements Directive (CRD IV) in 2013, the CBM became responsible for transposing provisions relating to capital buffers as specified therein, for credit institutions and investment firms. These provisions were transposed via the drafting of Directive no.11 on 'Macroprudential Policy', which was also published on the CBM's website.

As a result, amendments made to the Capital Requirements Regulation (CRR) and the CRD IV (i.e. CRR II and CRD V), which were published in the Official Journal of the European Union on 7 June 2019, necessitated the need to amend Directive no.11 in order to transpose the applicable provisions relating to the CBM's responsibilities.

Accompanying this consultation paper is a copy of Directive no.11 containing the proposed amendments in tracked changes for ease of reference. Both documents are fundamental to this consultation and should therefore be read in conjunction with each other.

This consultation will run until 14 December 2020, with the Directive becoming applicable as of 28 December 2020.

## 1.0. Introduction

The Basel Committee on Banking Supervision (BCBS) finalised the internationally agreed Basel standards, commonly referred to as Basel III, in 2017.<sup>1</sup> The Basel III Accord is a set of financial reforms that was developed by the BCBS with the objective of strengthening regulation, supervision, and risk management within the banking industry. By building on the previous Accords, i.e. Basel I and II Accords, the Basel III Accord aims to enhance banks' ability to absorb financial shocks while simultaneously strengthening their transparency and disclosure requirements. The finalisation of the Basel III Accord therefore necessitated the need for the revision of the Capital Requirements Regulation (CRR) and the fourth Capital Requirements Directive (CRD IV) of 2013 so as to adopt certain elements of the Basel framework at the EU level.<sup>2,3</sup> As a result, the revised version of the CRR (i.e. CRR II) and the CRD IV (i.e. CRD V) was published in the Official Journal of the European Union on 7 June 2019 and entered into force on 27 June 2019.<sup>4,5</sup> While most provisions of the CRR II automatically apply as of 28 June 2021, those of the CRD V apply once transposed by Member States through the adoption of a national law.

In this regard, the CBM is hereby presenting the main amendments to CBM Directive no.11 on 'Macroprudential Policy' arising from the transposition of CRD V.<sup>6</sup> In light of its mandate of ensuring financial stability, the CBM is the authority designated to develop and construct macroprudential tools, and to issue directives to implement macroprudential policy and the said tools. The CBM is tasked with implementing provisions related to macroprudential instruments as stipulated in the CRR/CRD framework. To this end, the amendments being proposed to Directive no.11 are limited to those provisions that fall within the remit of the CBM, relating specifically to amendments made to existing macroprudential tools in the CBM's macroprudential toolkit.

The CRD V introduces a number of changes and clarifications to the macroprudential toolkit available to both competent and designated authorities. In particular, it provides increased flexibility in the use of macroprudential instruments namely for the application of the systemic risk buffer (SyRB) such that it can be used to address macroprudential or systemic risks not already addressed by other capital buffers. As a result, CRD V provides a clearer delineation of the scope of the SyRB and the buffer for other systemically important institutions (O-SII). In contrast to the CRD IV in which the "higher of"

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<sup>1</sup> Basel Committee on Banking Supervision: Basel III Finalising post-crisis reforms (December 2017). Source: <https://www.bis.org/bcbs/publ/d424.pdf>

<sup>2</sup> Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012. Source: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013R0575&from=en>

<sup>3</sup> 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. Source: <https://eur-lex.europa.eu/legal-content/EN/TXT/PDF/?uri=CELEX:32013L0036&from=EN>

<sup>4</sup> Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012. Source: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019R0876>

<sup>5</sup> Directive (EU) 2019/878 of the European Parliament and of the Council of 20 May 2019 amending Directive 2013/36/EU as regards exempted entities, financial holding companies, mixed financial holding companies, remuneration, supervisory measures and powers and capital conservation measures. Source: <https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=CELEX%3A32019L0878>

<sup>6</sup> Central Bank of Malta Directive no.11 in terms of the Central Bank of Malta Act (Cap. 204) on Macroprudential Policy. Source: <https://www.centralbankmalta.org/centralbankofmaltadirectives>

principle applies, the CRD V stipulates that the SyRB rate is added to the G-SII/O-SII buffer rate on grounds that these buffers will be used to address different types of risks. In the case of the O-SII buffer, the buffer rate cap applicable at parent institution level and at subsidiary level, have both been increased over the levels prescribed under CRD IV.

