



EUROPEAN CENTRAL BANK

EUROSYSTEM

ECB response to the European Commission's call for advice on the review of the EU macroprudential framework

March 2022



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1 Executive summary

The European Central Bank (ECB) welcomes the opportunity to provide input to the European Commission’s Call for Advice (CfA) on the review of the EU macroprudential framework. The COVID-19 pandemic highlighted the fact that a comprehensive set of policies is necessary to address large and disruptive shocks to the financial system. The EU banking system proved resilient and continued to support the real economy during the crisis. This was due to: (a) the increased levels of resilience achieved thanks to the regulatory reforms put in place after the Global Financial Crisis; (b) implementation of micro- and macroprudential policies; (c) the extraordinary fiscal, monetary and prudential support measures put in place. Macroprudential policy is a crucial component of this mix, as it helped stabilise the provision of key services by giving capital relief to the banking sector. The pandemic also brought to the fore areas for improvement in the design and functioning of the macroprudential framework. The ECB’s advice aims to support the legislative process to address the shortcomings identified in the review of the EU macroprudential framework. Finally, the ECB supports full, timely and consistent implementation of the final Basel III standards agreed by the Basel Committee on Banking Supervision in EU legislation. These reforms will further enhance the resilience and stability of the financial system.

The review of the EU macroprudential framework was preceded by the ECB’s monetary policy strategy review, which emphasised that financial stability is a precondition for price stability and vice versa. This recognised that in view of the price stability risks generated by financial crises, there is a clear conceptual case for the ECB taking financial stability considerations into account in its monetary policy deliberations. The review also stressed that monetary policy is not primarily responsible for guaranteeing financial stability; macroprudential policies (together with microprudential policies and financial regulation) remain the first line of defence against financial stability risks. Monetary policy and macroprudential policy pursue their respective statutory objectives of price stability and financial system stability and in doing so are in most cases complementary. Monetary policy may affect financial stability risks: in one direction, accommodative monetary policy can reduce credit risk by boosting activity levels; in the other direction, accommodative monetary policy may encourage the build-up of leverage or affect asset prices. In a similar vein, macroprudential policies have implications for price stability; for instance, measures that avoid a build-up of imbalances reduce the likelihood of future financial crises with negative effects on price stability. The interplay between monetary and macroprudential policies strengthens further the case for enhancing the effectiveness of the macroprudential framework in the EU.

The ECB response covers the four broad areas included in the CfA: the overall design and functioning of the buffer framework, missing and obsolete instruments, internal market considerations and global risks. The CfA reflects the Commission’s mandate to complete a review of the macroprudential provisions in

the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD) by June 2022 and, if appropriate, to submit a legislative proposal to the European Parliament and the Council by December 2022. As a result, the proposals and considerations included in this response focus on the provisions contained in the CRR and the CRD. The response also offers some reflections on global risks, inspired by the relevant section of the CfA, but does not contain any concrete proposals on other EU legal acts, e.g. relating to non-banks; nor does it discuss institutional and governance arrangements not covered by the CRR and CRD. However, given the interactions between the resolution and macroprudential frameworks (e.g. on information exchange), the reviews of both frameworks should be aligned. Finally, the response includes an annex that provides analytical and, where possible, empirical analyses underpinning the proposals (Annex 1). It is accompanied by a background document on specific policy options to enhance macroprudential space in the banking union and the European Union (Annex 2).

Regarding the revision of the capital buffer framework, the ECB has three sets of proposals (see Section 2):

First, the ECB supports creating additional macroprudential policy space – in the form of a higher amount of releasable capital buffers – to enhance the ability of the financial system to withstand large, systemic shocks by better enabling banks to absorb losses while maintaining the provision of key financial services to the real economy. The ECB highlights the importance of increasing the availability of releasable capital buffers to enhance macroprudential authorities' ability to address large and disruptive systemic shocks that may go beyond the unwinding of domestic imbalances and may hit (large parts of) the banking union simultaneously. The ECB has identified a number of policy options that could be pursued: (a) a fully or partially releasable capital conservation buffer (CCoB); (b) a positive neutral rate for, or more active use of, the countercyclical capital buffer (CCyB); (c) a core rate for the releasable systemic risk buffer (SyRB), or a possible mix of these policy options (see also Annex 2). The ECB response thoroughly discusses the advantages and disadvantages of the three policy options, aiming to reflect a balanced overview of the opinions of the authorities in the banking union, but does not establish a hierarchy of options or recommend one specific option in view of the EU macroprudential review. Moreover, some authorities consider the present framework flexible enough to create higher releasable capital buffers. Beyond the option to increase the amount of releasable capital buffers, the ECB favours increasing the usability of buffers which are not releasable. The ECB supports strengthening the features of Additional Tier 1 (AT1) instruments to reduce the stigma effects associated with banks cancelling AT1 coupon payments when they fall beneath the level of their combined buffer requirements. The challenges associated with market perceptions of the features of AT1 instruments point to a more fundamental concern over the complexity of the capital framework; the ECB supports further work at the international level to consider ways of reducing the overall complexity of the prudential regime.

Second, the ECB suggests increasing the flexibility and effectiveness of the CCyB framework by supporting timelier activation in the build-up phase and

release in stress periods. The ECB supports strengthening the role of other quantitative cyclical indicators that could be considered when setting a CCyB rate, reducing the prominent role of the credit-to-GDP gap.¹ The ECB also suggests clarifying the CRD provisions on the implementation of the CCyB (e.g. allowing multiple decisions within a quarter, or applying a shorter transitional period if justified by the circumstances), which would increase the flexibility of the framework.

Third, the ECB suggests enhancing information exchange between resolution, competent and designated authorities. This would allow them to exercise their respective mandates in an effective and timely manner, including for macroprudential policy and financial stability analysis. Looking ahead, the ECB sees merit in further assessing the interactions between the prudential and resolution frameworks, given their implications for the functioning of the buffer framework. The ECB suggests that in the subsequent review of the EU's macroprudential policy framework the Commission, after consulting the ESRB, should assess whether the leverage ratio and the minimum requirement for own funds and eligible liabilities (MREL) present material obstacles to buffer usability, due to multiple use of capital for buffers and minimum requirements.

Fourth, the ECB does not support extending leverage buffers to O-SIIs at this stage. O-SII leverage buffers would strengthen the resilience of a small number of these institutions at the current juncture. However, introducing them might decrease the usability of releasable buffers in the risk-based framework and increase potential procyclical adjustments.² In the subsequent review of the EU's macroprudential rules the Commission, after consulting the ESRB and the EBA, should assess whether additional leverage buffers need to be introduced.

Regarding missing and obsolete instruments, the ECB has three main proposals (see Section 3):

First, the ECB supports introducing a data collection requirement for a minimum set of common lending standard indicators for residential real estate (RRE) loans for monitoring purposes. These lending standards indicators should be based on the common definitions in ESRB Recommendation 2016/14.³ The objective is to enhance the comparability of both risk assessments and, indirectly and gradually, prudential policy stances on borrower-based measures (BBMs) in the RRE sector across jurisdictions, supporting financial stability surveillance in the EU. It is important that the activation, design and calibration of macroprudential limits to lending standard indicators, i.e. BBMs, should remain within the remit of national authorities, to effectively address the risks identified and account for national specificities given the heterogeneity across national mortgage and real estate markets. The data collection requirements would not constrain national authorities

¹ These indicators could be complemented by qualitative information, ESRB guidance and expert judgement.

² This reflects the fact that, given their structural nature, an O-SII leverage buffer would not be releasable and assumes that banks' reluctance to dip into their risk-weighted capital buffers extends to leverage buffers too. The above results should be reassessed once MREL is fully phased in, as it may have implications on the magnitude of the impact.

³ [Recommendation of the European Systemic Risk Board of 31 October 2016 on closing real estate data gaps \(ESRB/2016/14\)](#) (OJ C 31, 31.1.2017, p. 1).

from using national definitions aligned with domestic specificities or collecting an even broader set of lending standard indicators to inform policy, including the application of BBMs at the national level.

Second, the ECB proposes consolidating all macroprudential risk weight measures for real estate into a single article. This would streamline the various legal provisions on regulatory risk weight adjustments for real estate and disentangle macroprudential and microprudential provisions. Moreover, consolidating the different provisions allowing risks weights to be tightened to address real estate risks would establish a consistent administrative procedure that would facilitate macroprudential policy action while ensuring the integrity of the Single Market for measures with a more material impact.

Third, the ECB does not at this stage support the introduction of the power to impose binding system-wide restrictions on distributions at Union and/or national level in the CRR/CRD. Limiting distributions is a way for banks to retain their capacity to absorb losses and ability to continue providing credit in times of crisis. The relevant recommendations by EU institutions, including the ECB, and the corresponding national actions, proved effective during the COVID-19 crisis. These measures were of an exceptional and temporary nature, reflecting the extraordinary uncertainty that the banking sector faced at the outset of the pandemic. Introducing the power for authorities to impose system-wide restrictions on distributions might signal that these measures could occur more frequently in future, which could have a negative impact on banks' valuations and limit their ability to raise capital. Such effects could be particularly pronounced if the EU were to take this step unilaterally, without other major jurisdictions introducing similar powers for their authorities.

Regarding internal market considerations, coordination mechanisms and procedures, the ECB has the following main proposals (see Section 4):

First, the ECB suggests mandating the EBA, in consultation with ESRB, to issue guidelines on a revised methodology for O-SII identification and buffer calibration. The proposal aims to further reduce the risk of unjustified heterogeneity in the setting of O-SII buffers and to develop a common methodology that would lead to a more consistent treatment across the EU. The EU-wide guidance would need to be flexible to ensure that national specificities, new developments and insights can be reflected appropriately.

Second, the ECB suggests mandating the ESRB to report on identifying systemic risks for the purposes of setting the SyRB and, if appropriate, to issue a recommendation to designated authorities on the application of the SyRB on the basis of this report. Differences in the current approaches to implementing the SyRB in the EU are justified to some extent by its use to address country-specific systemic risks, but they indicate there is a possibility of systemic risks being treated unevenly across countries. An ESRB report would support improving the consistency of treatment in addressing systemic risks within the EU, without constraining use of the SyRB as a flexible tool to cover both risks not mitigated by other tools and any new systemic risks that may emerge in future. On

the basis of this report, the ESRB could issue a recommendation to designated authorities, if considered appropriate.

Third, the ECB suggests streamlining the procedures governing national flexibility measures set out in Article 458 CRR. Targeted amendments could streamline the authorisation and extension procedures for Article 458 measures by (a) indicating that they can be implemented in cases when systemic risks remain elevated, and not only when an increase in the intensity of the systemic risk has been identified; (b) clarifying the scope of the assessments performed by the ESRB and EBA under their institutional mandates; (c) enabling the ESRB to take existing assessments of systemic risks for participating Member States into consideration; (d) replacing the current recurring mandatory comprehensive assessment by the ESRB, the EBA and the Commission with a simplified non-objection approach to extending an existing measure under Article 458.

Fourth, the ECB suggests revising the rules on calculating the thresholds for the sectoral SyRB and the interaction between the systemic risk buffer (SyRB) and the capital buffers for global and other systemically important institutions (G/O-SIIs). The ECB suggests converting the sectoral and general SyRB rates to a common denominator, the total risk exposure amount (TREA), before applying the additivity rules and thresholds triggering EU governance procedures. This proposal aims at establishing a consistent approach, with a view to eliminating adverse incentives that could discourage implementation of the sectoral SyRB. Moreover, it ensures that EU governance procedures will relate to the impact of these measures on the Single Market, while avoiding placing an undue burden on EU authorities for measures with a limited capital impact.

