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From:	Presidency
To:	Working Party on Financial Services (MiFID-MiFIR) Working Party on Financial Services (Securitisation) Financial Services Attachés
Subject:	CMRP: Presidency note in light of discussions at VTC 17.09.20

PRESIDENCY NOTE ON THE COMMISSION'S CAPITAL MARKETS RECOVERY PACKAGE PROPOSAL IN LIGHT OF THE DISCUSSIONS AT THE LAST INFORMAL VTC

In the upcoming informal Council Working Party (CWP) videoconference on 28 September, the Presidency will continue the discussions on the MiFIR trading obligations, European Single Electronic Format (ESEF) and securitisation (Article 270 CRR). To this end, the Presidency presents the following suggestions to get a better view on how the majority of Member States (MS) intends to move forward on these issues.

I. MiFIR Trading Obligations

In the informal CWP videoconference of 3 September, MS discussed on whether or not and if so how the issue of the MiFIR trading obligations should be taken forward in the CWP on CMRP. The Commission had not included this issue in the CMRP because it is of the view that any changes to the regulatory framework related to the trading obligations for shares and derivatives (STO/DTO) at this point in time were considered untimely due to the implications such an amendment could have on the talks on the future relationship between the UK and the EU. The Commission took the view that the issue of STO should be dealt with by ESMA on the basis of the approach laid down in its MiFID II/MiFIR Review Report of 16 July 2020[1], which had found support among a large majority of national competent authorities, and until a more permanent solution would be available in the course of the MiFID/MiFIR Review in 2021.

The views in the informal CWP videoconference were divided: While to the Presidency's understanding MS in principle did not question that the STO issue might need some fixing, one group of MS supported the Commission's point of view and advocated to not further discuss the issue in the CWP on CMRP at the present time. Another group of MS showed openness to further explore the issue of STO. The views among the MS in that group, however, were split as to the question on how to take the issue forward. Whereas one group of MS held the view that the issue of STO should be further explored on the basis of the IE proposal, another group of MS was of the opinion that the ESMA approach would be a more suitable basis to go forward. Against this backdrop, the Presidency would like to inquire with MS whether or not the ESMA approach would be a suitable basis for the Council to go forward, and if so, whether it should do so at this point in time. For the sake of illustration the Presidency has included a possible drafting solution on how this approach could be implemented.

Presidency suggestion: On the basis of MS feedback, the Presidency will decide on the way forward.

Possible drafting solution:

[REGULATION (EU) No 600/2014 (MiFIR)

Article 23

Trading obligation for investment firms

1. An investment firm shall ensure the trades it undertakes in shares **with an ISIN that contains the country code of an EEA country** admitted to trading on a regulated market or traded on a trading

[1] See doc. 10026/20: ESMA MiFID II/MiFIR Review Report of 16 July 2020 on the transparency regime for equity and equity-like instruments, the double volume cap mechanism and the trading obligations for shares (ESMA70-156-2682).

venue shall take place on a regulated market, MTF or systematic internaliser, or a third-country trading venue assessed as equivalent in accordance with Article 25(4)(a) of Directive 2014/65/EU, as appropriate, unless

their characteristics include that they:

(a) are non-systematic, ad-hoc, irregular and infrequent; or are carried out on a third country trading venue in the home currency of the third country in which the trading venue is located; or

(b) are carried out between eligible and/or professional counterparties and do not contribute to the price discovery process.

The obligation laid down in the first subparagraph is satisfied in relation to trades in shares denominated in the national currency of a third country where such trades take place on a trading venue located in that third country.]

II. ESEF

In the informal CWP videoconference of 3 September, MS discussed the possibilities to postpone the date of implementation for the European Single Electronic Format (ESEF) standard. The Commission had not included any modifications to the Transparency Directive (2004/109/EC) in the CMRP, but showed openness towards addressing concerns related to the implementation of ESEF through targeted changes of the Transparency Directive. The initiative to postpone the implementation of ESEF was widely supported by MS. The Presidency therefore suggests to postpone the implementation of ESEF by one year on the basis of the Commission drafting suggestion as set out below.

