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COMMISSION OF THE EUROPEAN COMMUNITIES

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Proposal for a

DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

amending Directives 2006/48/EC and 2006/49/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management

{SEC(2008) 2532}
{SEC(2008) 2533}

EXPLANATORY MEMORANDUM

1. CONTEXT OF THE PROPOSAL

A single financial market in the EU is a key factor in promoting the competitiveness of the European economy and the lowering of the capital cost to companies. The Financial Services Action Plan 1999-2005 (FSAP) aimed at laying the foundations for a strong financial market in the EU by pursuing three strategic objectives:

- ensuring a Single Market for wholesale financial services;
- open and secure retail markets and
- state-of-the-art prudential rules and supervision;

In this context, based on the 'Basel II' G-10 agreement, a new capital requirements framework was adopted in June 2006 as the Capital Requirements Directive (CRD); this comprises Directives 2006/48/EC and 2006/49/EC. The overarching goal of the current proposal is to ensure that the effectiveness of the Capital Requirements Directive is not compromised. The revision relates to:

- Revisions of rules that were brought forward from previous directives, such as the large exposures regime and derogations for bank networks from prudential requirements;
- Establishing principles and rules that had not been formalised at the EU level such as the treatment of hybrid capital instruments within original own funds;
- Clarifying the supervisory framework for crisis management and establishing colleges for enhancing both efficiency and effectiveness of supervision.

The revision of certain other areas has been prompted by the financial market turbulence that started in 2007 and is aimed at ensuring adequate protection of creditor interests and overall financial stability.

Inconsistencies that have been identified during the transposition phase of the CRD need to be addressed to ensure that the effectiveness of the underlying goals of the CRD is not compromised. The majority of these are of a technical nature and have been covered by separate comitology measures.

2. CONSULTATION OF INTERESTED PARTIES

An open Internet consultation was conducted from 16 April to 17 June 2008. The Commission received 118 responses. With the exception of those declared confidential by the respondents, all responses are available under:

http://circa.europa.eu/Public/irc/markt/markt_consultations/library?l=/financial_services/cross-sector_issues&vm=detailed&sb=Title

Three issues have been raised by many respondents and therefore merit particular attention.

2.1. Large inter-bank exposures

The Commission believes that inter-bank exposures are not risk-free and should be prudently managed. The Commission proposes to limit all inter-bank exposures to 25% of own funds or an alternative threshold of EUR 150 million, whichever is higher.

2.2. Capital Requirements for Securitisation

The consultation paper included a requirement that originators must hold a certain percentage of capital for the exposures that they securitize. In response to the consultation, it is now proposed to require that originators and sponsors retain a share of the risks and that investors ensure that this has indeed been respected. Considering the responses to a further public consultation, the Commission maintains its imperative for a demonstrable measure of due diligence and rigour in the case of the 'originate to distribute' business model.

2.3. Colleges of Supervisors

The consultation paper introduced the need to establish 'colleges' of supervisors for all cross-border banks and required supervisors participating in those colleges to discuss and agree on specific issues with a non-binding mediation mechanism via the Committee of European Banking Supervisors (CEBS) without changing the allocation of responsibilities between home and host supervisors.

This proposal was seen as unsatisfactory by most stakeholders for different reasons.

It is key that colleges remain effective and efficient for the supervision of banking groups. Therefore, the Commission considers that the increased information flows should be accompanied by the eventual decision for two key aspects being entrusted to the consolidating supervisor (Pillar 2 capital requirements and reporting requirements).

2.4. Expertise

From 2005 to 2007, the Commission issued several calls for advice to CEBS on hybrid capital instruments and large exposures. As to hybrid capital instruments, CEBS proposed conditions that any hybrid instrument should meet in order to be considered to be eligible Tier 1 capital in the EU. Concerning large exposures, CEBS made suggestions on definitions, the scope of application of the large exposures regime, exposure limits and the calculation of exposure values. The principles set out in their responses were broadly taken into account. CEBS' advice is published on the following web site:

http://www.c-ebs.org/Advice/advice.htm

The Commission services also established a working group with members nominated by the EBC, which in 2007 and 2008 conducted meetings that stretched over nine days. The EBC endorsed a draft of this proposal at its meeting on 20 June 2008.

3. IMPACT ASSESSMENT

The impact assessment report is accessible on the following web site:

http://ec.europa.eu/internal_market/bank/regcapital/index_en.htm#capitalrequire

Altogether, over 60 different policy options have been assessed. The below summary describes the preferred policy options in each of the six issue areas covered by the impact assessment and their expected impact on key stakeholders.