Regarding global risks, the ECB sees the rationale for removing the CRD provisions on third-country CCyB rates, given the significant challenges to activating this instrument and the high coordination costs related to its exposure-based nature. The SyRB can be used to address third-country risks in a broader context than that of the third-country CCyB, without this constituting a unilateral decision by an EU authority to increase the rate of a macroprudential instrument that is part of the third country toolkit. With regard to market-based finance, the ECB does not at this stage see any need for a regulatory change in the macroprudential toolkit for banks to address the risk of exposures to non-banks. However, the ECB supports strengthening the regulatory framework for non-banks, including from a macroprudential perspective. This should include limiting liquidity risk in both money market and open-ended funds as well as the procyclicality of derivative margins. Mandatory holdings of public debt and increased weekly liquid asset requirements for private debt funds would enhance their shock-absorbing capacity. In addition, liquidity buffers for money market funds should be made more practical and authorities should have a role in directing their use. Finally, the ECB stresses the unique features of climate-related and broader environmental risks and is actively participating in the debate on designing policy measures to capture them. Any evidence-based assessment may well extend beyond the completion of the EU macroprudential framework review; however, the Commission could consider inserting any related proposals into EU law separately but in a timely manner, after

consulting the ESRB and ECB. Finally, with regard to cyber risk, given the relatively early stage of analysis, the ECB may consider macroprudential policy proposals at a later stage.

2 Overall design and functioning of the buffer framework from the macroprudential perspective

2.1 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?

Enhancing macroprudential policy space in the form of higher releasable buffers

1. **The ECB suggests increasing the amount of releasable capital buffers to enhance macroprudential authorities' ability to address large and disruptive systemic shocks that may go beyond the unwinding of domestic imbalances and may hit (large parts of) the banking union simultaneously.**
2. **To operationalise the first proposal, the ECB suggests pursuing one of the specific policy options to increase the amount of releasable capital buffers in the banking union (and the European Union). These include: (a) a fully or partially releasable capital conservation buffer (CCoB); (b) a positive neutral rate for, or more active use of, the countercyclical capital buffer (CCyB); (c) a core rate for the releasable systemic risk buffer (SyRB), or a possible mix of these policy options.**

The banking system proved to be resilient and continued to perform its fundamental functions throughout the COVID-19 pandemic, in part due to the extraordinary fiscal, monetary, and prudential support measures that were put in place. To date, no significant losses occurred within the banking sector and banks continued to provide credit and other critical services to the real economy.

Macroprudential policy helped stabilise the provision of key services by providing capital relief to the banking sector. Although prudential measures were taken promptly and decisively by authorities around Europe and the globe, the recent experience of the pandemic has raised questions as to (a) whether there is sufficient releasable capital in place to address future systemic shocks, and (b) whether the ability of macroprudential authorities to act in a coordinated and predictable manner under very adverse circumstances (particularly in the form of a large and disruptive systemic shock that hits (large parts of) the banking union simultaneously) should be further strengthened.

The case for, and specific policy options aimed at, operationalising an increase in the amount of releasable capital buffers have been discussed by

the ECB's Macprudential Forum, the final report of which is annexed to this reply as a background document. The report develops and analyses specific policy options that could enhance macroprudential authorities' ability to address large and disruptive systemic shocks by increasing the amount of releasable capital buffers. Capital buffers are a key element of the Basel framework and are designed to be usable by banks to absorb losses while maintaining the provision of key services to the real economy in a downturn. Although downward portfolio adjustments by individual banks did not result in credit supply constraints at the aggregate level, not least due to the formidable policy support provided by authorities during the pandemic, some micro-level analysis suggests that current bank capital buffers may not be fully usable for these purposes (in the sense of banks being willing to use them; this is separate from their ability to do so, which may also be constrained by parallel regulatory requirements).⁴ The potential reluctance of banks to use their buffers when needed has reinforced a debate on the case for a greater amount of releasable capital buffers. When released, these allow banks to operate at lower capital ratios without breaching a regulatory threshold, thus addressing some of the possible impediments to the use of buffers and helping to avoid potential procyclical adjustments and harmful deleveraging.

The policy options set out in the annexed report are meant to further strengthen the current macroprudential framework, which mainly includes releasable capital buffers to address cyclical systemic risk relating to excessive credit growth. As illustrated by the pandemic, regardless of country-specific financial or economic cycles, having effectively releasable macroprudential buffers available might be helpful in addressing large and disruptive systemic shocks that may go beyond the unwinding of domestic imbalances and may hit (large parts of) the EU or the banking union simultaneously (even though the effects of the pandemic on Member States and their banking system were heterogeneous). In particular, the possibility of disruptive shocks such as the one induced by the coronavirus creates uncertainty for the financial system, where it is not possible to precisely define their expected nature or magnitude before they occur. When these systemic shocks hit, the availability of releasable and effectively usable capital buffers can enhance financial system resilience by enabling banks to better absorb losses while maintaining the provision of key financial services to the real economy, in line with the objectives of the capital buffer framework.

The report includes three separate policy options: (a) a fully or partially releasable capital conservation buffer (CCoB); (b) a positive neutral rate for, or more active use of, the countercyclical capital buffer (CCyB); (c) a core rate for the releasable systemic risk buffer (SyRB). It also discusses the possibility of mixing or combining these options. The options are assessed against five broad criteria: financial system resilience, Basel compliance, capital neutrality, European

⁴ See Annex 1 and, e.g., Basel Committee on Banking Supervision (2021), "[Early lessons from the Covid-19 pandemic on the Basel reforms](#)", Bank for International Settlements, Basel, July; Berrospide, J., Gupta, A. and Seay M. (2021), "[Un-used Bank Capital Buffers and Credit Supply Shocks at SMEs during the Pandemic](#)", *Finance and Economics Discussion Series*, 2021-043, Federal Reserve Board, Washington, D.C., April; Couaillier, C., Lo Duca, M., Reghezza, A., Rodriguez d'Acri, C. and Scopelliti, A. (2021), "[Bank capital buffers and lending in the euro area during the pandemic](#)", *Financial Stability Review*, Special Feature, ECB, Frankfurt, November.

governance, and simplicity. Further consideration and background on each of the criteria is provided in the annexed report. For some of the criteria – notably capital neutrality and European governance – views differ on how they should be interpreted and whether meeting them is even desirable. Meeting all criteria simultaneously is challenging, if not impossible. The report does not aim to generate a ranking between the options and does not put a weighting on the relative importance of the different criteria, since views on these aspects are very divergent. It thoroughly and transparently evaluates the benefits and challenges of each option, assessed against the criteria. A quantitative assessment of the effects of the options following a large systemic shock is provided in Section 2 of Annex 1.

While there is broad agreement on the usefulness of increasing the amount of releasable buffers, discussions among the relevant authorities in the banking union have shown that preferences on the specific policy options vary widely across jurisdictions. Different authorities attach different weights to the importance of individual criteria, implying that no option has emerged as the single most preferred variant. The report thoroughly discusses the advantages and disadvantages of the three policy options, aiming to reflect a balanced overview of the opinions of the authorities in the banking union, but does not establish a hierarchy of options or recommend one specific option in view of the EU macroprudential review. Moreover, some authorities consider the present framework flexible enough to create higher releasable capital buffers. Considering the different views, the report also discusses the possibility of mixing or combining elements of the various policy options. There is no consensus that a mixed option would be preferable to any of the individual ones, as preferences are equally divergent in this respect, too. Nevertheless, the possibility of mixing different options may increase the degrees of freedom to a certain extent and could hence be analysed further.

Increasing the usability of non-releasable buffers

Beyond the policy options to increase the availability of releasable capital buffers discussed in the annexed report, there is a need to consider ways of improving the usability of buffers that are not released. Market intelligence and bank-specific anecdotal evidence suggest a widespread perception among market participants that cancelling coupon payments on AT1 instruments is expected only as a last resort when the bank is already likely to fail.⁵ As the ECB has noted,⁶ credit institutions might not be willing to use their buffers for additional lending due to concerns about being obliged to cancel AT1 coupons and face potentially negative reactions from market participants. To remedy this, there is a need to strengthen the ability of AT1 to act as going concern capital, specifically regarding the flexibility of payments. In particular, the CRR definition of “distributable items”, recently amended by the CRR2, should be reviewed to ensure that only profitable banks or banks with positive retained earnings could make AT1 coupons / CET1 dividends payments.

⁵ See “[Early lessons from the Covid-19 pandemic on the Basel reforms](#)”, Basel Committee on Banking Supervision, 6 July 2021.

⁶ [Opinion of the European Central Bank of 20 May 2020 on amendments to the Union prudential framework in response to the COVID-19 pandemic \(CON/2020/16\)](#) (OJ C 180, 29.5.2020, p.4).

Improvements could also be made to loss absorption in the going concern perspective (e.g. requiring accounting classification as equity, removing the need for obsolete automatic triggers⁷) and permanence (e.g. by limiting the possibility to call the instrument only if replaced with a CET1 instrument or a cheaper AT1 instrument⁸). The Commission should also carefully analyse the impact of such amendments on the loss-absorbing capacity of AT1 instruments and assess whether the role of these capital instruments in the capital buffer framework should be reconsidered.

The challenges associated with market perceptions of the features of AT1 instruments point to a more fundamental concern over the complexity of the capital framework. Since the Global Financial Crisis, new international standards for microprudential regulation, macroprudential policy and crisis management regimes have substantially increased the overall resilience of the banking sector. However, one potential negative side effect is an overall increase in the level of complexity of capital regulation. This can inhibit efficient supervision and poses a risk to the effectiveness of macroprudential policy if it makes it difficult for public authorities, banks, and market participants to understand which requirements will be binding at different points in time. The complexity of international standards in the EU results from the existence of multiple parallel requirements (risk-based and non-risk-based) in both the going and gone concern frameworks (see Section 2.3). It also stems from the layering of the resolution requirements – total loss-absorbing capacity (TLAC) and MREL – on top of prudential rules which already require banks to maintain resources that absorb losses only in gone concern.⁹ As set out in Section 2.3, the ECB advocates reviewing in the next macroprudential review whether overlapping leverage ratio and MREL requirements present material obstacles to buffer usability. In preparation for that review, the ECB also supports further work at the international level to consider ways of reducing the overall complexity of the prudential regime.

2.2 Is there scope for making the buffer framework more effective in smoothing 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?

As discussed in reply to question 2.1, a greater amount of releasable capital buffers could strengthen macroprudential authorities' ability to address future systemic shocks, including large and disruptive systemic shocks that go

⁷ See CAP10.11(11), where a minimum trigger of 5.125% is required for instruments classified as liabilities for accounting purposes. The current minimum level of triggers is far below the point of non-viability: to be credible (if kept), they should be set at a level where the write-down or conversion takes place before the institution is declared failing or likely to fail.

⁸ Reinforcing current provisions against market expectation that AT1 is called.

⁹ Tier 2 capital is explicitly designed only to absorb losses on a going concern basis; for the reasons mentioned above, AT1 is also not currently viewed as able to absorb losses before the point of non-viability has been reached.

beyond the unwinding of domestic imbalances. Specific policy options for how this objective could be achieved are outlined in Section 2.1 and discussed in detail in the attached background document. In addition and separately to those considerations, a number of targeted adjustments to existing instruments would also be beneficial in making the buffer framework more effective in smoothing financial and economic cycles through both pre-emptive and timely build-up of additional resilience in the EU banking system and the timely release of buffers.

