EBA REPORT ON INTERDEPENDENT ASSETS AND LIABILITIES IN THE NSFR UNDER ARTICLE 428f(3) OF THE CRR

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EBA EUROPEAN BANKING AUTHORITY

Contents

1. Executive Summary 4

1.1 Interdependent assets and liabilities and CRR mandate to the EBA 4

1.1.1 Work done 5

1.2 EBA's policy recommendations to the Commission 5

1.2.1 Covered bonds – Article 428f(2)(c)(ii) 5

1.2.2 Derivatives client clearing activities - Article 428f(2)(d) 6

2. Analysis of cases observed under Article 428f(1) – Description, observations and policy recommendations with regards to paragraph 1 of Article 428f 8

3. Analysis of cases observed under Article 428f(2) - Description, observations and policy recommendations with regards to paragraph 2 of Article 428f 9

3.1 Centralised regulated savings 9

a. Description of the activities observed 9
b. Analysis of the conditions in Article 428f(1) 9
c. Impact observed 12
d. Observations and recommendations 12

3.2 Promotional lending 13

a. Description of the activities observed 13
b. Analysis of the conditions in Article 428f(1) 14
c. Impact observed 15
d. Observations and recommendations 16

3.3 Covered bonds 17

a. Description of the activities observed 17
b. Analysis of the conditions in Article 428f(1) 19
c. Impact observed 21
d. Observations and recommendations 22

3.4 Derivative client clearing activities 26

3.4.1 Direct client clearing activities 26

a. Description of the activities observed 26
b. Analysis of the conditions in Article 428f(1) 26
c. Impact observed 28
d. Observations and recommendations 28

3.4.2 Indirect client clearing activities 28

a. Description of the activities observed 28
b. Analysis of the conditions in Article 428f(1) 29
c. Impact observed 30
d. Observations and recommendations 30

Abbreviations

ASF	Available stable funding
CCP	Central counterparty clearing house
COREP	Common European Reporting
CRR	Capital Requirements Regulation
EBA	European Banking Authority
EU	European Union
IM	Initial margin
LCR	Liquidity coverage ratio
NSFR	Net Stable Funding Ratio
OTC	Over the counter
RSF	Required stable funding
SPE	Special purpose entity

1. Executive Summary

1.1 Interdependent assets and liabilities and CRR mandate to the EBA

1. Interdependent assets and liabilities refer to activities where no funding risk exists for the Institution under the NSFR and as such, the activities are effectively exempted from stable funding requirements by receiving 0% RSF and 0% ASF in the calculation of the NSFR.

2. This preferential treatment is subject to compliance with the conditions established in Article 428f of the CRR.

3. Article 428f (1) lists the conditions required to treat assets and liabilities as interdependent.

4. Article 428f (2) lists a number of activities that are considered to meet the conditions required in paragraph 1.

5. Article 428f (3) includes a mandate to the EBA to monitor and draft a report on interdependent assets and liabilities. Article 428f (3) states: "*3. EBA shall monitor assets and liabilities, as well as products and services that are treated as interdependent assets and liabilities under paragraphs 1 and 2, to determine whether and to what extent the suitability criteria laid down in paragraph 1 are met. EBA shall report to the Commission on the results of that monitoring and shall advise the Commission on whether an amendment to the conditions set out in paragraph 1 or an amendment to the list of products and services in paragraph 2 would be necessary.*"

6. The mandate can be split into three parts:

   a. **Part 1 – Assessment of transactions and CRR compliance ("***EBA shall monitor assets and liabilities, as well as products and services that are treated as interdependent assets and liabilities under paragraphs 1 and 2, to determine whether and to what extent the suitability criteria laid down in paragraph 1 are met. EBA shall report to the Commission on the results of that monitoring…"***):** The EBA needs to look at **all the transactions (under para 1 and 2) applying the treatment of interdependency** and **assess if criteria in paragraph 1 are met by all of them**.

   b. **Part 2 – Assessment of potential amendments to the conditions established ("…***and shall advise the Commission on whether an amendment to the conditions set out in paragraph 1…would be necessary***):** The EBA needs to assess if the **conditions in paragraph 1** (which apply to all interdependent assets and liabilities – under paragraphs 1 and 2) **need to be amended**. The EBA needs to assess if the conditions are sufficient to "eliminate funding risk".

   c. **Part 3 – Assessment of potential amendments to the products listed (***and shall advise the Commission on whether… an amendment to the list of products and services in paragraph 2 would be necessary.***):** The EBA needs to see if the **list of products in paragraph 2 needs to**

be amended – e.g., they need to be further specified or corrected if the EBA understands that they "trigger funding risk".

1.1.1 Work done

7. While the CRR does not envisage a notification approach to the EBA of the cases where Article 428f is applied, the EBA has benefited from contributions from EU competent authorities as regards those institutions under their supervisory remit applying Article 428f(1) or (2) CRR. This has allowed the EBA to understand the background, characteristics of the transactions in place, special arrangements, impact, etc. and to assess the compliance with and the effectiveness of the conditions envisaged in paragraphs 1 and 2 and whether potential amendments to the conditions in paragraph 1 or 2 would be necessary. This information has also been complemented with the available COREP data on the NSFR.

8. The EBA assessed the description of the transactions on which Article 428f has been applied. The EBA analysed if the conditions in paragraph 1 and the definition in paragraph 2 of Article 428f were met by those products or services. The EBA also assessed if the conditions in paragraph 1 and the definitions in paragraph 2 ensure the absence of funding risk or whether any amendment is necessary for consideration.

1.2 EBA's policy recommendations to the Commission

9. All in all, the EBA has only limited recommendations to make at this stage, which concern two products envisaged in Article 428f(2) CRR. The EBA will continue to monitor the transactions reported by banks as interdependent assets and liabilities in the NSFR in cooperation with competent authorities.

1.2.1 Covered bonds – Article 428f(2)(c)(ii)

10. Point (ii) of Article 428f(2)(c) envisages as eligible covered bonds those where, in addition to the condition in point (i), "*the underlying loans are fully match funded with the covered bonds that were issued or the covered bonds have non-discretionary extendable maturity triggers of one year or more until the term of the underlying loans in the event of refinancing failure at the maturity date of the covered bond*". The EBA considers that some amendment is necessary in point (ii) of Article 428f(2)(c) CRR in the description of covered bonds that are eligible to apply the treatment of interdependent assets and liabilities in the cases of maturity mismatch between the underlying loans in the cover pool and the covered bonds to cover any funding risk. The CRR envisages for these specific cases, where the loans are not fully match funded with the covered bonds, the extension of the maturity of the covered bonds in case the bank fails to refinance at the maturity date of the covered bond.

11. The EBA considers that the extendable maturity trigger needs to be observable in markets as an objective indicator where the bank will not need to take any action since the bondholder needs to be aware that once the specific trigger/threshold is reached the extension of the maturity of the covered bond will be automatic. The EBA has concerns that a trigger that might

necessitate any action to be taken by the bank might not be ultimately exercised due to the reputational issues and subsequent market consequences that acknowledging failure to refinance by the bank might pose. The specification of the observable indicator in markets and the trigger should be established in the contractual arrangement or regulatory framework of the covered bond to ensure its effective application by the bank and the bond holder in an automatic manner.