3.1. Large exposures

An amended limit-based backstop regime is considered to be most effective as it is specifically tailored to respond to the identified shortcomings of the current regime. Furthermore, the distribution of costs and benefits among stakeholder groups under this option is the most consistent. Banking industry is expected to see savings in administrative burden brought about by a more harmonized regime and its closer alignment with the solvency regime. Certain types of investment firms will be exempted from the scope of the regime. Importantly, financial stability will be enhanced by the certainty that a maximum exposure of a given credit institution to a third party is limited.

3.2. Hybrid capital instruments

A common regulatory European framework would address the shortcomings of the current situation by facilitating convergence between Member States and sectors, consequently contributing to stronger level playing field conditions within the single market. Clear EU regulation will improve the quality of capital from an industry and supervisory perspective, while providing more choice and liquidity to investors.

3.3. Home-host issues and crisis management arrangements

Colleges comprising authorities supervising group entities in different Member States will address potential conflict and supervisory overlap. This will be aided by reinforced powers of the consolidating supervisor. In crisis situations, stakeholders will benefit from enhanced supervisory cooperation and a clearer allocation of responsibilities. Mediation mechanisms will ensure conflict resolution while regular exchanges will allow for early detection of financial stress.

3.4. Derogations for bank networks from certain prudential requirements

It is appropriate to "regularize" the situation in the Member States that have implemented the derogations under Article 3 of the CRD in their legal systems after the time limits. For other Member States, this may open a possibility for EU bank networks with assets over € 331 billion and representing more than 5 million members to qualify for the supervisory treatment under the article. Such networks typically consist of cooperative banks even though Article 3 is not limited to them.

3.5. Treatment of Collective Investment Undertakings (CIUs) under the Internal Ratings Based (IRB) Approach

Applying more targeted increases to the Standardized risk-weights would provide for a sound and risk-sensitive alternative treatment of exposures in CIUs, whereby the percentage increase in risk weights would be lower for well-rated exposures and higher for lower-rated and unrated exposures.

3.6. Capital requirements and risk management for securitization positions

Potential conflicts of interest in the 'originate to distribute' model should be addressed by making sure originators and sponsors of credit risk transfer retain some share of the risks they have underwritten. For this reason, investors will be required to ensure that originators and sponsors retain a material share of the risks and in any event not less than 5 per cent of the total so that effectively, equally originators and sponsors that are regulated by the CRD and those that are not regulated by it will have to retain a share of the risks. A stronger and more rigorous securitization framework including more rigorous due diligence should contribute towards more responsible underwriting and avoidance of a repeat of the enormous costs that have been borne by investors and financial institutions over the past 18 months.

4. LEGAL ELEMENTS OF THE PROPOSAL

A Directive amending the current directives is the most appropriate instrument. The proposal is based on Article 47(2) of the Treaty, which is the legal basis to adopt Community measures aimed at achieving the Internal Market in financial services.

In accordance with the principles of subsidiarity and proportionality as set out in Article 5 EC, the objectives of the proposed action, cannot be sufficiently achieved by the Member States and can therefore be better achieved by the Community. Its provisions do not go beyond what it is necessary to achieve the objectives pursued.

Only Community legislation can ensure that credit institutions and groups of credit institutions operating in more than one Member State are subject to the same requirements of prudential supervision, which ensures a level playing-field, avoids unwarranted compliance costs for cross-border activities and thereby promotes further single market integration. Community action also ensures a high level of financial stability within the EU.

This proposal does not increase administrative burden for Member States or economic operators. On the contrary, the large exposure regime is simplified and reporting requirements reduced. The harmonisation of the treatment of hybrid capital instruments also leads to a simplification and therefore to a reduction of administrative burden for banks operating cross-border.

5. BUDGETARY IMPLICATION

The proposal has no implication for the Community budget.

6. DETAILED EXPLANATION OF THE PROPOSAL

6.1. Hybrid capital (Chapter 2 Section 1 of Directive 2006/48/EC)

Hybrid capital instruments (hybrids) are securities that contain features of both equity and debt. The purpose of issuing such instruments is to cover capital needs of banks while appealing to an investor class who is willing to take more risk than in fixed income (debt) products and who therefore also expect higher returns. These instruments are usually designed in a way aiming at ensuring their qualification as 'original own funds' for regulatory purposes.