The countercyclical buffer

- 3. The ECB suggests amending the CRD to clearly indicate that the credit-to-GDP gap (and the buffer guide) is only one quantitative indicator among several that designated authorities (DAs) have to take into account when setting a CCyB rate.**
- 4. The ECB suggests clarifying the CRD provisions to clearly indicate that a decision on the CCyB rate adopted for a given quarter does not prevent a DA from subsequently lowering that rate fully or again later in the quarter if justified by prevailing circumstances.**
- 5. The ECB suggests amending the CRD to allow a shorter transitional period when increasing the CCyB rate if deemed necessary by DAs, by removing the reference to exceptional circumstances.**

The current wording of the CRD gives the buffer guide, and the credit-to-GDP gap on which it is based, a prominent role. The credit-to-GDP gap is broadly considered to have provided good early warning signals for past systemic banking crises and enables comparability across jurisdictions. However, the indicator has several shortcomings in informing the CCyB calibration: it tends to have a downward bias after periods of prolonged credit expansion and is sensitive to the length of the time series available for computing it. This is supported by ECB research,¹⁰ which suggests that other indicators can perform better in providing early warning of looming financial crises.

The ECB therefore proposes to reduce the prominent role of the credit-to-GDP gap by making it just one cyclical risk indicator among others that guide the setting of CCyB. The amended Article 136 CRD could specify that the buffer guide based on the credit-to-GDP gap is to be considered along with all other relevant cyclical quantitative indicators. These would then be complemented and used together with any other available qualitative information, the ESRB guidance and

¹⁰ Detken C. et al. (2014), “Operationalising the countercyclical capital buffer: indicator selection, threshold identification and calibration options”, *Occasional Paper Series*, No 5, European Systemic Risk Board, Frankfurt, June; and Lang J.H., and Welz, P. (2017), “Measuring credit gaps for macroprudential policy”, *Financial Stability Review*, Special Feature, ECB, Frankfurt, May.

expert judgment to guide and inform the final setting of a CCyB rate.¹¹ This would facilitate the pre-emptive and timely build-up of additional resilience in the EU banking system, while maintaining compliance with the Basel framework. A timely and sufficient build-up of a CCyB would also facilitate loss absorption by EU banks, without breaching regulatory requirements or reverting to procyclical deleveraging with negative effects on the real economy.

The ECB is of the view that the CRD text should make explicit reference to the possibility of taking more than one quarterly decision on the CCyB rate, to enable the full or partial release of the CCyB on the basis of prevailing circumstances. Currently, DAs assess the intensity of cyclical systemic risk and the appropriateness of the CCyB rate on a quarterly basis and set or adjust the CCyB rate if necessary. However, a sudden and unexpected shock could render the assessment of cyclical systemic risks and the corresponding decision on a CCyB rate irrelevant. In these situations, it is of particular importance that DAs are able to react in a timely manner and adjust macroprudential policy by revising the CCyB rate downwards or releasing it fully. Clarifying the relevant CRD provisions would also better align them with the objectives of the CCyB. This proposal reflects decisions on the CCyB rate taken by the DAs of certain Member States at the outbreak of the COVID-19 crisis.

The ECB considers that the period for implementing decisions to set or increase a CCyB rate could be shorter than 12 months if deemed necessary and appropriate by DAs, even in the absence of exceptional circumstances. This will enable DAs to assess whether there is a need to implement CCyB decisions earlier, while still allowing enough time for the institutions affected to build up the buffer. Removing the reference to exceptional circumstances will allow authorities to set a shorter period for the implementation of an increase in a CCyB even in normal times, where this is sufficiently justified and appropriate. DAs should take the impact on banks into account and ensure they are able to accommodate the capital increase resulting from earlier implementation of the CCyB in their capital planning. They should also ensure that the shorter implementation period does not unduly constrain credit to the real economy. Overall, the ECB is of the view that this measure would support adjusting the CCyB in a timely manner, mitigate the aggravation of cyclical systemic risks and strengthen the functioning of the financial system.

2.3 Is there need and scope for redesigning the macroprudential buffer framework in view of its

¹¹ For a description of the indicators used at the ECB to measure the build-up of cyclical systemic vulnerabilities, see: Detken C., Fahr, S. and Lang, J.H. (2018), “Predicting the likelihood and severity of financial crises over the medium term with a Cyclical Systemic Risk Indicator (CSRI)”, *Financial Stability Review*, Special Feature, European Central Bank, Frankfurt, May; also the analytical apparatus in Constâncio V. et al. (2019), “Macroprudential policy at the ECB: Institutional framework, strategy, analytical tools and policies”, *Occasional Paper Series*, No 227, ECB, Frankfurt, July. The CSRI is available for all euro area countries and provides information on the medium-term likelihood and severity of financial crises which clearly surpasses the Basel credit gap in terms of predicting financial crises and large recessions.

interaction with other capital requirements (leverage ratio minimum requirements, minimum requirements for own funds and eligible liabilities (MREL)), and if so, how?

6. **The ECB suggests introducing targeted amendments to the BRRD and the CRD specifying that resolution, competent and designated authorities shall on request provide each other with all information relevant for the exercise of their respective mandates, including for the purposes of macroprudential policy and financial stability analyses. This information exchange should also include macroprudential authorities and central banks with a financial stability mandate, where different from the authorities mentioned above.**
7. **The ECB suggests inserting a clause to the effect that in the subsequent review of the EU's macroprudential framework, after consulting the ESRB the Commission should assess whether the leverage ratio and MREL present material obstacles to buffer usability. If obstacles are deemed material, the Commission is invited to consider mitigating options.**

Authorities should be able to assess the overlap of the leverage ratio and MREL requirements with the combined buffer requirement (CBR), but the necessary data might not be available to authorities. These two items are important elements of the regulatory framework and contribute to the resilience and resolvability of the EU banking sector; they are also relevant from a financial stability perspective. Their introduction led, however, to an increase in the complexity of the interaction between different regulatory frameworks; for instance, risk-weighted capital buffers can be counted towards non-risk-weighted MREL requirements. Authorities involved in setting macroprudential buffers and analysing financial stability need to be able to review buffer usability, distance to breaches¹² and the interplay of different regulatory objectives. Bank-specific information on all applicable requirements and the resources eligible to meet them should therefore be available to both micro- and macroprudential authorities¹³ and resolution authorities.¹⁴ However, the ESRB has concluded that “macroprudential authorities or designated authorities, especially if they are not also competent authorities, might not have access to all necessary supervisory data, data on MREL requirements and resources.”¹⁵ Any information gaps at the national level might affect the effectiveness of policymaking, therefore the ECB considers it important that these gaps be closed. It would be beneficial to anchor the expectation of this information

¹² Distance to breach refers to how large a capital surplus a bank has above its combined buffer requirement or minimum requirements. This distance is different for risk-based, leverage and MREL requirements. The severity of the consequences of breaches also differ. Breaching buffer requirements has less severe consequences than breaching minimum requirements.

¹³ Competent and designated authorities are defined by the CRR and CRD; macroprudential authorities are defined in [Recommendation ESRB/2011/3](#) (OJ C 41, 14.2.2012, p.1).

¹⁴ Extended public disclosure by banks to allow holistic analysis of a bank's position compared to requirements could be considered, to facilitate the use of disclosure data by market participants and academia. The current disclosure templates may be too complicated to capture the extent to which the constraints are having an effect.

¹⁵ ESRB (2021), [Report of the Analytical Task Force on the overlap between capital buffers and minimum requirements](#), Frankfurt, December.

sharing directly in EU law, so national law and inter-institutional memoranda can implement it in the specific national context.

The ECB has identified three main data gaps regarding access to information at a national level. First, competent authorities do not necessarily have access to MREL requirements. Second, designated authorities as well as macroprudential authorities and central banks with a financial stability mandate do not necessarily hold supervisory data or data on MREL resources and targets and Pillar 2 requirements, unless they are competent authorities, and these may only be available on request. Third, disclosure templates may not make it possible to identify the relative bindingness of respective capital requirements.¹⁶ These data gaps were identified in a survey¹⁷ investigating EU law provisions and are in line with the relevant findings of the ESRB.¹⁸ Data availability depends on national implementation and inter-institutional provisions and is therefore country-specific. The survey participants also mentioned that cross-border data sharing might be a particular issue and that the ESRB could facilitate data sharing among authorities.

Targeted amendments to the BRRD and the CRD can ensure information flows to macroprudential authorities. Since information on MREL requirements might not be available to macroprudential authorities, Article 90 BRRD could be amended to make exchange of information among competent, resolution and other relevant authorities for macroprudential and financial stability purposes compulsory. In addition, Section II of Title VII CRD could be amended to require competent authorities, including the ECB, to share necessary information collected for supervisory purposes with other relevant authorities, if justified by financial stability considerations and subject to appropriate confidentiality arrangements.

Existing analyses indicate that the interaction of the buffer framework with other capital requirements limits the usability of buffers. Even if banks are willing to use capital buffers, the consequences of breaching the leverage ratio or MREL may prevent them from doing so. By the same token, the release of buffers by authorities may not free capital if other minimum requirements are the binding constraint. These potential impediments are a consequence of the ability of banks to use buffer capital to meet both leverage ratio and leverage-based MREL requirements. The leverage ratio was implemented to function as a backstop to risk-weighted requirements. Analysis conducted by the ESRB shows that buffer usability is materially limited by the leverage ratio in some Member States, and may further decline once MREL requirements apply. Allowing buffers to be used without triggering resolution processes is particularly important.

The limitations on buffer usability stemming from parallel minimum requirements warrant further monitoring. If they remain significant, the

¹⁶ While public disclosure might be not sufficient for analysing buffer usability and distance to breaches by market participants, any extension of transparency should be weighed against the risks of potentially exacerbating market tensions.

¹⁷ The voluntary internal survey within the ESRB Analytical Task Force was conducted in August 2021 and yielded responses from six authorities, mostly from larger Member States. While not representative in itself, the survey confirmed that at least some authorities shared the ECB's assessment of the existence of data gaps. The EU framework should aim to ensure that these gaps do not exist in any jurisdiction.

¹⁸ [ESRB \(2021\)](#).

Commission should assess whether a more fundamental revision is needed.

The magnitude of impediments is bank-specific and can evolve over time. Ongoing regulatory reforms, such as the finalisation of Basel III, may reduce these impediments, but are unlikely to eliminate them fully. Monitoring the evolution of buffer usability is recommended. At the next macroprudential review the Commission should assess, after consulting the ESRB, whether the impediments to buffer usability due to overlaps of parallel minimum requirements warrant a fundamental revision of the regulatory framework to ensure buffers are effectively usable. If this proves to be the case, the Commission is invited to consider pursuing mitigating options. Potential ways of addressing impediments to buffer usability would have to be thoroughly assessed, in particular for their impact on the complexity of the framework, capital requirements and consistency with international standards.¹⁹

¹⁹ [ESRB \(2021\)](#) discusses a range of mitigating options and their implications. The list of options mentioned in the report is not exhaustive, however, and the views of the membership on their merits and viability differ.

2.4 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?