12. The EBA recommends the following amendment to point (ii) of Article 428f(2)(c) (changes to the current wording of the article are underlined): "*the underlying loans are fully match funded with the covered bonds that were issued or the covered bonds have non-discretionary extendable maturity triggers of one year or more until the term of the underlying loans in the event of refinancing failure at the maturity date of the covered bond. The maturity trigger shall be based on objective criteria which are public and observable in the market and are specified and required pursuant to a legal, regulatory or contractual commitment. These criteria shall be prudent enough to ensure a trigger event both during a funding market wide scenario as well as during an idiosyncratic stress scenario.*"

1.2.2 Derivatives client clearing activities - Article 428f(2)(d)

13. The EBA considers that, in view of the cases assessed, indirect derivatives client clearing activities, with the central institution of an IPS as intermediary between the CCP and the final customer's bank, do not seem to pose more funding risk than in the case of direct derivatives client clearing activities between the CCP and the customer's bank as clearing member directly, provided that the customer's bank does not provide to its clients guarantees of the performance of the CCP and the central institution in the case of indirect client clearing activities.

14. The EBA recommends adding specifically the case of indirect derivatives client clearing activities to the established direct derivatives client clearing activities to make sure that the necessary safeguards envisaged in Article 428f(2)(d) apply here.

15. With respect to these safeguards the EBA recommends clarifying the need that no funding risk can lie under these transactions when benefitting from the application of the treatment of interdependent assets and liabilities. The EBA considers that, as is established now, the fact that the institution does not provide guarantees of the performance of the CCP, or the central institution as proposed, is a necessary condition to ensure absence of funding risk but still not sufficient itself and thus the wording "as a result" might be misleading and lead to consider that the conditions in Article 428f(1) are not relevant. For these purposes the EBA recommends some amendment by deleting that wording to avoid a potential misunderstanding or wrong application of the rule.

16. The EBA recommends the following amendment to Article 428f(2)(d) (changes to the current wording of the article are underlined): "*derivative client clearing activities, provided that the institution does not provide to its clients guarantees of the performance of the CCP or of the performance of the central institution in a cooperative network or institutional protection*

scheme in the case of indirect derivatives client clearing activities, and ~~, as a result,~~ does not incur any funding risk."

2. Analysis of cases observed under Article 428f(1) – Description, observations and policy recommendations with regards to paragraph 1 of Article 428f

17. The EBA received information related to two activities authorised to apply the treatment of interdependent assets and liabilities under Article 428f(1) CRR.

18. The EBA has assessed compliance of those activities with the conditions established in that provision.

19. Based on the information received, the assets and liabilities are clearly identified, on a client-by-client basis, the amount being the same in each case.

20. The link between the relevant asset and liability treated as interdependent is established contractually, in one case, and in the relevant member state's law, in the other case, and the liabilities are not utilised to fund any other asset. The funds received from the interdependent assets are only used to settle liabilities payments which happens within 20 days. Furthermore, it is established that the counterparties should be different.

21. The description provided of interdependent assets and liabilities shows that the bank will not anticipate repayment of its liabilities if the monies have not been received first from its assets. The relevant competent authority has confirmed that any prefunding agreement is not included in the treatment under Article 428f(1).

22. The impact observed on NSFR values is material.

23. The EBA considers that there do not seem to be reasons to think that the criteria under Article 428f(1) are not met or that any funding risk remains.

24. No policy recommendation to amend Article 428f seems necessary based on the cases observed.

3. Analysis of cases observed under Article 428f(2) - Description, observations and policy recommendations with regards to paragraph 2 of Article 428f

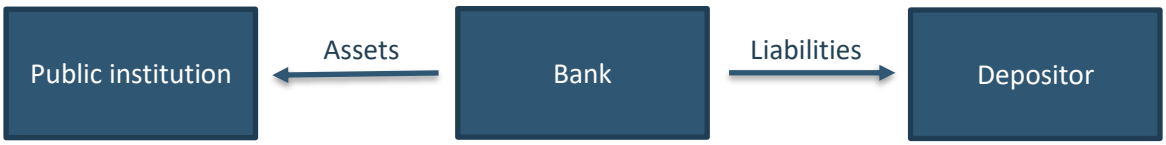
3.1 Centralised regulated savings

a. Description of the activities observed

25. The EBA received information that 8 EU banks apply the treatment of interdependent assets and liabilities as regards centralised regulated savings envisaged in point (a) of Article 428f(2) of the CRR.

26. These transactions refer to regulated savings centralised to a public institution. They are saving products whose functioning is framed by a member state's law and individual agreements between the collecting banks and a public institution.

27. The centralised share of regulated savings products subject to a centralisation obligation contributes to the financing of the government's economic policy. As such, the public institution dedicates its initiatives to the financing of social housing and urban planning policies.



b. Analysis of the conditions in Article 428f(1)

28. This section is based on the description of the transactions as provided by relevant competent authorities.

(a) the institution acts solely as a pass-through unit to channel the funding from the liability into the corresponding interdependent asset;

29. Under this structure, according to the relevant member state's law, credit institutions collecting the regulated savings from retail customers are legally obliged to centralize a part (target rate defined by decree) of these funds into the public institution in order to finance the social housing entities and urban renewal. Article 428(f)(2)(a) applies only to this centralised part.

30. The banks describe that they are required to deposit a portion ("centralisation" or "centralised part") of the proceeds of these regulated saving accounts at the state-owned public institution

to fund general interest investments mainly social housing and sustainable development in the relevant member state.

31. The government organises the collection of funds from savers via distributor networks according to regulatory procedures set out in the relevant member state's rules. Relevant banks are legally obliged to transfer around 60% of the funds collected to the public institution. It involves a so-called "centralisation" mechanism at the public institution, via an ad hoc national savings fund vehicle.

32. For Centralized Regulated Savings the notion of intermediary is confirmed by the nature of deposit defined by the law and the contract existing between the client and the bank.

(b) the individual interdependent assets and liabilities are clearly identifiable and have the same principal amount;

33. The account in the public institution and the deposit accounts are mirroring themselves. Pursuant to the applicable legal framework, the credit institutions and the public institution calculate periodically the amount of regulated savings to be centralised in case of a net positive variation in the stock of regulated savings since the previous reference date or to be collected by credit institutions in case of a negative variation in the stock of regulated savings since the previous reference date.

34. Individual interdependent assets and liabilities are clearly identifiable and correspond to the centralised part. The amount of the centralised part is updated every 10 days. Individual interdependent assets and liabilities have the same amount as only the portion of these deposits centralised at the public institution is considered as interdependent.

35. The savings collected, including the centralised share, are recorded as liabilities in the form of customer deposits and the centralisation with the public institution is recorded as assets and constitutes a receivable from the public institution. For the centralised share, the balance sheet therefore includes an asset amount equal to the liability amount.

36. For Centralized Regulated Savings, the assets amount is based on each eligible deposit made by the clients so criteria on identification and principal amount are respected.

(c) the asset and interdependent liability have substantially matched maturities, with a maximum delay of 20 days between the maturity of the asset and the maturity of the liability;

37. These assets and liabilities have the same maturity. They are non-maturing products as they constitute a deposit from saver and a deposit to the public institution. In addition, at each centralisation date, an "inflow" or "outflow" occurs between the bank and the public institution. This flow reflects the inflow, minus the outflow observed between the credit institution and the saver customer. Under the centralisation mechanism, credit institutions inform the public institution of any increase or decrease in the amounts deposited by savers. In the case of an increase (i.e. the amounts collected are higher than those withdrawn), the institutions centralise a portion with the public institution. In the case of a decrease (i.e. the amounts collected are

lower than those withdrawn), the public institution returns the centralised share of the amount of the outflow to the credit institutions. This centralisation mechanism takes place monthly or four times a month (the 7th, 15th, 23rd and last day of each month) under the so-called "10-day" centralisation process, introduced by the relevant member state's law and which applies at the option of the collecting institutions. This mechanism ensures a matching in maturities between assets and liabilities.

