I

(Resolutions, recommendations and opinions)

OPINIONS

EUROPEAN CENTRAL BANK

OPINION OF THE EUROPEAN CENTRAL BANK

of 6 August 2010

on a proposal for a Directive of the European Parliament and of the Council amending Directives
2006/48/EC and 2006/49/EC as regards capital requirements for the trading book and for re-
securitisations, and the supervisory review of remuneration policies

(CON/2010/65)

(2010/C 223/01)

Introduction and legal basis

On 12 November 2009, the European Central Bank (ECB) issued Opinion CON/2009/94 (1) on the
and 2006/49/EC as regards capital requirements for the trading book and for re-securitisations, and the
supervisory review of remuneration policies (hereinafter the ‘proposed directive’). On 7 July 2010, the
European Parliament adopted the proposed directive (2), which is now subject to the Council of the
European Union’s formal adoption. This opinion is based on the version of the proposed directive
adopted by the European Parliament.

The ECB’s competence to deliver an opinion is based on the last paragraph of Article 127(4) of the Treaty
on the Functioning of the European Union, according to which the ECB may submit opinions, inter alia, to
the appropriate Union institutions on matters in its fields of competence. In this respect, the proposed
directive contains provisions affecting the European System of Central Banks’ (ESCB) task to define and
implement the monetary policy of the Union, as referred to in the first indent of Article 127(2) of the
Treaty and the ESCBs’ contribution to the smooth conduct of policies relating to the stability of the financial
system, as referred to in Article 127(5) of the Treaty. In accordance with the first sentence of Article 17.5 of
the Rules of Procedure of the European Central Bank, the Governing Council has adopted this opinion.

1. General observations

1.1. The ECB is concerned about the extension of the waiver for exposures in the form of covered
bonds (3), collateralised by loans secured by residential and commercial real estate, contained in
Annex I, paragraph 2(c)(ii) to the proposed directive. The extension of the waiver from
31 December 2010 to 31 December 2013 allows unlimited use of senior units issued by securitisation
entities securitising residential and commercial real estate exposures in the cover pool of

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(3) As defined in Article 22(4) of Directive 85/611/EEC of 20 December 1985 on the coordination of laws, regulations
and administrative provisions relating to undertakings for collective investment in transferable securities (UCITS)
covered bonds. Moreover, the adopted text removes the reference to the most favourable credit quality required for these units (1).

1.2. The proposed directive, thus, affects UCITS-compliant covered bonds and asset-backed securities (ABSs) eligible for Eurosystem credit operations, as laid down in Guideline ECB/2000/7 of 31 August 2000 on monetary policy instruments and procedures of the Eurosystem (2). In this respect, the Eurosystem’s collateral framework imposes a stricter treatment from a risk management perspective, e.g. higher haircuts and rating requirements, on ABSs compared to UCITS-compliant covered bonds. A possible consequence of the proposed directive could be to provide strong incentives for monetary policy counterparties to package their ABSs into the cover pool of such covered bonds, thereby obtaining more favourable treatment, to the detriment of the Eurosystem’s risk exposure.

1.3. At the same time, and without prejudice to the ECB welcoming regulatory steps which mitigate the reliance of legislation on external ratings, the ECB has some concerns about the removal of the reference to the most favourable credit quality required for these units, as this could further undermine the credibility and transparency of the covered bonds market and, ultimately, have consequences for financial stability.

1.4. In general, the aim for the regulators in the near future should be to remove the waiver and develop a rigorous set of criteria for assets to be included in the cover pool of covered bonds which: (i) does not rely on external ratings; and (ii) is strong enough to secure market confidence in covered bonds, while allowing financial institutions sufficient time to adjust their respective business models. The reduction of the limit of the nominal amount of the outstanding issue from 20 % to 10 %, contained in Annex I, paragraph 2(c)(i) and (ii) to the proposed directive, can be seen as a positive movement in this direction.

2. Drafting proposals

Where the ECB recommends that the proposed directive is amended, specific drafting proposals are set out in the Annex accompanied by explanatory text to this effect.

Done at Frankfurt am Main, 6 August 2010.

The President of the ECB

Jean-Claude TRICHET

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ANNEX

Drafting proposals

<table>
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<tr>
<th>Text proposed by the European Parliament</th>
<th>Amendments proposed by the ECB (i)</th>
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<tbody>
<tr>
<td>Amendment</td>
<td></td>
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<td>Annex VI, point 68(ii)</td>
<td>(ii) the third paragraph is replaced by the following:</td>
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<td></td>
<td>“Until 31 December 2013, the 10 % limit for senior units issued by French Fonds Communs de Créances or by equivalent securitisation entities as specified in points (d) and (e) does not apply, provided that: (i) the securitised residential or commercial real estate exposures were originated by a member of the same consolidated group of which the issuer of the covered bonds is also a member or by an entity affiliated to the same central body to which the issuer of the covered bonds is also affiliated (that common group membership or affiliation to be determined at the time the senior units are made collateral for covered bonds); and (ii) a member of the same consolidated group of which the issuer of the covered bonds is also a member or an entity affiliated to the same central body to which the issuer of the covered bonds is also affiliated retains the whole first loss tranche supporting those senior units. Before the end of this period, and by 31 December 2012 at the latest, the Commission shall review the appropriateness of this delegation and, if relevant, the appropriateness of extending similar treatment to any other form of covered bond. In the light of that review, the Commission may, if appropriate, adopt delegated acts in accordance with the power referred to in Article 151a to extend this period or make this delegation permanent or extend it to other forms of covered bonds”:</td>
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<td>(iii) the third paragraph is replaced by the following:</td>
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<td>“Until 31 December 2013, the 10 % limit for senior units issued by French Fonds Communs de Créances or by equivalent securitisation entities as specified in points (d) and (e) does not apply, provided that: (i) those senior units have a credit assessment by a nominated ECAI, which is the most favourable category of credit assessment made by the ECAI in respect of covered bonds; (ii) the securitised residential or commercial real estate exposures were originated by a member of the same consolidated group of which the issuer of the covered bonds is also a member or by an entity affiliated to the same central body to which the issuer of the covered bonds is also affiliated (that common group membership or affiliation to be determined at the time the senior units are made collateral for covered bonds); and (iii) a member of the same consolidated group of which the issuer of the covered bonds is also a member or an entity affiliated to the same central body to which the issuer of the covered bonds is also affiliated retains the whole first loss tranche supporting those senior units. Before the end of this period, and by 31 December 2012 at the latest, the Commission shall review the appropriateness of this delegation and, if relevant, the appropriateness of extending similar treatment to any other form of covered bond. In the light of that review, the Commission may, if appropriate, adopt delegated acts in accordance with the power referred to in Article 151a to extend this period or make this delegation permanent or extend it to other forms of covered bonds.”</td>
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this requirement by using hedging strategies. For these reasons, the ECB does not consider that these requirements in themselves provide sufficient safeguards, which would warrant the inclusion of these assets in the cover pool of covered bonds. However, the ECB recognises that the requirements do provide a certain degree of protection for bondholders, especially if coupled with the reininsertion of the reference to the most favourable credit quality required for the senior units.

(1) Bold in the body of the text indicates where the ECB proposes inserting new text. Strikethrough in the body of the text indicates where the ECB proposes deleting text.