G-SII and O-SII buffer requirements

8. **The ECB suggests that future changes to the G-SII buffer methodology as agreed by the Basel Committee be reflected in the EU framework.**
9. **The ECB suggests that the EBA, in consultation with the ESRB, be mandated to issue guidelines on a revised methodology for O-SII identification and on O-SII buffer calibration (also included in Section 4.1).**
10. **The ECB suggests not extending the leverage buffers for O-SIIs at this stage. At the subsequent review of the EU's macroprudential rules the Commission should assess, after consulting the ESRB and the EBA, whether additional leverage buffers should be introduced.**

The methodology used to calibrate G-SII buffers is agreed at the international level and therefore any changes should follow completion of the relevant Basel Committee discussions. The 2018 update of the Basel Committee's methodology has been reflected in CRD V. However, changes may be necessary depending on the outcome of the review of the implications of developments related to the banking union for the G-SIB methodology, announced in November 2021.²⁰

The ECB supports the development of comprehensive EU-wide guidelines specifying how O-SIIs are identified and their buffer rates calibrated, to ensure sufficient flexibility to account for Member States. There is a high level of heterogeneity in O-SII buffer rates which existing studies have been unable to attribute entirely to differences in systemic risk. The introduction of the ECB O-SII floor methodology reduced this heterogeneity at the lower end of buffer rates, and also promoted financial stability across the euro area by safeguarding against them being set too low. To further reduce this unjustified phenomenon, the ECB proposes developing an EU-wide guideline on identifying O-SIIs and calibrating their buffer rates.²¹ A detailed discussion of these guidelines and their rationale is presented in Section 4.1.

Additional leverage buffers for O-SIIs would strengthen the resilience of those bound by the leverage ratio. This could come at the cost of reduced usability of releasable risk-weighted macroprudential buffers, if the risk-weighted O-SII

²⁰ Monitoring the effects and prevention of window dressing are also relevant issues. However, it would be preferable to address these in a coordinated way at the global level, as changes to the Basel methodology would likely be necessary.

²¹ A guideline, which allows a comply-or-explain approach, is preferable to a regulatory technical standard, which would have less flexibility to deal with national features.

buffer alone is mirrored. Similar to G-SII leverage buffers, those for O-SIIs are intended to bolster the resilience of systemically important banks that pose a bigger threat to financial stability than smaller banks. The vast majority of banks would continue to be constrained by the risk-based framework rather than by leverage requirements, even if they were introduced for O-SIIs.²² O-SII leverage buffers would reduce the risk of excessive leverage from the lower risk weight densities of O-SIIs compared to non-systemically important institutions and therefore strengthen the backstop function of the leverage framework. However, they would strengthen the resilience of only a small number of O-SIIs at the current juncture. If O-SII buffers are not released due to the structural nature of the risk they address and banks' reluctance to dip into their risk-weighted capital buffers extends to leverage buffers too, their introduction has the potential to decrease the usability of releasable buffers in the risk-based framework and increase the potential procyclical adjustments. The results should be reassessed considering the phasing-in of the Basel III package and MREL, as this may have implications for the magnitude of the impact (for further details see Section 4 of Annex 1).

While the ECB does not at present advocate the introduction of leverage buffers for O-SIIs²³, it recognises the merits of designing the leverage framework so that it includes O-SII leverage buffers and increases total usability of buffers, while not restricting usability of releasable buffers. One possibility would be mirroring non-structural buffers too in the leverage ratio framework, which implies revising the role of the leverage ratio in banking regulation. The introduction of additional leverage buffers would make the leverage ratio framework a fully-fledged complementary framework to the risk-based one, and it could become the constraining requirement for more banks than currently.²⁴ This redesign would imply an increase in capital requirements and stricter rules than current global minimum standards. It would also increase the complexity of the framework, and as more banks would be subject to leverage buffers, differences between risk-based and leverage frameworks could be exacerbated.²⁵ Buffer setting practices may also have to be amended to take into account their impact on the size of the leverage buffer.²⁶ These changes are not advocated now, but should be considered again at the subsequent review, in conjunction with addressing potential

²² Leverage ratio requirements, including a fully phased-in G-SII LR buffer, were above their risk-weighted prudential requirements for only five out of 70 O-SIIs and G-SIIs supervised by the SSM (7%) as of end-2020. If an O-SII LR buffer with a 50% conversion factor was introduced, the leverage ratio would be the most constraining requirement for eight banks (11%); see also Section 4 of Annex 1. However, MREL may be in fact the most constraining requirement.

²³ A minority of Eurosystem members are, however, in favor of considering the introduction of additional leverage buffers already at this stage.

²⁴ This assumes: (a) the same factor applies when converting individual risk-based buffers to leverage buffers; (b) breaching LR buffers has the same consequences as breaching CBR (as a different approach would increase regulatory complexity).

²⁵ One key difference is that risk-based buffers can be met only with CET1 capital and sit on top of risk-based MREL, whereas the current G-SII leverage buffer can be met with Additional Tier 1 capital and does not sit on top of any MREL requirements according to the European Commission.

²⁶ This would not mean non-compliance with Basel standards, which set minimum rules. However, higher capital requirements than third countries could put EU banks at a competitive disadvantage. There is merit in coordinating such profound changes with Basel, so as to preserve a global level playing field. In addition, heterogeneous calibration of O-SII buffers within the EU would translate into the O-SII leverage buffer.

impediments to buffer usability stemming from the leverage ratio and MREL (see Section 2.3).

3 Missing or obsolete instruments

3.1 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?

11. **The ECB suggests introducing to the CRR a data collection requirement for a minimum set of lending standard indicators for residential real estate loans for monitoring purposes.**

Introducing a requirement to collect data for a minimum set of lending standard indicators for residential real estate (RRE) loans as defined in Recommendation ESRB/2016/14²⁷ for monitoring purposes would enhance the comparability of risk assessments in the RRE sector and the prudential policy stance on borrower-based measures (BBMs) across EU jurisdictions. The assessment of RRE-related risks and the design and implementation of policies to address them crucially depend on the availability of reliable, granular and timely data on real estate markets. Indicators of lending standards such as loan/value (LTV), debt service/income (DSTI) and debt/income (DTI) ratios are key to evaluating the sustainability of borrowers' debt and assessing the riskiness of banks' mortgage loan portfolios, as they relate to borrowers' probability of default and the loss given default. Regular reporting of these lending standard indicators, based on common EU definitions, ²⁸ for monitoring purposes would enhance the comparability of RRE risks and, indirectly and gradually, the BBM policy stance across EU countries, supporting financial stability surveillance in the EU. Granular information on lending standards is also crucial for hybrid regulatory instruments such as risk weights differentiated by the level of lending standard (e.g. higher risk weights for loans carrying high LTV ratios).

The introduction of the data collection requirement for a minimum set of lending standard indicators for RRE loans does not imply any change in the design or institutional attribution of BBMs and will be based on the existing work of the ESRB, with a view to minimising compliance and implementation costs. Activating, designing and calibrating macroprudential limits on lending standard indicators, i.e. BBMs, should remain within the remit of national authorities, so as to effectively address the risks identified and allow for national specificities

²⁷ [Recommendation of the European Systemic Risk Board of 31 October 2016 on closing real estate data gaps](#) (OJ C 31, 31.1.2017, p.1), as complemented and amended by [Recommendation ESRB/2019/3](#) (OJ C 271, 13.8.2019, p.1).

²⁸ While based on the ESRB Recommendation, the common definitions of indicators would also have to consider a number of related concepts already defined in the CRR as well as the possible need to provide some flexibility in view of national specificities.

given the heterogeneity across national mortgage and real estate markets. Recommendation ESRB/2016/14 can provide a basis for establishing common definitions and the corresponding data collection requirements.²⁹ More specifically, the collection of indicators based on common definitions should use existing reporting frameworks at the national level, where available, and allow for an appropriate transition period. It should not constrain national authorities from using national definitions aligned with domestic features for policy purposes, nor from collecting a broader set of lending standard indicators to inform the application of BBMs at the national level.

3.2 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?

12. The ECB does not suggest adding the power to impose binding system-wide restrictions on distributions at the Union and/or national level to the CRR/CRD at this stage.

Limiting distributions is a way for banks to retain their capacity to absorb losses and their ability to continue providing credit to viable firms and households in times of crisis, as evidenced during the COVID-19 crisis. Banks' distribution policies are relevant for both the safety and soundness of individual banks and the stability of the financial system. At the onset of the COVID-19 pandemic, the ECB recommended that banks refrain from distributing cash dividends and executing share buy-backs.³⁰ This was based on the consideration that in the heightened systemic uncertainty and stressed economic conditions created by the pandemic, preserving capital was necessary to ensure prudent capital planning and allow banks to retain their capacity to support the economy. At the same time, the ESRB complemented actions by the ECB and the European Supervisory Authorities by issuing a recommendation to banks, certain investment firms, insurers, reinsurers and central counterparties in an attempt to establish a uniform approach to restrictions on pay-outs across the EU and across different segments of the financial sector.³¹ The ESRB recommended that the relevant authorities request certain

²⁹ While based on the ESRB Recommendation, the common definitions of indicators would also have to consider a number of related concepts already defined in the CRR as well as the possible need to provide some flexibility in view of national specificities.

³⁰ See [Recommendation of the European Central Bank of 27 March 2020 on dividend distributions during the COVID-19 pandemic and repealing Recommendation ECB/2020/1](#) (ECB/2020/19) (OJ C 102 I, 30.3.2020, p. 1); [Recommendation of the European Central Bank of 27 July 2020 on dividend distributions during the COVID-19 pandemic and repealing Recommendation ECB/2020/19](#) (ECB/2020/35) (OJ C 251, 31.7.2020, p. 1); [Recommendation of the European Central Bank of 15 December 2020 on dividend distributions during the COVID-19 pandemic and repealing Recommendation ECB/2020/35](#) (ECB/2020/62) (OJ C 437, 15.12.2020, p. 1).

³¹ See ["Statement on dividends distribution, share buybacks and variable remuneration"](#), Paris, 31 March 2020; and ["The EBA continues to call on banks to apply a conservative approach on dividends and other distributions in light of the COVID-19 pandemic"](#), Paris, 15 December 2020; also ["EIOPA statement on dividends distribution and variable remuneration policies in the context of COVID-19"](#), Frankfurt am Main, 2 April 2020; and EIOPA's ["Financial Stability Report"](#), Frankfurt am Main, December 2020.

financial institutions to refrain from (a) making dividend distributions; (b) buying back ordinary shares; (c) creating an obligation to pay variable remuneration to material risk takers.

The ECB does not at this stage see the need to introduce new powers for authorities to impose system-wide restrictions on distributions. The ECB's Recommendation on dividend distributions was not a legally binding act. It was ultimately up to banks' management and shareholders to decide what distributions their banks would make. Nevertheless, the Recommendation proved effective in so far as all significant institutions followed it. The benefits of introducing new binding powers to restrict distributions need to be weighed carefully against possible drawbacks. In particular, the ECB has reiterated on many occasions that its Recommendation was exceptional and temporary and reflected the extraordinary uncertainty the banking sector faced at the outset of the COVID-19 pandemic. Introducing new powers for authorities to impose binding system-wide restrictions on distributions might signal that these restrictions could occur more frequently in future. Given the importance of distributions in enabling financial institutions to raise capital externally, heightened expectations of future restrictions as a result of the introduction of new binding powers might negatively affect banks' valuations and their ability to raise capital in private markets.³² These effects could be particularly pronounced if the EU were to unilaterally decide to introduce new powers for system-wide distributions, without other major jurisdictions introducing similar powers for their authorities.