38. For Centralized Regulated Savings, there is convergence of the maturity between asset and liabilities. The process of centralization of the regulated saving is made each 10 open calendar days. The maximum delay between the maturity of the asset and the maturity of the liability is 10 days, well below 20 days, as the required amount to centralize is adjusted.

(d) the interdependent liability has been requested pursuant to a legal, regulatory or contractual commitment and is not used to fund other assets;

39. For the centralised regulated savings the institutions act solely as a pass-through unit to channel the funding from the liability into the public institution. As mentioned before it is regulated by the relevant member state's law and individual agreements between the collecting institutions and public institution. Funds centralized to the public institution are guaranteed by the relevant member state's central government.

40. By law, the bank is required to deposit a portion of the proceeds of these regulated saving accounts at the state-owned public institution to fund general interest investments mainly social housing and sustainable development in the relevant member state. By construction of the centralization framework, the interdependent liability matches the asset and hence cannot be used to fund any other asset.

41. This interdependence is governed by the relevant member state's law establishing the centralisation mechanism and by specific agreements concluded between the public institution and the supervised entities.

42. For Centralized Regulated Savings, these liabilities are clearly defined by the law (to identify the nature of deposit eligible) and a contract exists between the client and the bank.

e) the principal payment flows from the asset are not used for other purposes than repaying the interdependent liability;

43. The principal payment flows to and from the interdependent asset is by construction of the centralization framework exclusively related to the interdependent liability: in case of deposit decrease, the centralized portion of the withdrawn amount is reimbursed by the public institution to the bank.

44. An inflow is transferred by the public institution to the credit institutions when withdrawals from clients exceed new deposits (i.e. net outflow from the bank perspective). The inflow is perfectly matching with the net outflow, at the latest within the following three working days

or the next business day, if the three working days are closing Target days. Conversely, in case of a net inflow from clients, a corresponding outflow occurs towards the public institution.

45. The principal payment flows from the asset are not used for other purposes than repaying the interdependent liability.

46. Furthermore, as mentioned, a contractual relationship exists by means of which the amount coming from the asset can be used only for the interdependent liabilities.

(f) the counterparties for each pair of interdependent assets and liabilities are not the same.

47. The counterparties for each pair of interdependent assets and liabilities are not the same: the counterparty of the asset is the public institution and the counterparty of the liabilities are retail banking clients.

48. These interdependent assets and liabilities are the result of the sums deposited by savers in passbook savings accounts whose deposits are partially centralised in the public institution. As such, each pair of interdependent assets and liabilities represent the part of the deposit by a considered saver that is centralised and the equivalent amount on the asset side that is lent to the public institution.

c. Impact observed

49. If these transactions were not treated as interdependent assets and liabilities a 95% ASF factor would apply to the amount of the retail deposits centralised in the public institution - Regulated savings are demand deposits. As to the RSF some banks apply 100% RSF factor applying to the deposit placed with the public institution, where the expectation is that the public institution will not be obliged to repay the deposits in the short-medium term, whereas others apply 50% RSF to unencumbered loans to the public institution below 6 months.

50. Following the NSFR values provided, as most recent available date at the time of the discussions of this report, for a limited number of the institutions, around 30% of them, the impact is material.

d. Observations and recommendations

51. Following the description provided, the assets and liabilities are identifiable and have the same amount, which is the amount of the centralised savings placed with the public institution (assets) and received from retail depositors (liabilities). The time for the public institution to repay is 3 days at most. Since the calculation of the amount to be received from the public institution (or placed with) is done every week or every month, the maximum difference between maturities of the assets and liabilities would be 10 days or 1 month which seems in line with the transfer of deposits on at least a monthly basis as required in the CRR.

52. To be noted that the transfer of deposits from the public institution to the bank is guaranteed by the relevant member state's central government. The impact on NSFR values of applying the treatment of interdependent assets and liabilities is low in general.

53. No policy recommendation to amend Article 428f seems necessary here.

3.2 Promotional lending

a. Description of the activities observed

54. The EBA received the description of promotional lending activities in the context of point (b) of Article 428f(2) of the CRR corresponding to more than 1000 EU banks. The promotional loans target public objectives and materialise in the context of specific financing activities like export funding but also as general financing to companies.

55. Interdependent assets and liabilities relate to promotional loans and corresponding funding from promotional banks to support the general economic development for which the institution acts purely as an intermediary.

56. Promotional lending is very much a public initiative lending activity oriented to strategic economic targets with public policy objectives of the relevant member state's government. Promotional lenders are generally public banks in the form of public sector entities (PSEs). The authorised institution acts as an intermediary between the original promotional lender and the final customer (non-financial corporates and private customers). Promotional lenders make use of intermediaries to channel and facilitate these activities throughout the full territory. The intermediary passes through the promotional loans to the final customers. The member state's government provides guarantees that can reach up to 90% of the repayment of each promotional loan. The extension (pass-through) of the loan by the promotional bank to the intermediary is fully guaranteed by the member state's government.

57. The intermediary passes the funds received from the promotional lender on to the final customer. Interdependent assets and liabilities presented by the intermediary bank refer to liabilities against the promotional banks (on behalf of the member state's government) for the funding received and assets in the form of loans to final customers (as borrowers).

b. Analysis of the conditions in Article 428f(1)

(a) the institution acts solely as a pass-through unit to channel the funding from the liability into the corresponding interdependent asset;

58. The bank is the lender, but merely passes on the favorably granted refinancing of the promotional bank to the loan customer. The bank therefore acts purely as an intermediary.

59. The promotional lender provides funding to the intermediary in the amount of the loan to the customer that the intermediary has committed to. The monies received by the intermediary from the promotional lender are for the specific purposes of being passed through to the final customer as a promotional loan.

60. In terms of repayment of the loans, the monies received from the customer by the intermediary will be used only for repayment of the funding originally provided by the promotional lender for the purposes of the loan to be passed through.

61. The money received in both transactions are in terms of extension of the loan expected to be immediately passed on to the final customer in the extension of the loan, or in terms of repayment of the loan immediately passed on to the promotional lender, in the repayment of the loan, once received from the final customer by the intermediary.

(b) the individual interdependent assets and liabilities are clearly identifiable and have the same principal amount;

62. The interdependent assets and liabilities can be identified 1:1, on a single loan basis, by the institution. Both assets and the associated liabilities are stored and linked in the core banking system. The assets and liabilities are identical in terms of both amount and maturity.

(c) the asset and interdependent liability have substantially matched maturities, with a maximum delay of 20 days between the maturity of the asset and the maturity of the liability;

63. The system and accounting settings or organizational/process specifications are set in such a way that payment by the institution to the promotional bank is made only after payment by the ultimate borrower to the institution. Although the repayment of the loan by the customer is made to an account of the institution, this inflow is immediately forwarded to the funding bank (outflow).

64. The interdependent assets and liabilities have the same maturity. The funding provided by the promotional lender has only to be repaid when the loan to the final customer matures or is terminated by the intermediary institution. Generally, Article 428f (2) CRR is only applied for loans that are fully performing and non-doubtful. Otherwise, the intermediary would not be allowed to net the relevant assets and liabilities. In that case the assets would be assigned with

an RSF factor of 50% or 100% and the liabilities with 0%, 50% or 100% ASF in accordance with their maturity[1].