In addition to the above changes, the CRD V amended the notification procedures of a number of macroprudential instruments and designated the European Systemic Risk Board (ESRB) as the notification hub. In relation to the countercyclical capital buffer (CCyB), the assessment of the CCyB rate and its publication on the designated authority's website, remain on a quarterly basis but an official notification shall only be sent to the ESRB when there is a change in the CCyB rate, rather than on a quarterly basis. Similarly, designated authorities are required to notify the ESRB in case of a reduction in the SyRB rate, and are only subject to additional coordination and authorisation from the European Commission in case of an increase in the SyRB above certain thresholds as specified in CRD V. In this regard, an opinion from the European Commission is required where the combined SyRB rate is between 3% and 5%, while authorisation from the European Commission is required when this exceeds 5%.

In addition, the list of 'other institutions' which are exempt from the scope of CRD V has been updated and includes the Malta Development Bank. In light of the new prudential framework for investment firms, the Investment Firms Regulation (IFR) and Investment Firms Directive (IFD), which entered into force on 25 December 2019, only systemic investment firms as defined in the afore-mentioned regulations will be in scope of Directive no.11.<sup>7</sup>

## **2.0. The proposed amendments to Directive no.11**

As explained in the previous section, the amendments being proposed to Directive no.11 take into consideration revisions made to the CRD in relation to macroprudential instruments which fall under the responsibility of the CBM. In this regard, the table below provides an overview of the main changes proposed between the current text of Directive no.11 and the revised version. Thus, the changes outlined in the below table do not incorporate all the amendments made to Directive no.11. For an exhaustive overview of all changes, one should refer to the document attached to this consultation which presents an amended version of the Directive where proposed insertions/deletions to the current text are outlined in red ink.

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<sup>7</sup> The IFR/IFD framework was published in the Official Journal of the European Union on 5 December 2019 and entered into force on 25 December 2019: Official Journal of the European Union L 314, Volume 62. Source: [http://publications.europa.eu/resource/ellar/ceb0d926-1745-11ea-8c1f-01aa75ed71a1.0006.03/DOC\\_1](http://publications.europa.eu/resource/ellar/ceb0d926-1745-11ea-8c1f-01aa75ed71a1.0006.03/DOC_1)

	<b>Current Directive no.11</b>	<b>Revised Directive no.11</b>
<b>Scope and application</b>	Directive no.11 applies to credit institutions and investment firms.	Directive no.11 applies to credit institutions and to systemic investment firms as per the Investment Firm Regulation and Directive (IFR/IFD).  Directive no.11 does not apply to the Malta Development Bank.
<b>Definitions</b>	Definitions as deemed relevant and as included in the CRR/CRD framework are included.	New definitions in line with the definitions included in the CRR/CRD framework have been included in Directive no.11
<b>Systemic Risk Buffer</b>	The CBM may apply a SyRB of Common Equity Tier 1 capital on all exposures (i.e. for the entire financial sector) or one or more subsets of the financial sector.	The CBM may apply a SyRB of Common Equity Tier 1 capital on all exposures (i.e. for the entire financial sector), on sectoral exposures (for example retail exposures to natural persons secured by residential property, exposures to legal persons secured by commercial immovable property, and any other exposure to legal and natural persons), or on subsets of sectoral exposures as previously specified.  Where the SyRB applies to all exposures, a justification of the non-duplication of the O-SII buffer is to be provided.
	The SyRB is used to prevent and mitigate long-term non-cyclical systemic or macroprudential risks.	The use of the SyRB is now no longer limited to the prevention and mitigation of long-term non-cyclical systemic or macroprudential risks, but can be used to prevent and mitigate macroprudential or systemic risks not covered by the CRR and by the institution-specific CCyB and by the O-SII/G-SII buffer of the CRD.
	No formula on the calculation of the SyRB is provided.	The formula of how institutions shall calculate the SyRB taking into consideration the potential of different SyRB rates applicable to different sectors and exposures, as stipulated in CRD V is included.
	Before setting a SyRB up to 3%, the CBM is required to notify the European Commission, the ESRB, the EBA and the authorities of the Member States concerned, one	Where the setting of a SyRB on any set or subset of exposures does not result in a combined SyRB higher than 3%, the CBM is required to notify the ESRB