The ECB also sees a risk that introducing binding powers for authorities to restrict distributions across the system could lead to additional fragmentation of the internal market during periods of financial stress. The ECB Recommendation was generally applicable at the consolidated level of significant supervised groups, so as to maintain a free flow of resources among the different legal entities within banking groups. However, some national authorities restricted distributions by all banks in their jurisdiction, irrespective of whether they were subsidiaries of groups headquartered elsewhere in the EU. These actions were motivated by financial stability considerations at the national level. However, measures of this sort – especially if taken by multiple national authorities simultaneously – can impede the ability of cross-border banks to fulfil their role of enabling private risk-sharing across the EU. They can also harm the resilience of cross-border groups by limiting their ability to gain strength from the geographical diversification of their risks across the internal market. Introducing these powers into the EU toolkit could potentially lead to more frequent imposition of restrictions on the transferability of resources within cross-border groups, particularly in periods of stress. This outcome, while possibly justified on financial stability grounds, would run counter to the objectives of other important legislative initiatives aimed at completing

³² Experience during the pandemic demonstrated that a recommendation to not pay dividends or buy back shares negatively affects banks' valuations, in particular by increasing uncertainty over future payouts. Andreeva, D., Bochmann, P., Mosthaf, J. and Schneider J. (2021), "Evaluating the impact of dividend restrictions on euro area bank valuations", *Macroprudential Bulletin*, Issue 13, ECB, Frankfurt am Main.

the architecture of the banking union and promoting the integrity of the EU's internal market for banking.

3.3 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?

13. **The ECB suggests streamlining the framework by replacing existing macroprudential risk weight articles in the CRR with a single article that allows authorities to set floors or tighten risk weights for exposures secured by real estate on macroprudential grounds.**

Macroprudential measures addressing risks in systemically important sectors, in particular exposures secured by real estate, by adjusting the risk weights, constitute an important part of the macroprudential toolkit. The ECB analysis shows that sectoral SyRBs cannot fully substitute for such measures, as their impact may not be fully replicated. The use of a sectoral SyRB would generate particularly high capital requirements for banks where risk weights in the sector targeted are already high, which may not be optimal.³³ Authorities may in some cases need to rely on risk weights measures instead of, or in conjunction with, a sectoral SyRB to be more targeted and avoid potential negative externalities (see also Section 7.1 of Annex 1).

Basel III input and output floors will not render macroprudential tools for risk weights redundant. Although Basel III floors may increase risk weights for banks using internal ratings-based (IRB) models, they do not directly target macroprudential objectives and may not be sufficient to achieve them. First, they are microprudential in nature and not designed to address systemic risks, which can go beyond idiosyncratic risks. Second, the output floor defines a lower limit to a bank's total risk exposure amount, not to its individual portfolios, therefore the impact on the portfolio targeted may be only indirect and potentially insufficient. This would be the case, for example, with banks that have high risk weights in other IRB portfolios or for market risk. Third, the input floors for banks using IRB models will increase risk weights for exposures secured by RRE only marginally, and therefore do not safeguard against the risk weights falling below levels that authorities in some Member States regard as too low from a macroprudential perspective (see also Section 7.2 of Annex 1).

While risk weights can be increased within certain ranges for macroprudential reasons under Article 124 CRR for banks using the standardised approach

³³ Tailoring a sectoral SyRB rate for a bank to its average risk weight in the targeted portfolio would create considerable complexity and reduce the transparency of the macroprudential action.

(SA), for IRB banks direct intervention at risk weight level is only possible under Article 458 CRR. This is procedurally more complex and can only be used as a last resort. Article 458 CRR measures are intended to be used only when the other macroprudential tools in the CRR or CRD are considered ineffective in addressing the systemic RRE risk identified. If used regularly, the EU governance procedures for Article 458 CRR measures safeguarding the internal market may present a significant capacity strain for the parties involved. It is estimated that completing the procedures at EU level can take about three months.³⁴ This may be disproportionate for a measure that will not last for more than two years. The existing simplified option for measures with lower capital impact may also not be sufficient to address risks in IRB banks efficiently.³⁵

The ECB suggests concentrating all the relevant provisions in a dedicated article to streamline the macroprudential risk weight measures related to real estate. The new article would replace the macroprudential use of Articles 124, 164 and 458(2)(d)(iv)³⁶ CRR and enable authorities to increase risk weights – rather than individual risk weight parameters such as PD or LGD – for RRE and commercial real estate (CRE) exposures based on macroprudential concerns. Besides amending risk weights for banks using both the standardised and IRB approaches, the new article should also enable authorities to impose stricter criteria for treating these exposures as fully secured under the SA, as is possible under the current Article 124 CRR. The new article should retain flexibility on the design of the measure, as specified in Article 458 CRR for both SA and IRB bank.³⁷ This would allow macroprudential authorities to retain the ability to link risk weight adjustments to different lending standards indicators, such as the LTV or DSTI of a loan book, where appropriate.³⁸ The administrative procedures aimed at safeguarding the Single Market should be modelled on the existing macroprudential provisions for tightening risk weight measures for real estate. The factors and conditions to be considered when assessing the appropriateness of risk weights and minimum LGD values which the EBA specified pursuant to the delegations provided in Articles 124 and 164 CRR

³⁴ One month for the ESRB and EBA to deliver their respective opinions, one month for the Commission to come up with a proposal and one month for the Council to decide whether to reject the measure. Pre-consultations with the ECB and ESRB may take additional time. Given the involvement of EU institutions, some national authorities are also required by national law to hold public consultations, which further extends the procedure.

³⁵ Article 458(10) CRR allows a simplified procedure for certain measures that result in a relatively low capital impact. Of the six Member States that have triggered a risk weight measure under Article 458, only that of Norway qualified for the simplified procedure. The remaining five followed the full procedure described in the text.

³⁶ Articles 124 and 164 CRR allow authorities to increase risk weights in the standardised approach and LGD floors in the IRB approach for mortgage exposures based on loss experience and forward-looking property markets developments, and if warranted from the macroprudential perspective. Article 458(2)(d)(iv) CRR allows risk weights to be increased to target asset bubbles in the residential and commercial property sectors if other measures in the CRR and CRD are not effective in addressing macroprudential risks stemming from these exposures.

³⁷ When applied in the form of a floor, risk weight measures can reduce risk sensitivity from the microprudential viewpoint. Banks using the SA may be discouraged from investing in more accurate IRB models, and IRB banks with higher average risk weights be discouraged from reducing risks if this does not lead to lower risk weights and capital saving. Macroprudential overlay may also be one of the reasons why risk-weighted capital ratios are less comparable across banks and Member States; for example, flat risk weight floors may overlay differences in risk between individual banks' portfolios. This underscores why macroprudential intervention should only be used in cases where this is warranted from the systemic risk perspective.

³⁸ De Nederlandsche Bank, for example, linked the introduction of stricter risk weight measures under Article 458 CRR with the LTV of individual loans as described in its [notification of 11 March 2020](#).

should continue to apply. As is currently the case for Articles 124 and 164 CRR, the new article should also invite the ESRB to issue a recommendation, inter alia, on a) factors which could adversely affect current or future financial stability and b) indicative benchmarks to be considered by macroprudential authorities when determining higher risk weights. The ability to increase LGD floors on macroprudential grounds would be removed to avoid interfering with microprudential aspects of internal models and eliminate a source of cross-country heterogeneity in the design of macroprudential risk weight interventions.³⁹

The new article would improve the efficiency of the macroprudential toolkit as regards risk weights while retaining safeguards for the integrity of the Single Market. Including all macroprudential measures concerning risk weights in a single article would streamline the various legal provisions and disentangle macroprudential and microprudential rules. Consistent administrative procedures across instruments and a balance between facilitating the application of risk weight instruments within the established thresholds⁴⁰ and ensuring the integrity of the Single Market for measures with a more material impact would ensure the framework operates efficiently. The thresholds for IRB risk weights should be developed taking into account the currently thresholds under Articles 164 and 458 CRR and allow for sufficient national flexibility in Member States where bank risk weights are low.⁴¹ The effectiveness of the measures adopted on the basis of this new article should be supported by mirroring the current recognition and reciprocity arrangements. This would imply mandatory recognition⁴² for measures within the established ranges⁴³ in order to avoid regulatory arbitrage and support the level playing field. Measures exceeding the ranges would continue to be subject to voluntary reciprocity.

³⁹ Experience shows that low risk weights stem primarily from the PD parameter. Using Article 164 CRR to tighten LGDs in order to offset the effect of low PDs would cause LGDs to deviate from their appropriate values and unduly penalise banks with more prudent PDs (see the notifications issued by the central banks of [Belgium](#), [Estonia](#), [Finland](#) and [Norway](#)). Only one Member State has made use of Article 164 CRR so far, while five have used Article 458 CRR to increase risk weights for IRB residential mortgages.

⁴⁰ The threshold for SA risk weight should be 150% as under the current Article 124 CRR. The threshold for IRB risk weight measures would have to be established based on quantitative assessments to ensure the tool is simple and effective and avoids unwarranted fragmentation.

⁴¹ The thresholds could be based on (i) a percentage increase in existing risk weight requirements, akin to the 25% in the current Article 458(10) CRR, (ii) an increase in risk weights in percentage points, (iii) an absolute value of risk weight, or (iv) a combination of all of these, bearing in mind the need to keep the framework simple.

⁴² This would be similar to automatic recognition under the current Articles 124 and 164 CRR.

⁴³ Mandatory recognition would be applicable for risk weight measures set within the specified ranges, allowing for a simple activation procedure. Voluntary reciprocation, similarly to what is currently envisaged in Article 458 CRR, would be applicable for measures exceeding the specified ranges.

4 Internal market considerations

4.1 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?

The O-SII buffer

As indicated in Section 2.4 the ECB suggests that the EBA, in consultation with the ESRB, shall be mandated to issue guidelines on a revised methodology for identifying O-SIIs and calibrating their buffers.

There is a high-level of heterogeneity in O-SII buffer rates that existing studies cannot entirely attribute to differences in systemic risk.⁴⁴ The heterogeneity can be seen from the fact that O-SIIs with similar scores based on the EBA standardised methodology can be required to maintain very different buffers in different jurisdictions. Nor do structural features such as the size or concentration of the banking system, or the phase of the financial cycle, fully account for the differences in buffer rates observed.⁴⁵ Heterogeneous application of O-SII buffers in the banking union has been partly reduced (at the lower end) by the introduction of the ECB's O-SII buffer floor methodology in 2016.⁴⁶ Buffer rates set by the national authorities of Member States in the Single Supervisory Mechanism (SSM) are compliant with this floor methodology, which is subject to a phase-in period lasting until 2023 in some countries, partly due to the pandemic.⁴⁷ The floor is a minimum and is not necessarily the appropriate rate for each Member State.

The ECB proposes developing an EU-wide guideline on the calibration of O-SII buffer rates to further reduce the risk of unjustified heterogeneity in the setting of O-SII buffers in the EU.⁴⁸ The guidance would need to be flexible to ensure that

⁴⁴ EBA (2020c), [EBA Report on the appropriate methodology to calibrate O-SII buffer rates](#), Paris, December.

⁴⁵ Besides inappropriate buffer setting, window dressing and limited buffer usability are a source of concern.

⁴⁶ ECB (2017), [Macroprudential Bulletin](#), Issue 3, Frankfurt am Main, June.