(d) the interdependent liability has been requested pursuant to a legal, regulatory or contractual commitment and is not used to fund other assets;

65. Interdependent liabilities occur as a result of contractual obligations of eligible loan projects and are not used to fund other assets. The banks liabilities are governed by a contractual agreement that foresees the financing of corporate loans. There are contractual arrangements between the parties involved containing the details of the contractual obligations and description of the transaction.

e) the principal payment flows from the asset are not used for other purposes than repaying the interdependent liability;

66. It is ensured in the contractual instructions of the transactions that the principal payment flows from the asset are not used for other purposes than repaying the interdependent liability:

- Extension of loans: The funds provided by the promotional lender are passed through by the intermediary to the final customer without undue delay. The interdependent asset and liability exist just after the loans have been disbursed to the final customer.

- Repayment of loans: The funds collected from the final customer via direct debiting are then passed through to the promotional lender without undue delay. These funds cannot be used for anything else due to the matching maturity.

(f) the counterparties for each pair of interdependent assets and liabilities are not the same.

67. The counterparties on the assets side are retail customers, SMEs and corporate customers. The counterparties on the liabilities side are the promotional banks. The counterparties on the asset side and on the liability side of the interdependent assts and liabilities are not the same. Promotional lenders cannot take out loans as “final customers” in promotional loan programs.

c. Impact observed

68. If these transactions were not treated as interdependent assets and liabilities, the following treatment is foreseen:

- A 50% RSF factor would apply to the amount of the loans to customers (expected to be non-financial) in the asset side with a residual maturity of less than 1 year. A 65% or 85% RSF, depending on the risk weight (35 % or less in the former case) would apply to the amount maturing in one year or more.

[1] This is a conservative approach. As most institutions qualify as PSEs a different treatment is also possible: 50/50/100 % ASF

- As to the liabilities against the promotional bank, a 0%, 50% or 100% would apply if the residual maturity is lower than 6 months, lower than 1 year or 1 year or higher, respectively[2].

	< 6 months	Between 6 and 12 months	>= 12 months
Loans to non-financial customers (RSF)	50%	50%	65% or 85%
Liabilities against promotional banks (ASF)	0%	50%	100%

Following the information provided, as most recent available date at the time of the discussions of this report, in most of the cases the descriptions provided indicate that the NSFR values would not change materially if Article 428f(2) would not apply.

d. Observations and recommendations

69. Following the description provided the EBA does not have concerns about the compliance with the conditions established in Article 428f(1) of the CRR. The description shows that the banks applying Article 428f(2)(b) is acting as an intermediary. The bank provides to the customer the funding received from the promotional bank and passes-through the payment of the loans from the customer to the promotional bank. The interdependent assets (loan to customers) and obligation to the promotional banks are described to be identified one by one and with the same amount and maturity. The funding received by the intermediary from the promotional bank is only specifically for the purposes of passing-through the promotional loan to the specific final customer. At the same time the monies received by the intermediary from the final customer in repayment of the promotional loan passed-through by the intermediary are for the specific and sole purposes of repaying to the original promotional lender. The arrangements of these transactions, including rights and duties for both, customer and promotional banks, are established contractually. Both contractual counterparties, promotional bank, in the liability side, and final customer, in the asset side, are different.

70. Point (b) of Article 428f(2) CRR considers promotional loans fulfilling the criteria in the LCR for institutions acting as simple intermediaries that do not incur any funding risk. The EBA is of view that the described promotional loans fulfill these criteria and that the intermediaries do not incur any funding risk.

[2] This is a conservative approach. As most institutions qualify as PSEs a different treatment is also possible: 50/50/100 % ASF

71. The EBA is of view that the criteria envisaged under Article 31(9) LCR DR for promotional loans through intermediaries are met. In this regard, the last subparagraph of Article 31(9), with respect to promotional loans through intermediaries, states that "The promotional loans referred to in this paragraph shall be available only to persons who are not financial customers on a non-competitive, not for profit basis in order to promote public policy objectives of the Union or that Member State's central or regional government.". The description shows that the loans are granted to non-financial corporates and private customers only which would meet the requirement that the borrower is not a financial customer. The loans are granted in the context of the programs of the promotional bank which is linked to publics objective on behalf of the government.

72. In extending and passing-through the promotional loan by the intermediary to the final customer, no funding risk seems to arise for the intermediary. Passing-through is subject to having received the monies before from the promotional lender.

73. For the application of the treatment of interdependent assets and liabilities, in the repayment of the promotional loan, it is described that the funding provided by the promotional lender has only to be repaid when the loan to the final customer matures or is terminated by the intermediary institution. In case of default of the final customer at maturity to repay the loan, the intermediary would still be liable to repay to the promotional lender but it should be noted that, importantly, a government guarantee applies and would cover the default. Furthermore, in this case, the loan would be considered non-performing/doubtful and Article 428f(2) would cease to apply. Therefore, in view of the EBA the intermediary would not incur any funding risk.

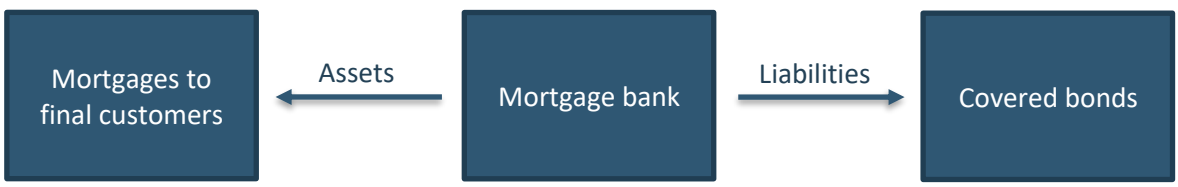
74. No policy recommendation to amend Article 428f seems necessary here.

3.3 Covered bonds

a. Description of the activities observed

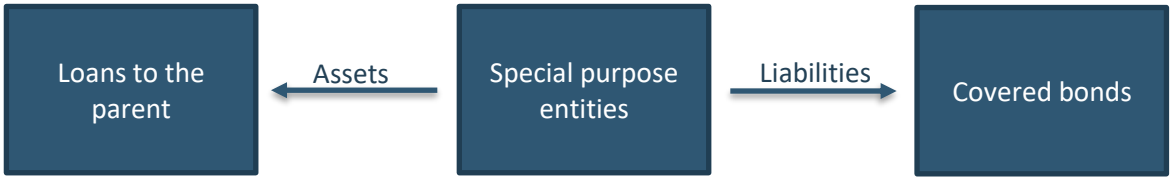
75. We have received information that 11 EU banks apply the treatment of interdependent assets and liabilities as regards covered bonds as envisaged in point (c) of Article 428f(2) of the CRR. We see different business models in them:

76. In some cases they are "mortgage banks" that issue covered bonds to provide directly funding in the form of mortgages to final customers. Here covered bonds are considered as interdependent liabilities and the corresponding mortgage loans as interdependent assets.



77. In other cases the banks, as “special purposes credit institutions (SPE)”, operate solely as pass-through, issuing covered bonds, that are considered as interdependent liabilities, and channeling the proceeds via loans granted to their parent company, that are considered interdependent assets. The bank (subsidiary) is actually created by the parent for these purposes.

