Capital Requirements Regulation: transitional arrangements for mitigating the impact of the introduction of IFRS 9 on own funds and the large exposures treatment of certain public sector exposures denominated in non-domestic currencies of Member States

2016/0360B(COD) - 30/11/2017 - Text adopted by Parliament, 1st reading/single reading

The European Parliament adopted by 495 votes to 41, with 10 abstentions, a legislative resolution on the proposal for a regulation of the European Parliament and of the Council amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements and amending Regulation (EU) No 648/2012.

The European Parliament's position adopted at first reading following the ordinary legislative procedure concerns the amendments to Regulation (EU) No 575/2013 with regard to the transitional arrangements designed to mitigate the impact of the introduction of IFRS 9 on own funds and for the large exposure treatment of certain public sector debt of Member States denominated in other than domestic currencies of Member States.

The proposed Regulation recalled that IFRS 9 was published by the International Accounting Standards Board in July 2014. Regulation 2016/2067 requires EU banks to use it in their financial statements for financial years starting on or after 1 January 2018.

IFRS 9 is aimed at improving the loss provisioning of financial instruments by addressing concerns that arose during the financial crisis. It responds to the G20's call for a more forward-looking model for the recognition of expected credit losses on financial assets.

The application of IFRS 9 may lead to a sudden significant increase in expected credit loss provisions and consequently to a sudden decrease in institutions' Common Equity Tier 1 capital.

The proposed amendments to Regulation (EU) No 575/2013 are intended to **introduce transitional arrangements, which will apply from 1 January 2018, with a view to mitigating the potential negative regulatory capital impact on banks of the introduction of International Financial Reporting Standard (IFRS) 9**.

A recital refers to the resolution of 6 October 2016 in which the European Parliament called for a progressive phase-in regime that would mitigate the impact of the new impairment model of IFRS 9.

The resulting draft regulation will allow banks to add back to their 'common equity tier 1' capital a portion of the increased expected credit loss provisions as extra capital during a **five-year transitional period**. That added amount will progressively **decrease to zero** during the course of the transitional period.

Institutions should decide whether to apply those transitional arrangements and inform the competent authority accordingly. During the transitional period, an institution should have the possibility to reverse once its initial decision, subject to the prior permission of the competent authority which should ensure that such decision is not motivated by considerations of regulatory arbitrage

The draft Regulation also provides for the **phasing-out over three years** (from 1 January 2018) of an exemption from the large exposure limit available for exposures to certain public sector debt of Member States denominated in other than domestic currencies of Member States.