⁴⁷ O-SII buffers were scheduled to be fully implemented by 1 January 2022 in the countries in the SSM. Due to the unforeseen circumstances of the COVID-19 pandemic, three countries (Cyprus, Greece and Portugal) extended the phase-in period by one year. Specific phase-in arrangements going beyond 2023 may apply to individual banks which have been designated an O-SII or whose O-SII buffer has increased after the introduction of the ECB's O-SII buffer floor.

⁴⁸ In fulfilment of a mandate in CRD, the EBA reported to the Commission on the appropriate methodology for the design and calibration of O-SII buffer rates in December 2020; see EBA (2020c). In its report the EBA proposed introducing a floor methodology for calibrating O-SII buffers.

national specificities, new developments and insights can be reflected appropriately. The guideline should encompass both the identification phase⁴⁹ and buffer calibration and should be in line with the Basel Committee's D-SIB principles-based framework. The aim would be to develop a common methodology that would lead to consistent treatment across the EU, while allowing for a certain degree of flexibility in setting buffer rates. One possible starting point for work on common methodology is EBA (2020c). The guideline should be developed by the EBA in consultation with the ESRB and strike the right balance between flexibility and harmonisation, recognising the diversity of the landscape in the EU and national specificities while providing a consistent and comparable approach.

The systemic risk buffer

14. The ECB suggests instructing the ESRB to report on the identification of systemic risks for the purposes of setting the SyRB and, if appropriate, to issue a recommendation to DAs on the application of the SyRB on the basis of this report.

Only a few countries in the SSM have imposed positive SyRB rates. At present, they are in place in just four countries (Austria, Bulgaria, Croatia and Slovakia), which in part reflects the current economic and financial situation following the pandemic⁵⁰. The relevant authorities in these countries have cited structural characteristics of their banking systems and national economies as the reasons for applying the SyRB. Some of these are country specific. For example, in Austria the SyRB is partly aimed at mitigating risks stemming from the high level of exposure in the country's banking system to emerging markets in central, eastern and south-eastern Europe. Other structural systemic risks are likely to be common across multiple jurisdictions in the EU, such as risks from the levels of public and/or private sector debt (cited by Bulgaria and Croatia), the size of the banking system compared to the national economy (cited by Austria, Croatia and Slovakia), and external shocks to the economy (cited by Bulgaria, Croatia and Slovakia).

The ECB notes the potential for heterogeneity in the application of the SyRB and suggests that the potential for greater convergence and the need for further guidance on the use of the SyRB should be assessed. Differences in the current approaches to implementing the SyRB across countries, while justified to some extent by its use in addressing country-specific systemic risks, may indicate that systemic risks are treated unevenly across countries. Furthermore, while use of the SyRB is currently limited, it could cover additional risks in future, for example

⁴⁹ The identification phase is currently governed by [EBA/GL/2014/10](#). National practice has demonstrated that these guidelines may, in some circumstances, not be fully suitable when it comes to the choice of the mandatory indicators used to identify O-SIBs, and a review may therefore be warranted. For example, outstanding bank debt securities, which are one of the mandatory indicators under these guidelines, may not be indicative of a bank's contribution to systemic risks in countries where banks are predominantly funded with deposits.

⁵⁰ In addition to measures already in place, activation of a sectoral SyRB is planned in two other jurisdictions (Lithuania, Germany).

those stemming from specific sectors of the economy (such as residential real estate), climate risk (see also Section 5) or risks related to financial innovation.⁵¹

The ECB recommends mandating the ESRB to report by [July 2024] on the identification of systemic risks for the purposes of setting the SyRB, with a view to contributing to adequate coverage of systemic risks in the monetary union and each member of it and ensuring that the use of the SyRB does not go beyond what is necessary to address systemic risks.⁵² The report should help to improve the consistency of the treatment of systemic risks in the EU, without constraining the use of the SyRB as a flexible tool able to cover risks which are not mitigated by other tools and new systemic risks that emerge in future. The ESRB should liaise with the ECB, the EBA and national authorities to ensure there is a clear delineation between the risks captured by the SyRB, the risks captured by microprudential requirements and those captured by other macroprudential measures.⁵³ On the basis of this report, the ESRB should, if appropriate, issue a general recommendation to all relevant authorities concerning the application of the SyRB.

4.2 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?

Article 458 CRR

15. The ECB suggests making targeted amendments to the CRR to streamline the authorisation and extension procedures by clarifying the scope of the assessment performed by the ESRB and the EBA and enabling the ESRB to take existing assessments of systemic risks for participating Member States into consideration.

The ECB is of the view that the authorisation procedure for activating and extending stricter national measures under Article 458 CRR should be streamlined, while maintaining the legal safeguards intended for the integrity of the internal market. The current procedures were established to ensure that Article 458 is activated as a last resort by Member States and to allow a balance to be struck between financial stability and internal market considerations. However,

⁵¹ Now that CRD V has come into force, it can no longer be used for risks that are covered by the O-SII buffer; it can, however, now be applied for both sectoral and cyclical risks not covered by the CCyB (see also Section 3).

⁵² The ESRB report could potentially build on the taxonomy of structural systemic risks identified in ESRB (2017), [Final report on the use of structural macroprudential instruments in the EU](#), Frankfurt am Main, December; and relevant work by the Financial Stability Committee.

⁵³ As an example, the use of stress tests to calibrate the systemic risk buffer might lead to overlaps with Pillar 2 guidance that is also based on stress test results.

the ECB believes there is a need to make it easier to use Article 458 measures effectively without impinging on the functioning of the Single Market.

Activating and extending stricter national measures under Article 458 CRR should not be conditional solely on an increase in the intensity of systemic risk, but should also be possible in situations where systemic risks remain elevated. Under the current framework, the application of stricter national measures pursuant to Article 458 is conditional on identifying changes in the intensity of macroprudential or systemic risk in the financial system with the potential to have serious negative consequences to the financial system and the real economy. However, the experience of some DAs suggests that macroprudential intervention may be warranted even when there are no changes in the intensity of systemic risk, if systemic risks remain persistently elevated. The amendment would support macroprudential policy action and increase the effectiveness of the framework. At the same time, it does not change the temporary and extraordinary nature of Article 458 measures, which warrant regular review by national and EU institutions.

The complexity of the authorisation procedure could be reduced by revising and clarifying the scope of the assessment performed by the ESRB and the EBA when issuing their respective opinions, to align them with their institutional mandates. Currently, the roles of the EBA and the ESRB in the procedure for activating Article 458 measures are not clearly distinguished and their respective assessments intersect, which is not an appropriate reflection of their institutional mandates.⁵⁴ Revisiting the involvement of both authorities within their respective field of expertise could streamline the authorisation procedure and limit any overlap in their assessments. The EBA's assessment could focus on concerns related to the internal market from the perspective of microprudential supervision, complementing the ESRB assessment of risks to financial stability and suitability and the effectiveness and proportionality of the measures proposed. This would allow for a more expedited and targeted process, increasing the effectiveness of macroprudential policy in the EU.

The authorisation procedures set out in Article 458 could be further streamlined by explicitly allowing the ESRB to take the ECB's assessment of systemic risks into consideration where these relate to banks or banking sectors in the member countries of the SSM. With the establishment of the SSM, the ECB, together with the national DAs, assess systemic risk and macroprudential policy measures for banking systems both at individual country level and across Member States. When a country intends to adopt measures on the basis of Article 458 it needs to notify not only the ESRB, the EBA and the Commission but also the ECB, pursuant to Article 5(1) of Council Regulation (EU) No 1024/2013 establishing the Single Supervisory Mechanism. Given that the ECB already conducts an assessment of systemic risks and the appropriateness of planned measures, the ESRB could take the outcome of this into consideration to avoid duplication and as

⁵⁴ The EBA is an EU agency whose main tasks are to assist in the uniform implementation of EU law by developing the Single Rulebook, ensure supervisory convergence and facilitate coordination between national supervisory authorities. The ESRB is charged with macroprudential oversight of the financial system in the EU, including the prevention and mitigation of systemic risks, and contributing to the smooth functioning of the internal market.

far as possible reap synergies in conducting analytical work. This should not interfere with the ESRB's mandate to conduct its own assessment and provide an independent opinion as set out in Article 458.

The procedure for extending a measure under Article 458 could be simplified, for example by replacing the current recurring mandatory comprehensive assessment by the ESRB, the EBA and the Commission with a simplified non-objection approach.

Currently, Article 458 measures can be applied for up to two years. Every extension for up to an additional two years requires the same procedure as when activating the measure for the first time. To simplify the legal framework, the procedure for extending Article 458 measures could be streamlined to limit the administrative burden, without reducing the coherence of the implementation of macroprudential policy across the EU. This would not imply any changes in the notification requirement by activating authorities, that would need to provide adequate justification for the intended extension of an Article 458 measure. However, notification would only trigger the current EU governance procedure in the event that EU or national authorities raise an objection to the intended extension within a given deadline. The broad membership of the EBA and the ESRB ensures all relevant counterparts are consulted and should offset any potential concerns related to the functioning of the internal market.

The SyRB, G/O-SII interactions and caps

16. The ECB suggests converting the sectoral and general SyRB rates to a common denominator, the total risk exposure amount (TREA), before applying the additivity rules and the thresholds triggering EU governance procedures.

The current provisions of the CRD related to thresholds triggering EU governance procedures for sectoral SyRB rates raise concerns about the proportionality and consistency of the EU capital framework as regards setting sectoral SyRB rates. The current CRD governance procedures⁵⁵ do not distinguish between the thresholds triggering EU governance procedures for broad and sectoral SyRB, but they do provide for different calculation bases. The calculation of thresholds for a broad SyRB considers rates applied to the Total Risk Exposure Amount (TREA); for a sectoral SyRB, rates applied to the respective sectoral exposures. The current provisions can lead to situations where a sectoral SyRB rate applied to a relatively small portfolio could activate a stricter EU governance procedure, while a relatively lower broad SyRB would not, despite the latter having a much larger impact on bank capital requirements. As a result, thresholds are relatively more restrictive for the sectoral SyRB than for the broad SyRB. The current provisions can therefore generate inconsistencies in the capital framework which could influence the selection of macroprudential instruments by discouraging use of the sectoral SyRB. This approach does not appear to be warranted in view of the

⁵⁵ The CRD requires authorisation by the Commission if the combined SyRB rate for any given exposure (i.e. the broad SyRB rate plus the sectoral SyRB rate) exceeds 5%. For combined SyRB rates between 3% and 5%, authorities must comply with an opinion of the Commission or explain their reasons for not doing so. Finally, authorisation by the Commission is required if the sum of the SyRB rate and the higher of the O-SII and the G-SII buffer rates exceeds 5%. The Commission's authorisation is also subject to a mandatory opinion by the ESRB and a voluntary opinion by the EBA.

proportionality principle, as it could trigger EU governance procedures for measures that result in a relatively low capital impact, unduly increasing the burden for EU authorities.

The additivity rules for sectoral application of the SyRB should therefore be reconsidered. The ECB is of the view that the corresponding provisions of the CRD should be revised so general SyRB rates (applied to the TREA) and sectoral SyRB rates are first brought to a common denominator, which should be the TREA. In a second step, the general and sectoral measures expressed as percentages of this denominator could be added up to calculate the total SyRB rate; this would be the basis for possibly triggering EU governance procedures. These changes would increase the flexibility for authorities to calibrate SyRB rates at a level proportionate to the systemic risks they seek to address, including emerging ones such as climate change.

4.3 Are the provisions on reciprocity 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 reciprocity framework and procedures? If so, which options do you see and how would you evaluate them?