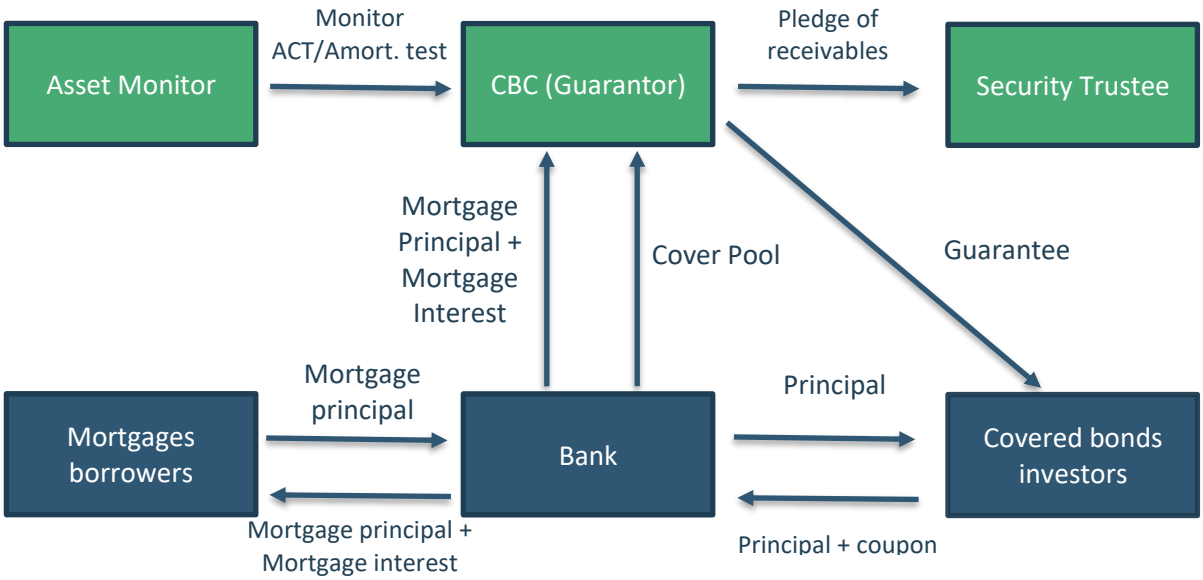
78. Funding provided to the parent is used to grant loans to individuals (mainly mortgage loans) directly or via other group entities. These loans granted by the parent are pledged as collateral with full transfer of ownership to the subsidiary according to the relevant member state’s law. In case of default of the parent company, all net revenues generated by the pledged loans will be applied to the repayment of the issued covered bonds in accordance with the relevant member state’s law. The parent company is primarily responsible for paying back the loans granted by its subsidiary. The loans pledged continue to be recognized on the parent company balance sheet which is still collecting the related cash flows.



79. Furthermore, in some case the bank issues conditional pass-through covered bonds, as interdependent liabilities, and the corresponding mortgage loans, as interdependent assets.

80. Cover assets are secured in favor of the covered bondholders via the transfer to a separate legal entity, the Covered Bond Company (CBC), a special purpose vehicle (SPV), by means of a guarantee support agreement. The mortgages and covered bonds remain on the balance sheet of the bank.

81. As conditional pass-through covered bonds, in the case that the bank defaults on its payment obligations on a covered bond, including a potential failure to issue and sell a new covered bond, the Covered Bond Company guarantee would apply to the bondholders.



b. Analysis of the conditions in Article 428f(1)

82. This section is based on the description of the transactions as provided by relevant competent authorities.

(a) the institution acts solely as a pass-through unit to channel the funding from the liability into the corresponding interdependent asset;

83. The mortgage banks' proceeds from issuing the covered bonds are transferred to the mortgage borrower and the amortization (and interest) from borrowers are passed on to the bond holders.

84. The SPE issues covered bonds and passes through the proceeds via loans to its parent company.

85. In the case of conditional pass-through covered bonds the bank acts as the issuing entity of the covered bond program solely as a pass-through unit to provide the funding to the mortgage borrowers.

(b) the individual interdependent assets and liabilities are clearly identifiable and have the same principal amount;

86. In the case of the mortgage banks, the terms of the mortgage mirrors that of the specific covered bonds (specific ISIN) issued to finance the mortgage.

87. In the case of the SPEs the assets and liabilities can be clearly identified and have the same principal amount.

88. Assets and liabilities are clearly identifiable in the conditional pass-through covered bonds, where interdependent assets (mortgages) and liabilities (covered bonds) have the same principal amount.

(c) the asset and interdependent liability have substantially matched maturities, with a maximum delay of 20 days between the maturity of the asset and the maturity of the liability;

89. In the case of the mortgage banks, callable loans are defined by having an interest rate and a maturity that matches the interest rate and the maturity of the underlying covered bonds issued, including an identical amortization profile.

90. In the case of mortgage loans with a longer maturity than the underlying bonds (e.g. 30 year mortgages versus 1 to 10 year bonds), the loans will be refinanced by issuing new bonds at the expiry of the underlying bonds. The interest on the mortgage loans is reset to the new market interest rate with every refinancing. If at the time of refinancing it is not possible to obtain a full refinancing (not sufficient buyers in the market) then the existing (expiring) bonds that are not refinanced will be prolonged by 12 months until full refinancing is again possible. The interest on the prolonged bonds will be 5 percentage points higher than before the refinancing.

91. In addition, mortgage loans with a maturity longer than the underlying bonds, where the underlying bonds have a maturity of up to 24 months, are also subject to a maturity extension based on an interest rate trigger. If the interest rate of the new (refinanced) bonds that clears the supply will be more than 5 percentage points higher than the interest on the expired bonds the expired bonds will be prolonged once by 12 months. The interest on the prolonged bonds will be 5 percentage points higher than before the refinancing.

92. The funds from the SPE borrowing (covered bonds issued) and the loans granted by the parent have the same amount and are fully identifiable. However, there might be some slight mismatch between the maturity of the covered bonds and the maturity of the loans to the parent.

93. The conditional pass-through case refers to mortgages with an average maturity of around 20 years funded with covered bond which in general have a maturity of 5 years. The covered bonds are bullet. For a maturity extension to be triggered, after which the bonds (liabilities) would mimic the maturity profile of the mortgages (assets) by extending its maturity up to 32 years, two conditions should be met:

    a. That the bank defaults on its payment obligations, which may arise when the bank would fail to refinance the maturing covered bonds with new ones[3]; and

    b. That the Covered Bond Company, after the event of default of the bank, would not have sufficient resources to repay the maturing covered bonds by selling a part of the cover pool assets.

[3] At the maturity date of the covered bond, it is reasonably expected that the bank would not have the resources to pay the interdependent covered bond liabilities, which are bullet, with the proceeds of the interdependent mortgages due to their maturity gap. Therefore the bank would need to issue new covered bonds to repay the maturing covered bonds.

(d) the interdependent liability has been requested pursuant to a legal, regulatory or contractual commitment and is not used to fund other assets;

94. The covered bonds issued by the mortgage banks can only be used to fund mortgages according to the relevant member state's mortgage regulation.

95. The SPE is a special funding vehicle created to fund its parent company lending to final customers, directly or via other group entities, and has no other object. This is envisaged in contractual arrangements.

96. The program documentation (contractual commitments) clearly states which assets can be funded and cover the conditional pass-through covered bonds (liability).

e) the principal payment flows from the asset are not used for other purposes than repaying the interdependent liability;

97. Payment flows can only be used by the mortgages banks to pay the interdependent liability according to the regulation in place.