	month before publication of the decision.	one month before publication of the decision.
	Where the SyRB is set between 3% and 5%, the CBM is required to notify the European Commission and await for an opinion before implementing it.	Where the setting of the SyRB on any set or subset of exposures results in a combined SyRB between 3% and 5%, the CBM is required to request an opinion from the European Commission before implementing it.
	Before setting a SyRB higher than 5%, the CBM is required to notify the European Commission, the ESRB, the EBA and the authorities of the Member States concerned one month before publication of the decision.	Where the setting of the SyRB on any set or subset of exposures results in a combined SyRB rate higher than 5%, the CBM is required to seek authorisation from the European Commission before implementing it.
	The higher buffer applies in case where an institution is subject to a G-SII/O-SII buffer and a SyRB.	The SyRB is cumulative to the G-SII/O-SII buffer provided that these buffers address different risks.
<b>Global and Other Systemically Important Institutions</b>	An O-SII may be an EU parent institution, an EU parent financial holding company, an EU parent mixed financial holding company or an institution.	An O-SII may be an institution or a group headed by an EU parent institution, an EU parent financial holding company, an EU parent mixed financial holding company, a parent institution in a Member State, a parent financial holding company in a Member State or a parent mixed financial holding company in a Member State.
	CBM, jointly with the competent authority, may require O-SIIs to maintain an O-SII buffer up to 2% of the total risk exposure amount.	CBM, jointly with the competent authority, may now require O-SIIs to maintain an O-SII buffer up to 3% of the total risk exposure amount.
	Domestic Authorities are not allowed to set an O-SII buffer at a level higher than 2%.	Domestic Authorities may require each O-SII to maintain an O-SII buffer higher than 3% subject to authorisation from the European Commission.
	When setting an O-SII buffer at a level up to 2%, the CBM, jointly with the competent authority, is required to notify the European Commission, the ESRB, the EBA, and the authorities of the Member States concerned one month before the publication of the decision on its website.	When setting an O-SII buffer at a level up to 3%, CBM, jointly with the competent authority, is required to notify the ESRB one month before publication of the decision on its website.
	Domestic Authorities are not allowed to set an O-SII buffer at a level higher than 2%.	Where the O-SII buffer is set at a level higher than 3%, CBM, acting jointly with the competent authority, is required to notify the ESRB three

		months before publication of the decision on its website.
	Where an O-SII is a subsidiary of either a G-SII or an O-SII which is an EU parent institution and subject to an O-SII buffer on a consolidated basis, the buffer that applies at individual or sub-consolidated level for the O-SII shall not exceed the higher of: (a) 1% of the total risk exposure amount; and (b) the G-SII or O-SII buffer rate applicable to the group at consolidated level.	Where an O-SII is a subsidiary of a G-SII or an O-SII which is an institution or a group headed by an EU parent institution and subject to an O-SII buffer on a consolidated basis, the buffer that applies on an individual or sub-consolidated level shall not exceed the lower of: (a) the sum of the higher of the G-SII or the O-SII buffer rate applicable to the group on a consolidated basis and 1 % of the total risk exposure amount; and (b) 3% of the total risk exposure amount, or the rate the Commission has authorised to be applied to the group on a consolidated basis.
	Where a group, on a consolidated basis is subject to a G-SII buffer and an O-SII buffer, or a G-SII buffer, an O-SII buffer and a SyRB, the higher buffer shall apply.	Where a group, on a consolidated basis, is subject to a G-SII buffer and to an O-SII buffer, the higher buffer shall apply.
	Where an institution, on an individual or sub-consolidated basis is subject to an O-SII buffer and a SyRB, the higher of the two shall apply.	Where an institution is subject to a SyRB, that buffer shall be cumulative with the O-SII buffer or the G-SII buffer.
<b>Countercyclical capital buffer</b>	CBM is required to assess the appropriateness of the CCyB rate on a quarterly basis.	CBM is required to assess the intensity of cyclical systemic risk and the appropriateness of the CCyB rate on a quarterly basis and adjust it if necessary.
	CBM is required to notify each quarterly setting of the CCyB rate to the ESRB.	CBM is required to notify each change of the CCyB rate to the ESRB and may thus not necessarily be on a quarterly basis.
<b>General</b>		Inclusion of new paragraphs relating to the use of Common Equity Tier 1 capital in meeting the combined buffer requirement, such that institutions do not use Common Equity Tier 1 capital that is maintained to meet one of the elements of its combined buffer requirement to meet the other elements of such requirement.

### **3.0. Coming into force**

The amended Directive no.11 shall be applicable as of 28 December 2020.

### **4.0. Contacts**

Any comments and feedback in relation to the attached draft proposed amended directive are to be submitted in writing to Mr. Stephen Attard and Ms. Christine Barbara on [directive11consultation@centralbankmalta.org](mailto:directive11consultation@centralbankmalta.org), by not later than 14 December 2020, in line with a one-week long consultation period. The CBM reserves the right to disregard any responses sent after the said date.