The ECB is of the view that reciprocity plays an important role in the EU macroprudential framework, as these arrangements foster effective implementation of measures. Reciprocity ensures that an activated measure is applied to all relevant institutions that have the exposures targeted in a given Member State, irrespective of their location.⁵⁶ Cross-border reciprocity of macroprudential instruments is key to implementing macroprudential policy efficiently. It helps avoid cross-border leakages and regulatory arbitrage and promotes a level playing field for domestic and foreign banks in an integrated financial market. This may become even more important in future, as further progress in the banking union and the capital markets union is expected to foster cross-border integration.

The framework for voluntary reciprocity has so far proved adequate for maintaining a level playing field and stopping national macroprudential measures being circumvented through regulatory arbitrage. While it is important for the EU macroprudential framework to provide sufficient coherence between instruments and Member States, it is necessary to retain a degree of flexibility. Reciprocity should therefore continue to apply on the basis of the existing

⁵⁶ In the Single Market, cross-border lending activities can be provided via foreign subsidiaries, foreign branches or direct cross-border lending. Macroprudential measures taken in one country usually apply only to domestic banks and subsidiaries of foreign banks. They therefore usually do not apply to cross-border exposures provided through direct credit and lending via foreign branches.

voluntary framework, supported by the relevant ESRB Recommendation.⁵⁷ Exposures that are below a specific threshold should continue to be exempt, to avoid any undue burden for banks. Altering the reciprocity regime at the current juncture is also not warranted in the context of the ongoing discussions and legislative process, which could have an impact on the minimum requirements and capital buffers. Given the evolution of the buffer framework, there is merit in continuously monitoring the reciprocity framework to collect empirical evidence and identify any additional areas for simplification and policy coordination that might ensure macroprudential measures are effective. However, the framework still has room for improvement to ensure legal provisions are consistent and clear.⁵⁸

4.4 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?

The role of the ESRB

- 17. The ECB suggests giving the ESRB the role of “notification hub” when relevant national authorities activate risk weight measures or reciprocate stricter national measures.**
- 18. The ECB suggests better delineating the role of the ESRB in existing delegations and ensuring it has a prominent role in any new instruments added to the EU macroprudential toolkit.**

The ESRB's role in exchanging information and coordinating the implementation of policy measures could be further strengthened. The revisions introduced to the CRR/CRD by CRR II/CRD V⁵⁹ assigned the ESRB the new role of “notification hub” for transmitting information on macroprudential

⁵⁷ [Recommendation of the European Systemic Risk Board of 15 December 2015 on the assessment of cross-border effects of and voluntary reciprocity for macroprudential policy measures \(ESRB/2015/2\)](#) (OJ C 97, 12.3.2016, p. 9).

⁵⁸ For example, Article 134 CRD stipulates that other Member States may reciprocate an SyRB rate set in accordance with Article 133 CRD and may apply that rate to domestically authorised institutions for exposures located in the Member State that sets that rate. At the same time, reciprocation of a sectoral SyRB is possible under Article 133(5)(d), which provides that the SyRB may apply to sectoral exposures, as identified in point (b) of this paragraph, located in other Member States only to enable recognition of a buffer rate set by another Member State in accordance with Article 134. Article 133(5)(d) does not provide for the reciprocation of a sectoral SyRB imposed on subsets of the exposures pursuant to Article 133(5)(f), which is not consistent with the principle of harmonised reciprocation of macroprudential measures and the apparent interpretation by the EBA in its Guidelines ([EBA/GL/2020/13](#)). These assume that SyRBs applied to subsets of sectoral exposures in accordance with Article 133(5)(f) may be reciprocated. Given the above, Art 134(5) CRD could benefit from clarification to expressly enable reciprocation of an SyRB applicable to subsets of exposures.

⁵⁹ Directive (EU) 2019/878 ([OJ L 150](#), 7.6.2019, p. 253) and Regulation (EU) 2019/876 ([OJ L 150](#), 7.6.2019, p. 1).

measures. The ECB sees great value in this role and suggests the ESRB be given a similar position for Articles 124(2) and 164(6) CRR and for reciprocation of measures under Article 458 CRR. This will enhance the ESRB's monitoring of Member States' macroprudential policies and strengthen the consistency of the macroprudential framework. If the proposal for a new article that brings together CRR provisions related to risk weight measures is adopted (see Section 3.3), a relevant provision on the "notification hub" role of the ESRB should be included here too.

The Commission should consider whether the ESRB's involvement in the existing powers to issue opinions or recommendations for macroprudential policy instruments could be better delineated. The amendments to Articles 124 and 164 CRR II could serve as a reference, since they clearly delineated the tasks of the ESRB and the EBA. More specifically, CRR II split the mandate to supplement Articles 124 and 164 CRR with respect to financial stability considerations, which had originally been given to the EBA in the CRR, into two parts and divided responsibility between the EBA and the ESRB, according to their respective fields of expertise. The EBA was tasked with developing technical standards related to the assessment of the adequacy of risk weights and LGD values, while the ESRB became responsible for issuing guidance on factors which could adversely affect current or future financial stability and on indicative benchmarks that have to be taken into account when determining higher risk weights or minimum LGD values. It is important that a similar delineation of tasks and responsibilities is applied to any new instruments and coordination mechanisms too, to ensure Member States benefit from the respective expertise of both authorities. The ECB therefore suggests that if new macroprudential instruments are added to the EU toolkit as a result of this review, e.g. if the proposal for a new article that brings together CRR provisions related to risk weight measures is adopted (see Section 3.3), the ESRB should retain a prominent role given its important mandate and proven competence in macroprudential policy.

5 Global risks

5.1 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?

19. The ECB suggests removing Articles 138 and 139 CRD, due to the significant challenges in activating them, the high coordination costs related to their exposure-based nature and the existence of other instruments to address macroprudential risks arising from banks' exposures to third countries. This would contribute towards simplifying the current framework.

The ECB acknowledges the relevance of monitoring the potential for third-country and global developments to generate or amplify systemic risks in the EU. At the same time, the ECB supports the removal of Articles 138 and 139 CRD due to the existence of other instruments in the EU macroprudential toolkit that can be used to target macroprudential third-country risks and concerns about the implementation of a third-country CCyB. The Global Financial Crisis, and more recently the pandemic, have demonstrated how financial shocks can spread through financial and trade links. Monitoring global vulnerabilities and having instruments to address them is key.

The nature and design of a third-country CCyB imply challenges related to its implementation as well as high coordination and monitoring costs.

Implementing it may be challenging, as a unilateral decision by EU designated authorities to goldplate a macroprudential instrument that is already part of the third country toolkit could prove controversial. As a result, activation would need to be coordinated with the relevant authorities in third countries. This is likely to be time-consuming and impede prompt policy action. The narrow, exposure-based nature of the measure and the mandatory reciprocity associated with its activation imply a high degree of coordination to promote consistent implementation across the EU. The specialist nature of the instrument requires going beyond regular monitoring of global risks and includes the regular identification of material third countries for exposures covered by the CCyB, as well as a detailed monitoring of developments related to excessive credit growth in non-EU countries.

In the EU, the changes introduced by CRD V enabling the use of the SyRB to address all risks not covered by Articles 130 and 131 CRD, thereby extending its application to cyclical risks, make the SyRB an appropriate instrument to address systemic risks from third-country exposures. The SyRB has a number of benefits over the CCyB when it comes to addressing systemic risks in third countries: it has broader scope beyond excessive credit growth, additional flexibility

(for example it can be applied to a subset of banks or address risks stemming from a cluster, rather than individual countries), and is a European instrument whose implementation does not suggest lack of action by a third country for a BCBS instrument under their macroprudential remit. The ECB therefore supports the removal of Articles 138 and 139 CRD.

5.2 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?

20. The ECB suggests no regulatory change in the macroprudential toolkit for banks to address the risk of exposures to non-banks at this stage.

21. The ECB suggests strengthening the regulatory framework for non-banks, including from a macroprudential perspective. This should include limiting liquidity risk in both money market funds (MMFs) and open-ended funds as well as procyclical derivative margins. In particular, a mandatory public debt requirement and increased weekly liquid asset requirements for private debt MMFs would enhance their shock-absorbing capacity. In addition, liquidity buffers for MMFs should be made more usable and authorities should have a role in directing their use. The introduction of a symmetric volatility adjustment for insurers may also be warranted to enhance the resilience of the sector.

Market-based finance has increased in importance and size, with non-bank financial institutions playing a growing role in financing the real economy.

Non-bank financial intermediaries such as money market funds, investment funds, insurance companies, pension funds and a host of other, more specialised, financial institutions have become increasingly relevant in the euro area. Since the Global Financial Crisis in 2008, total assets held by these entities have increased substantially and now represent more than half of the total financial asset holdings in the euro area.⁶⁰

Banks need to be aware of and adequately manage their counterparty risks, including the risks arising from non-bank financial institutions. This was demonstrated by the losses of some banks following the Archegos default.

Banks are exposed to non-bank financial institutions which sometimes take very highly leveraged and highly concentrated bets on financial markets. The recent default of the family office Archegos highlighted how interconnected risks are across the broader financial system, and how important strong risk management is. The

⁶⁰ Schnabel, I. (2021), "[The rise of non-bank finance and its implications for monetary policy transmission](#)", speech at the Annual Congress of the European Economic Association (EEA), 24 August.

event showed how stress in non-regulated financial firms can spill over to the banking system, by imposing significant losses on banks with exposure to these entities. It is therefore important to closely monitor risks emerging from the broader non-bank financial sector.

This recent stress event further highlights the need to strengthen the regulatory framework for the non-bank financial sector, including from a macroprudential perspective. At a minimum, there should be greater transparency on large and highly leveraged investors, so as to make concentrated losses from cases like Archegos less likely in future and mitigate these risks.

Greater availability and use of ex ante liquidity measures could mitigate the build-up of systemic risks in the non-bank financial sector, while reducing dependence on ex-post liquidity management tools. The growing relevance of the sector and the absence of policies to limit the build-up of structural vulnerabilities have repeatedly triggered calls from financial regulators and central bank representatives for enhancements to the regulatory framework.⁶¹ Existing (ex post) crisis management tools such as suspensions were not able to adequately mitigate that stress in March 2020; combined with a reluctance among funds to use their existing liquidity buffers, this resulted in liquidity strains that only eased once extraordinary monetary policy action had been taken in the euro area and other parts of the world.⁶² The Financial Stability Board has issued recommendations aimed at addressing structural vulnerabilities in the sector,⁶³ and the ECB has highlighted the need to incorporate additional ex ante requirements in the regulatory framework.⁶⁴

A comprehensive macroprudential framework for non-banks should rest upon several key principles, while taking into account the diversity of the sector. Specifically, it should take a system-wide perspective, because liquidity risk materialised across markets and non-bank financial intermediation (NBFIs) in the pandemic. It should focus on building up ex ante resilience, rather than relying on ex post measures, and ensure that non-banks are a stable source of funding, even in times of stress. Finally, given the heterogeneity in the NBFIs sector, it should be tailored to a diverse set of entities and activities and be flexible, so it can be adjusted over time as risks evolve.