98. Flows from assets (loans to the parent company) are channeled to repay the covered bonds issued by the SPE.

99. In the conditional pass-through, the principal payment flows are only used to repay the liabilities, although in the pre-extension phase the pool has a dynamic nature, i.e. the mortgages can be replaced, but the principal amount of the assets always equals the principal amount of the interdependent liability.

(f) the counterparties for each pair of interdependent assets and liabilities are not the same.

100. In the case of mortgage banks, investors in covered bonds and loan takers are in principle not the same. However, anyone can invest in the covered bonds, also loan takers.

101. Covered bonds are bought by investors and bank's loans are granted to the parent company.

102. In the securities note it is specified that the conditional pass-through covered bonds cannot be offered to retail investors. Therefore, the counterparties for the mortgages, that are retail, are not equal to the counterparties regarding the covered bonds.

c. Impact observed

103. If these transactions were not treated as interdependent assets and liabilities, the following treatment is foreseen:

- A 50% RSF factor would apply to the amount of the mortgages in the asset side with a residual maturity of less than 1 year. A 85% RSF would apply to the amount maturing in one year or more as assets encumbered in a cover pool more than one year.

- As to the covered bonds in the liability side, if the holder is a financial customer then a 0%, 50% or 100% would apply if the residual maturity of the covered bond is less than 6 months, less than one year or of one year or more, respectively. If the holder is not a financial customer then a 50% or 100% would apply if the residual maturity is less than one year or of one year or more, respectively. In this case, if the holder is not identifiable then it is treated as a financial customer, following the ITS on NSFR reporting.

	< 6 months	**Between 6 and 12 months**	**>= 12 months**
Loans (RSF)	50%	50%	85%
Covered bonds (ASF)	0% or 50%	50%	100%

104. The impact seems, to some extent, to be referred to the point in time of the lifetime of the covered bonds and related loans.

105. There seems to be a material impact on NSFR values of the applying Article 428f(2) CRR to the cases of covered bonds.

d. Observations and recommendations

106. Following the analysis described, the EBA considers that banks applying Article 428f(2) to covered bonds transactions might still have some funding risk in the relevant assets and liabilities treated as interdependent, as long as additional liquidity sources to the interdependent assets would be necessary to cover the interdependent liabilities, in case of failure of the interdependent assets.

107. Furthermore, in the analysis conducted by the EBA an issue arises with regards to the way the extension of the maturity of covered bonds with shorter maturity than the relevant assets in the cover pool is defined in paragraph 1 of Article 428f. The provision does not seem to provide the necessary guarantees for the extension of the maturity to be triggered and subsequently to eliminate funding risk in the bank applying the treatment of interdependent assets and liabilities.

Interlinked interdependent assets and liabilities

108. The description of the transactions indicate that the issuer bank would be obliged to pay and anticipate funds to the covered bond holders if the mortgage borrower would not pay at maturity. There is no contractual arrangement established where the payment to the covered bond holder would not need to be done if the borrower would have not provided payment of the mortgages at maturity.

109. In the absence of such arrangement and in case of arrear or default of the borrower the bank would incur funding risk. The bank would need to seek for alternative funding to the interdependent asset.

110. The conditions established in Article 428f(1) refer to a one-to-one link between identified individual interdependent assets and liabilities, the individually identified covered bond and loans in the cover pool of the issuer in this case. The part of the balance sheet that will benefit from this treatment is self-funded where the interdependent liabilities cannot be used for other assets and the interdependent assets are to be used to repay the interdependent liability. The underlying principle here, as also underlined in paragraph 45 of the NSFR Basel standard (or paragraph 30.35 of the consolidated version), is that "the liability cannot fall due while the asset remains on the balance sheet". One of the cases where this might happen is the case of an arrear or default of the asset and where the bank would still be obliged to pay the liability at maturity.

111. Over-collateralisation in the cover pool via liquid assets and loans, is clearly a way to minimize funding risk. By nature a number of loans will at any point in time be in arrears. The magnitude of arrears will vary over the business cycle. Over-collateralisation requirements in the covered bonds legislation seek to ensure, that the mortgage banks always have the means to pay the bond holders. However, the concept of interdependent assets and liabilities in the NSFR with 0% RSF and 0% ASF envisages a one-to-one link between relevant interdependent assets and liabilities with no funding risk to be covered by other resources. In addition to this, the use of other assets to cover the repayment of interdependent liabilities, in case of failure of the interdependent assets, might alter the adequate funding structure of the rest of the balance sheet of the bank. Liquid assets as over-collateralisation will help to meet the NSFR requirements since the RSF factors applicable to liquid over-collateralisation are low. Furthermore, the predominant position of long-term loans in the cover pool triggers 85% RSF versus long term bonds that trigger 100% ASF. For the same reasons, any other individual assets than individual loans in the cover pool cannot be considered as interdependent assets to cover funding risk of the covered bonds as interdependent liabilities.

Extendable maturity trigger

112. Point (ii) of Article 428f(2)(c) requires that for the cases where the underlying loans are not fully match funded with the covered bonds that were issued the covered bonds should "*have non-discretionary extendable maturity triggers of one year or more until the term of the underlying loans in the event of refinancing failure at the maturity date of the covered bond*".

113. Specific cases have been observed where there is a substantial difference between the residual maturity of the covered bonds and relevant mortgages. For example in the case of the mortgage banks referred to, the relevant covered bonds are refinanced yearly, every third year or at a lower frequency depending on the refinancing schedule chosen by the borrower. For the shorter bonds of maturities of up to 24 months, the relevant member state's covered bonds legislation envisages that if the refinancing rate that clears the supply is more than 5 percentage points higher than at the previous fixing, bonds will automatically be extended by one year and borrowers would pay an interest equaling the interest rate of the previous year plus 5

percentage points until next reset. The trigger is non-discretionary as required by the provisions of article 428f(2)(c)(ii).

114. The relevant covered bonds are also subject to a second extension trigger. This trigger states that in the unlikely case there is not sufficient demand for the new bonds, an extended maturity will be triggered at the maturity of the covered bond. In this case, the current covered bond holders shall keep its position for an additional year. The interest on the prolonged bonds will be 5 percentage points higher than before the refinancing. At the end of this prolonged maturity the same process as described would apply. In cases like this, the EBA has concerns that some action to recognise failure to refinance by the issuer bank will be necessary to trigger the extension of the maturity. Banks might intend to avoid the exercise of the trigger to avoid reputational issues in markets.

115. The EBA has concerns that in a situation of no demand for the new bonds, a bank would need to anticipate and seek alternative funding for covered bonds to cover such funding risk arising. This might even include accessing central bank or government funding, if necessary, to avoid reaching the point in time where the extension of the maturity would be triggered. This means that the required interlink between the interdependent assets and liability, i.e. between identified individual mortgages and covered bond, would not take place. This would not allow for the application of the treatment of interdependent assets and liabilities. This is irrespective of the fact that still the alternative funding that a bank could access might still provide the necessary ASF to cover the RSF from the mortgages.

116. The EBA considered that the way point (ii) of Article 428f(2)(c) is drafted in the CRR may impede that the trigger will apply in practice if it is subject to any action from the bank and is not based on observable and automatic indicators. This is due to the pre-requisite for the extendable maturity to be triggered, i.e. "*in the event of refinancing failure at the maturity date of the covered bond*". The EBA has concerns that the relevant bank issuer will intend to avoid the trigger to be exercised due to the expectedly reputational impact this might cause to the bank with subsequent market and business penalization. In these cases, the EBA has concerns that the bank will avoid the trigger and therefore the maturity of the covered bond ultimately will not be extended. This means that the refinancing risk remains in the bank and the envisaged pass-through mechanism cannot remove it.