Presidency suggestion: Postpone the implementation of ESEF by one year on the basis of the Commission drafting suggestion.

Commission drafting suggestion: [will be provided in a separate document]

III. Securitisation / CRR

In light of the discussions in the informal CWP videoconference of 17 September and the written comments thereafter, it is the view of the Presidency that there has been broad support for the Presidency compromise proposal to keep simple forms of committed synthetic excess spread (SES) in the list of STS-criteria for synthetic on-balance sheet securitisations as specified in Article 26e(6) of the Commission proposal for amending the SecR, but to limit the scope of Article 270 CRR to those transactions that do not involve any forms of committed SES. A relevant group of MS as well as the Commission, however, criticised the proposed exclusion of transactions with SES features from the preferential treatment status. While those MS acknowledge that SES shall remain among the STS criteria and refer to EBA's positive assessment of SES to substantiate their view,[2] they raise doubts as to whether an EU STS label for synthetic on-balance sheet securitisations would resonate in the market if

[2] According to the EBA report on the creation of an STS framework for synthetic securitisations published in April 2020, "not allowing the inclusion of SES among the STS criteria would substantially limit the use of STS balance-sheet synthetics for many asset classes" (p. 74).

SES, which is an integral part in many transactions and hence good market practice, would disqualify for the preferential regulatory treatment. It is the concern of those MS that such an STS standard might barely be used and therefore will not meet its purpose, i.e. increasing transparency and standardisation in the market. That concern was shared by the Commission.

Given the heterogeneity in MS positions, it is the view of the Presidency that – though its initial compromise proposal already points in the right direction – a more tailor-made proposal might be better suited to achieve broad agreement among MS. Such a tailor-made proposal would, on the one hand, respect the arguments in favor of the initial Commission proposal on Art. 270 CRR. On the other hand, it seeks to directly address the concerns raised about a potential misuse of SES for arbitrage reasons, i.e. using SES to avoid capital requirements. Such arbitrage concerns were raised due to the fact that there do not yet exist specific and comprehensive regulatory capital requirements for SES in the CRR.

After thorough discussions with the EBA and the Commission and following comments from few MS and the Commission during the last CWP videoconference, the Presidency therefore proposes to keep the scope of Art 270 CRR as proposed by the Commission and to introduce provisions for a prudential treatment of SES in the CRR. This means that all forms of SES would be subject to capital requirements. Such an approach would leverage on the detailed work by the EBA in its report[3] on significant risk transfer at EU level as well as work on the matter within the Basel Committee on Banking Supervision (BCBS) at international level.

The introduction of a capital treatment for SES transactions would require further technical work, notably with regard to Article 248 (exposure value) and Art. 256 CRR (attachment and detachment point). Such work would clarify how the exposure value of SES is to be determined and thus ensure that all forms of SES constitute (on or off) balance sheet exposures which would, subsequently, be risk weighted. While the risk weighting could follow the general treatment of first loss tranches, i.e. a 1250% risk weight with the possibility to offset it with credit loss provisions for the securitised exposures, the EBA would be mandated to develop a RTS regarding the determination of the exposure value, for which the level 1 text would work out detailed criteria. EBA and Commission will explain this approach in the CWP. The provisions would then be subject to adjustments to latest assessments and international standards as part of the general review foreseen in 2022.

Overall, the Presidency takes the view that such an approach could strike the right balance between MS that are expressed concern with respect to arbitrage possibilities and others which considered the exclusion from a preferential capital treatment detrimental to the usability of SES. Even though such an approach would require further technical work, the Presidency therefore sees merit in seeking views whether such an approach should be further explored in view of MS.

Presidency suggestion: Do MS agree to conduct further technical work alongside the principles outlined above, i.e. to introduce a dedicated capital treatment for SES, as an appropriate compromise solution?

[3] The report will be published in due course but since work on it is already advanced, main insights of it could be used to inform the current debate in Council. In light of this EBA has offered its support to find an agreement in Council.