In the case of MMFs, the ECB supports a requirement for these funds to hold a minimum position in more liquid public debt that can be used in times of market stress to meet redemption pressures and improve shock-absorbing capacity. MMFs are used mainly as a cash management vehicle. To preserve this function in a crisis, as revealed during the pandemic, it will be important to ensure they hold enough liquid assets to deal with large and unexpected outflows. Incorporating holdings of public debt, which has been shown to be far more liquid

⁶¹ Constâncio, V. (2017), “[Macroprudential stress-tests and tools for the non-bank sector](#)”, speech at the ESRB Annual Conference, 22 September.

⁶² Lagarde, C. (2020), “[Our response to the coronavirus emergency](#)”, The ECB Blog, 19 March.

⁶³ FSB (2017), “[Policy Recommendations to Address Structural Vulnerabilities from Asset Management Activities](#)”, Basel, January.

⁶⁴ De Guindos, L. (2019), “[Global financial regulation: where next? Pending tasks for regulators and macroprudential policy makers](#)”, speech in London City Week, 21 May.

than private debt during periods of market turmoil, would aim to ensure that funds have sufficient and diverse liquid assets to meet large redemptions. Holdings of public debt would be made mandatory, as part of an overall increased liquidity buffer. This would be complemented by taking action to increase the usability of these liquidity buffers and making them releasable during times of market stress. Authorities should have the power to direct that parts of the liquidity buffer be released and provide guidance on the appropriate timing for rebuilding them. Greater availability of liquidity management tools for MMF managers would strengthen the resilience of these funds, although authorities should not have a role in mandating the use of these tools, which should remain the prerogative of the manager.

The ECB also supports further work to develop policies addressing liquidity risk in open-ended investment funds (OEFs) and the procyclicality of margins.

For OEFs, this should include a forward-looking perspective and focus on better aligning the liquidity of assets and redemption terms. For margins, the work should focus on a) increasing transparency on modelling and governance practices; b) reducing the excessive procyclicality of margins at central counterparties; c) ensuring non-banks are better prepared for margin calls.

Further amendments to the Solvency II framework for insurers, such as the introduction of a symmetric volatility adjustment, could also be warranted.

In September 2021, the Commission adopted the Solvency II review package proposing to amend the [Solvency II Directive](#) and introduce a new [Insurance Recovery and Resolution Directive](#). The Solvency II proposal includes elements which would help to increase the resilience of the sector, including new tools with a macroprudential impact. It also puts forward changes to the volatility adjustment which make this tool entity-specific and help mitigate cliff-edge effects in cases of substantial volatility in spreads at a country level. The proposal could also make the tool symmetrical, since the current design allows capital to be released in periods of stress, but buffers are not built up in good times.⁶⁵ This is not in line with the need to build ex ante resilience.

5.3 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)?

Climate-related risks

22. The ECB sees a need to assess the use of macroprudential policy instruments to address climate change as well as broader environmental

⁶⁵ See also “[Response letter to a consultation of the European Commission on the review of Solvency II](#)”, ESRB, 16 October 2020; “[ESRB Response to the EIOPA Consultation Paper on the 2020 review of Solvency II](#)”, ESRB, 2020; and “[Enhancing the macroprudential dimension of Solvency II](#)”, ESRB, February 2020.

risks. This evidence-based assessment may extend beyond the completion of the review of the EU macroprudential framework. The Commission should, after consulting the ESRB and ECB, consider inserting any related proposals into EU law in a timely manner.

Climate risk drivers⁶⁶ are characterised by unique features, as climate-related events are uncertain and may be subject to non-linearities and tipping points.⁶⁷

These unique features have triggered a debate on whether the current regulatory framework can adequately address the risks. The Basel Committee is scrutinising the existing banking regulatory framework and its ability to sufficiently capture these unique features. Tackling the impact of climate-related financial risks in all its complexity poses a daunting task. The regulatory framework faces numerous challenges, from significant data gaps to methodological issues. Financial markets and institutions may have an incentive to be short-termists and ignore climate risks in the face of uncertainty and in the expectation that they will only materialise in the long run. Hence, the unique features of climate risks and system-wide incentive structures can lend a systemic dimension, both physically and in the form of transition risks. There is increasing evidence to show that climate risk drivers, transition and physical risks may represent a source of systemic risk to the financial system.⁶⁸

Climate risks are concentrated, both regionally and sectorally, and events are often interrelated, with a strong systemic component. Climate-related systemic risks may also be exacerbated by the classic risk externalities caused by interconnectedness and second-round effects that apply to other types of risk, too. The partial irreversibility of climate risks, their complexity and long-time horizons imply a high level of uncertainty regarding their timing and impact. This poses a major challenge in terms of quantification and forward-looking risk projections. These specific aspects of climate risks require new and innovative models to quantify their key drivers and developments over time.

Microprudential supervision expects banks to prudently manage climate-related and broader environmental risks.⁶⁹ The systemic dimension of climate risks, however, goes beyond idiosyncratic risks to individual banks and may require a further set of tools. The materialisation of climate risk is likely to affect similarly concerned banks simultaneously. Spillover effects across markets may further aggravate the impact beyond individual institutions' direct exposures. Common exposures and portfolio correlations may further build-up systemic risks. Macroprudential and microprudential supervisory approaches may need to complement each other to account for the long horizon of climate-related risks and the complex way they interact. Given the urgency of the climate challenge and the risk of tipping points, it is crucial to act swiftly and develop further solutions to avoid

⁶⁶ See ECB/ESRB Project Team on climate risk monitoring (2021), "[Climate-related risk and financial stability](#)", ECB, Frankfurt am Main, July.

⁶⁷ See BCBS (2021a), "[Climate-related risk drivers and their transmission channels](#)", Bank for International Settlements, Basel, April.

⁶⁸ See de Guindos, L. (2021), "[Shining a light on climate risks: the ECB's economy-wide climate stress test](#)", ECB Blog, 18 March.

⁶⁹ See ECB (2020), "[Guide on climate-related and environmental risks](#)", Frankfurt am Main, November.

an inaction bias.⁷⁰ Similar considerations may apply to broader environmental risks, and further assessment should be undertaken to assess their systemic dimension.

The existing portfolio of macroprudential tools may already be able to contribute to limiting the build-up of systemic climate risks and increasing banks' resilience against them materialising. Recent analysis has shown the impact of climate change on the EU financial sector is uneven, with vulnerabilities concentrated in certain regions, sectors and firms.⁷¹ The breadth of the existing macroprudential toolkit allows flexibility in addressing different types of risk, and also targeting different subsets of exposure at sectoral, regional or entity level. The recital included in the CRD VI proposal further highlights the flexibility embedded in the provisions on the SyRB.⁷² This could, however, also emphasise the ability to apply the SyRB to subsets of exposures, for instance those subject to physical and transition risks, tackling these in a targeted manner and incentivising use of this buffer. Nonetheless, the extent to which existing macroprudential tools, including the SyRB, could be readily deployed to capture climate risks needs to be examined.⁷³ Other existing actions such as large exposure limits and borrower-based measures could be further analysed, to understand whether and to what extent they may help limit the build-up of concentrated climate risks.

An assessment of whether new tools are needed to address climate-related and broader environmental financial risks from a systemic perspective is warranted. This should look into other types of tools to tackle the high degree of concentration in climate risk exposures, such as sectoral concentration charges.⁷⁴ Investigating macroprudential tools that target climate-related risks should be a priority and legal changes should be introduced into EU law in a timely manner. A comprehensive assessment of the existing macroprudential tools to address climate risks (including a thorough evaluation of their positive and negative effects on climate risks) and additional measures may extend beyond the completion of the review of the EU macroprudential framework. Once concrete options have been identified, the Commission, after consulting the ESRB and the EBA, should consider introducing them into EU legislation in a timely manner. A similar assessment will also be required for broader environmental risks, following further consideration of their implications for financial stability.⁷⁵

⁷⁰ See Baranović et al. (2021), “[The challenge of capturing climate risks in the banking regulatory framework: is there a need for a macroprudential response?](#)”, *Macroprudential Bulletin*, ECB, Frankfurt am Main, October.

⁷¹ See [ECB/ESRB Project Team on climate risk monitoring \(2021\)](#).

⁷² Proposal for amending Directive 2013/36/EU as regards supervisory powers, sanctions, third-country branches, and environmental, social and governance risks, and amending Directive 2014/59/EU ([COM/2021/663 final](#)).

⁷³ With regard to the SyRB, the recital included in the CRD VI proposal is a welcome addition, providing soft guidance on the interpretation and implementation of the relevant provisions. However, further aspects of how the SyRB is used in practice to effectively address systemic climate risks, including at sectoral level, need to be investigated.

⁷⁴ For example, concentration charges could complement supervisory measures and take the form of a risk-weight add-on that applies once exposures to a certain sector exceed a specific threshold, increasing in stages as concentrations rise.

⁷⁵ For an interim assessment related to biodiversity see NGFS and Inspire Study Group on Biodiversity and Financial Stability (2021), “[Biodiversity and financial stability: building the case for action](#)”, *NGFS Occasional Paper*, NGFS and Inspire, Paris/London, October.

Cyber risks

23. The ECB suggests considering macroprudential policy proposals addressing systemic cyber risks at a later stage.

Recent analysis suggests that cyber risks can become systemic and severely impair the financial system.^{76 77}

Systemic risks triggered by cyber incidents are unique in that they propagate not only through the financial losses of the institutions affected, but also through operational disruption inhibiting delivery of key economic functions across interdependent institutions. Existing macroprudential tools are not designed specifically to prevent and manage the impact of cyber incidents and thus have limited capability to serve as mitigants. The tools available mostly aim to increase loss-absorbing capacity, support smooth provision of credit and shore up confidence in the financial system. These can typically provide backstops for financial loss and reputational contagion, but are not effective in preventing or mending operational disruption.

The ECB considers that new policy tools, not restricted to the CRR and the CRD, should be considered at a later stage, with a view to reducing the probability and severity of cyber incidents and intervening in a timely and focused manner.

Possible policy options could include a) establishing a pan-European systemic cyber incident coordination framework for financial authorities (EU-SCICF)⁷⁸ to effectively tackle cyber risks in collaboration with financial institutions; b) use of scenario stress testing to identify potential weaknesses in cyber resilience; c) developing and calibrating systemic cyber risk mitigants, including a requirement for supervised entities to diversify IT infrastructure/providers/suppliers so as to avoid a “single point of failure”. The ECB welcomes the Commission’s legislative proposal⁷⁹ aimed at improving the management of information and communication technology risks through monitoring and reporting for both banks and other financial entities, with supervisory authorities involved as well.⁸⁰ As the appropriate systemic cyber risk mitigants have not yet been identified and work is ongoing in international fora and the legislative processes of the EU, the ECB is of the view that these risks should be kept under observation. Macroprudential policy proposals may be considered at a later stage.

⁷⁶ See ESRB (2020), “[Systemic cyber risk](#)”, Frankfurt am Main, February.

⁷⁷ See BCBS (2021b), “[Newsletter on cyber security](#)”, Bank for International Settlements, Basel, 20 September.

⁷⁸ See [ESRB Recommendation of 2 December 2021 on a pan-European systemic cyber incident coordination framework for relevant authorities \(ESRB/2021/17\)](#).

⁷⁹ Proposal for a Regulation of the European Parliament and of the Council on digital operational resilience for the financial sector and amending Regulations (EC) No 1060/2009, (EU) No 648/2012, (EU) No 600/2014 and (EU) No 909/2014 ([COM/2020/595 final](#)).

⁸⁰ See [Opinion of the European Central Bank of 4 June 2021 on a proposal for a regulation of the European Parliament and of the Council on digital operational resilience for the financial sector \(CON/2021/20\)](#).

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