Policy recommendation

117. It is proposed to ensure that indeed the extension of the maturity of the covered bond in a stress scenario, either idiosyncratic or market wide, will always happen when its maturity is lower than that of the mortgages.

118. The provision is proposed to be reformulated to emphasize that the event that triggers a maturity extension is objective and observable in the market. Since extension of the maturing bonds might signal problems at the issuing institution, the institution might for reputational reasons want to avoid that the extension is triggered. Therefore, for the maturity extension trigger to be effective, what triggers the extension of the maturity should be observable in the

market and should not depend on any discretionary action to be taken by the issuer. These objective criteria should be specific and, thus, not subject to interpretation by the issuer or the bond holder. Both parties should understand that the extension of the maturity takes place automatically once the criteria are met.

119. The criteria should be formally established in the regulation or contractual arrangements of the covered bonds, again to avoid the need of any reaction by the institution failing to refinance and to make the trigger automatic. Both parties should, therefore, be aware of the rules applies for the automatic extension of the maturity.

120. Potential cases of banks setting unrealistic thresholds for the triggers should be avoided. The expectation is that refinancing should happen easily below the threshold of the trigger. Therefore, the criteria should be prudent and reflect cases of failure to refinance in the context of an idiosyncratic or market wide stress scenario.

121. Therefore point (ii) of Article 428f(2)(c) is proposed to be reformulated along the following lines (changes to the current wording of the article are underlined): "*the underlying loans are fully match funded with the covered bonds that were issued or the covered bonds have non-discretionary extendable maturity triggers of one year or more until the term of the underlying loans in the event of refinancing failure at the maturity date of the covered bond. The maturity trigger shall be based on objective criteria which are public and observable in the market and are specified and required pursuant to a legal, regulatory or contractual commitment. These criteria shall be prudent enough to ensure a trigger event both during a funding market wide scenario as well as during an idiosyncratic stress scenario.*"

3.4 Derivative client clearing activities

3.4.1 Direct client clearing activities

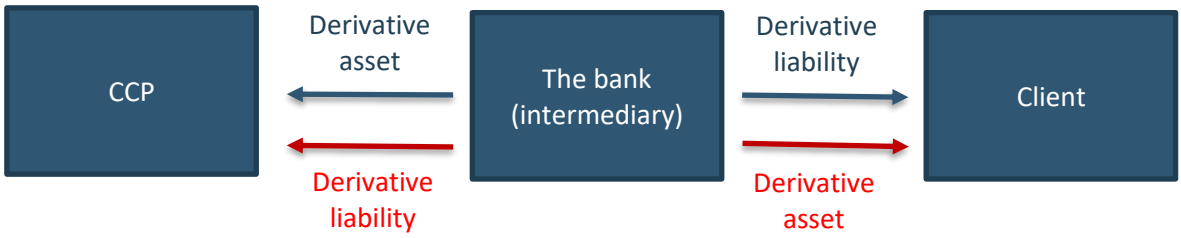
a. Description of the activities observed

123. 8 EU banks recognise interdependent assets and liabilities as regards derivatives client clearing activities under Article 428f(2) CRR.

124. Following the descriptions provided the intermediary bank meets daily CCP calls with margins it receives from its clients (stemming from positions in red in the chart below). The amount of margin the bank receives from clients will be at least equal, if not more, to the amount that has been called by the CCP for its client positions. In some case it is stated that excesses received are not included as part of the exemption.

125. Any compensation claim against the bank is limited to the amount which the bank has received from the central counterparty in the case of positive market value for the client of the derivatives and for the contracts that are terminated (stemming from positions in blue in the chart below). The description envisages that per the standard documentation the bank does not guarantee the performance of CCPs to its clients.

126. The description of the interdependent assets and liabilities is the following:



127. These services are generally offered to clients who do not have the size or the will to be members of CCPs but have the obligation to clear some product classes. They are given the possibility to access the CCP via the bank. In this context, the bank collects collateral from its clients, which is posted to the CCPs to cover the interdependent margin requirement.

b. Analysis of the conditions in Article 428f(1)

(a) the institution acts solely as a pass-through unit to channel the funding from the liability into the corresponding interdependent asset;

128. The bank receives margin calls from CCPs and onwards calls its clients for margin calls. The margin that the bank receives from clients is passed through to meet CCP requirements and vice

versa for positive market value for the client and at the termination of the contracts. The bank will not be liable for any performance and loss.

129. The bank is an intermediary trading OTC with the client and is back-to-back with CCP. There is no market risk, clients post IM to the bank on their standalone position and the bank posts IM to the CCP on the portfolio of all its client clearing business.

(b) the individual interdependent assets and liabilities are clearly identifiable and have the same principal amount;

130. The description provided indicates that the interdependent assets and liabilities are identifiable in the IT systems and that they have the same principal amount. The balances are clearly identifiable and the amounts received from clients equals the amounts held in various accounts. As cash is fungible, there may not always be a one-to-one linkage from one liability to one asset, but in aggregate the amounts balance.

131. In the operating system, only the portion of the liability equal to the margin requirement of the CCP is treated as interdependent.

(c) the asset and interdependent liability have substantially matched maturities, with a maximum delay of 20 days between the maturity of the asset and the maturity of the liability;

132. These client clearing activities are stated to have substantially matched maturities. The daily margining process means there is no mismatch in term for both asset and liability. It is argued that, nonetheless, there can be intraday differences in maturities as CCPs have hard cut-off times by which margin payments must be made, whilst the bank may choose to allow clients to post margin later in the day/next day. However, it is confirmed that any differences would be < 20 days.

(d) the interdependent liability has been requested pursuant to a legal, regulatory or contractual commitment and is not used to fund other assets;

133. The derivative client clearing activity is based on specific contractual arrangements that the bank signs with the client ("Clearing Agreement") and with the CCP ("CCP rulebook"): based on these contracts, the client is committed to pay to the bank any charges or amounts incurred in connection with the provision of the clearing services and the bank is committed to post to the CCP the margins that it may be required to pay. Initial margin and additional variation margin calls made by the CCP are received from the bank's client and passed-through to the CCP for these specific purposes only. As the liability treated as interdependent is limited to the amount of the CCP margin requirement, the interdependent liability cannot be used to fund other assets.

e) the principal payment flows from the asset are not used for other purposes than repaying the interdependent liability;

134. The bank would recall cash from CCPs and segregated accounts as clients reduce or close-out their positions and use the proceeds to repay liabilities as they fall due. The principal payment flows from the asset are matching the principal payment flows from interdependent liability and hence cannot be used for other purposes than repaying the interdependent liability.

135. (f) the counterparties for each pair of interdependent assets and liabilities are not the same.

136. Counterparties for interdependent assets and liabilities are not the same, generally the client and the CCP.

c. Impact observed

137. If these transactions were not treated as interdependent assets and liabilities, the following treatment is foreseen:

- The derivative treatment would apply for every single transaction (each transaction is treated as a single netting set):
- That means 0% ASF for derivative liabilities or initial margin received and 100% RSF for derivative assets or 85% RSF for initial margin posted regardless of the counterparty.

138. Following the description provided with regards to the changes in the NSFR values applying Article 428f, as available at the time of the discussions of this report, the change seems generally significant.

d. Observations and recommendations

139. The EBA did not see reasons to think that any condition in Article 428f(1) might not be met in this case.

140. Point (d) of Article 428f(2) requires that the institution should not provide to its clients guarantees of the performance of the CCP in order to ensure that the institution does not incur any funding risk. The description provided shows that it is generally established that the bank is not liable for defaults of the CCP.

3.4.2 Indirect client clearing activities

a. Description of the activities observed

141. One bank applies the treatment of interdependent assets and liabilities as regards derivatives indirect client clearing activities under Article 428f(2) CRR. The bank clears its clients' derivatives transactions with the central institution of the IPS that acts as a direct CCP clearing member.

142. The structure of the indirect clearing is the following. It very much follows the scheme under the Commission Delegated Regulation on indirect clearing arrangements[4]. Recital 1 refers to the layers in the context of indirect clearing arrangements the central counterparty (CCP), the clearing member, the client of a clearing member and indirect client:

[4] Commission Delegated Regulation (EU) 2017/2155 of 22 September 2017 amending Delegated Regulation (EU) No 149/2013 with regard to regulatory technical standards on indirect clearing arrangements (link)

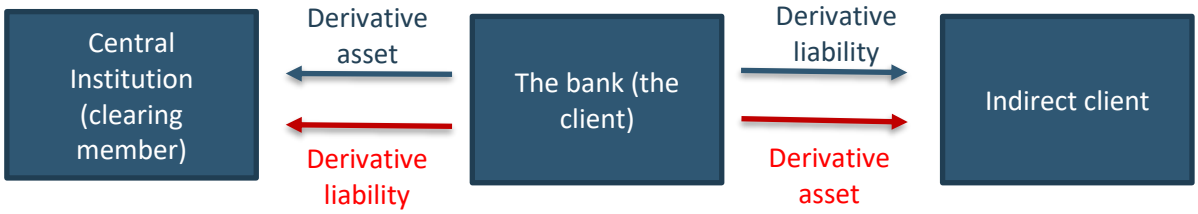
CCP	Clearing member of the CCP	Client of the clearing member	Indirect client
CCP	**IPS central institution**	**The bank**	**The bank's client**

143. The interdependent assets and liabilities reflect the market value of derivatives transactions from the customer of the bank. These amounts correspond to variation margins to cover mark-to-market losses of the participants' positions from the day before to the current day as well as additional margins to cover potential liquidation risk for the following business days.

144. The institution acts thereby as an intermediate between the customer and the central institution. Specifically,

a. If the transaction has a positive market value from the point of view of the customer then the bank has a derivative asset against the central institution and a derivative liability against the customer.

b. If the transaction has a negative market value, then the bank has a derivative asset against the customer and a liability against the central institution.



b. Analysis of the conditions in Article 428f(1)

(a) the institution acts solely as a pass-through unit to channel the funding from the liability into the corresponding interdependent asset;

145. The institution acts solely as a pass-through unit. It is ruled by contract that the bank is not liable for defaults of the central institution.

(b) the individual interdependent assets and liabilities are clearly identifiable and have the same principal amount;

146. The assets and liabilities are clearly identifiable and have the same principal amount.

(c) the asset and interdependent liability have substantially matched maturities, with a maximum delay of 20 days between the maturity of the asset and the maturity of the liability;

147. The maturities of the assets and liabilities are exactly the same.

(d) the interdependent liability has been requested pursuant to a legal, regulatory or contractual commitment and is not used to fund other assets;

148. It is guaranteed that the interdependent liability is not used to fund other assets as it is passed through immediately after maturity.

e) the principal payment flows from the asset are not used for other purposes than repaying the interdependent liability;

149. It is guaranteed that payment flows from the asset are not used for other purposes than repaying the interdependent liability as it is passed through immediately after maturity.

(f) the counterparties for each pair of interdependent assets and liabilities are not the same.

150. The counterparties for each pair of interdependent assets and liabilities are not the same.

c. Impact observed

151. If these transactions were not treated as interdependent assets and liabilities, the following treatment is foreseen:

- The derivative treatment would apply for every single transaction (each transaction is treated as a single netting set):
- That means 0% ASF for derivative liabilities and 100% RSF for derivative assets regardless of the counterparty.

152. The description provided points out that the application of Article 428f(1) hardly increases the NSFR value as of the latest data point available at the time of the discussion of the report. The impact is, hence, very low in the NSFR level.

d. Observations and recommendations

153. The EBA did not find reasons to think that any condition in Article 428f(1) might not be met in this case.

154. Point (d) of Article 428f(2) requires that the institution should not provide to its clients guarantees of the performance of the CCP in order to ensure that the institution does not incur any funding risk. The description provided shows that it is contractually established that the bank will not become liable to settle the transactions in case of default of the central institution.

155. Furthermore, in case of default of the indirect client, the bank would immediately close the respective position. The expectation is that the variation margins placed up to a point in time where the default takes place together with the additional margins placed to cover the liquidity risk for the following days would serve the purposes of closing the position of the indirect client. With this no further obligation with the CCP or the centralized institution would remain at the bank. It should be considered that the Delegated Regulation on indirect clearing arrangements

envisages mechanisms where the margins at the CCP stemming from the indirect client are clearly identified[5].

156. Therefore, the EBA considers that no funding risk seems to arise for the bank here in cases of default of any of the two counterparties, the central institution and the indirect client.

157. In this case, the central institution is not a CCP. The central institution would act as intermediary between the bank and a CCP. Article 428f(2) refers to derivative clearing activities in the context of a CCP and refers to any potential funding risk arising from the default of the CCP.

158. The Delegated Regulation on indirect clearing arrangements does not seem to reflect any obligation for the bank (client of the clearing member) in case of default (please see Article 5 of the Delegated Regulation). The obligations related to the indirect client with regards to holding assets and positions of their accounts seem to rest on the clearing member in Article 4(3). However, in this case it is already explained that contractually the bank (client of the clearing member) is exonerated from any obligation in case of default of the clearing member.

Policy recommendation

159. In view of the cases analysed, indirect derivatives client clearing activities with the central institution of an IPS as intermediary between the CCP and the final customer's bank, do not seem to pose more funding risk than in the case of direct derivatives client clearing activities between the CCP and the customer's bank as clearing member directly, provided that the customer's bank does not provide to its clients guarantees of the performance of the CCP and the central institution in the case of indirect client clearing activities.

160. With this, the EBA proposes the following amendment in point d) of Article 428f(2) (changes to the current wording of the article are underlined): *"derivative client clearing activities, provided that the institution does not provide to its clients guarantees of the performance of the CCP or of the performance of the central institution in a cooperative network or institutional protection scheme in the case of indirect derivatives client clearing activities, and~~, as a result,~~ does not incur any funding risk."*

[5] Recital 5 of the Commission Delegated Regulation (EU) 2017/2155 on indirect clearing arrangements (link) establishes "*Client clearing arrangements require offering individually segregated accounts. For indirect clearing arrangements, however, only a gross omnibus indirect account structure, with a mechanism to transfer called margin and, if agreed, margin in excess of called margin, from the indirect client all the way up to the CCP, and without allowing any netting of positions of different indirect clients in the same gross omnibus indirect account, should be required to be offered on top of omnibus indirect accounts allowing such netting. That mechanism allows for identifying, in a way equivalent to individually segregated accounts, between the collateral and the positions held for the account of a specific indirect client, on the one hand, and the collateral and the positions held for the account of the client or other indirect clients on the other.*"

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