The lack of legislation at EU level has lead to diverging eligibility criteria and limits throughout the EU. This results in the lack of a level playing field and the possibility of regulatory arbitrage for banks operating within the single market area as the differences in treatment between Member States impact the issuance costs of hybrid capital instruments.

6.1.1. Distinction between the "core" component of banks' own funds and hybrids eligible in banks' original own funds (Article 57 points (a) and (ca) of Directive 2006/48/EC)

To date, there is no clear terminology for describing hybrid instruments eligible as banks' original own funds ('tier 1 capital'). Since a list of specific instruments in the Directive would quickly be outdated because of constant innovation, principles have been developed, which define hybrids eligible for original own funds.

Core capital within banks' original own funds includes all instruments that are referred to in the national definition of equity capital, fully absorb losses on a going concern basis and represent the most subordinated claim during liquidation. More particularly, these instruments should represent the "last line of defence" for any bank both during normal times and liquidation. Usually these instruments are common shares and corresponding premiums but, more generally, any type of instrument not providing preferential rights in case of negative economic performance.

However, there are also instruments not falling within this scope such as preference shares that create preferential rights for dividend payments and liquidation, which thus are included in the category of hybrids.

6.1.2. Eligibility criteria (Article 63a of Directive 2006/48/EC)

For hybrids to be recognised as 'original own funds', they need to absorb losses, permit the cancellation of payment in times of stress, be deeply subordinated during liquidation and must be permanently available so that there is no doubt that it can support depositors and other creditors in times of stress. These criteria were agreed at the G10 level and announced in a Press Release in 1998 but they have not been transposed into EU legislation. Eligible instruments meet the permanence test if they are either undated or their original maturity is longer than 30 years. They can however be callable earlier but only at the initiative of the issuer, with supervisory approval and if they are replaced with capital of the same quality, unless the supervisor determines that there is adequate capital. Supervisors should also be empowered to suspend the redemption of dated instruments depending on the solvency of the bank.

Eligible instruments should also allow to cancel payments or to redeem them so long as minimum capital requirements are complied with. Eligible instruments must not be cumulative, i.e. any unpaid amount should be forfeited and no longer due and payable. However, an alternative payment in kind mechanism should be allowed (e.g. by issuing new shares) under strict conditions set by supervisors (the relevant costs being borne by shareholders through dilution of their stakes)

Eligible instruments should absorb losses during liquidation but also help the institution to continue operations on a going concern basis and they should not hinder the recapitalisation of the issuer. Thus, hybrids should be senior only to ordinary share capital and junior to hybrids included in bank's *additional* own funds.

6.1.3. Quantitative limits (Article 66 of Directive 2006/48/EC)

Banks and investment firms should not extensively rely on hybrid capital instruments to the detriment of "core" components indicated in Article 57 (a). To this end, the Commission proposes a limit structure allowing for different categories.

The main criterion for distinction between categories, the convertibility of hybrids in case of need, provides an incentive to develop hybrids that lead to higher quality of capital during crises (i.e. by a higher share of core capital). Supervisory authorities may temporarily waive the limits in emergency situations.

The most subordinated instruments of a credit institution that does not have proprietors or shareholders under national law, such as the members' certificates of some cooperative banks, should be treated like convertible hybrids insofar as the respective capital has been paid up and ranks after all other claims.

6.1.4. Transitional provisions (Article 154 paragraphs 8 and 9 of Directive 2006/48/EC)

The Commission acknowledges the importance of hybrids as a major source of funding and the need to limit the impact of the new regulation. To this end, the proposal allows firms not complying with the new set of quantitative limits to gradually adjust to the new rules over a period of 30 years.

6.1.5. Disclosure provisions (Annex XII, Part 2, points 3 (a) and (b) of Directive 2006/48/EC)

Following the establishment of criteria for hybrid capital instruments to be eligible for original own funds, Annex XII needs to be amended accordingly. These changes shall be included in this proposal. Banks are required to disclose specific information on hybrids, particularly on those eligible only within the transitional period.

6.2. Large exposures

The current CRD provisions are based on the general assumption that banks spread their exposures to their clients. However despite this, institutions could still be exposed to the same client or a group of connected clients. In extreme situations, this can lead to the loss of the full exposure or of its part. The aim of the large exposures regime is to prevent an institution from incurring disproportionately large losses as a result of the failure of an individual client (or a group of connected clients) due to the occurrence of unforeseen events. To address this, the European Commission issued a recommendation[1] in 1987, followed by a directive[2] in 1992. Given their limited number and extent of changes made at the time of the CRD adoption, the large exposures regime has not been reviewed for 16 years. In recognition of this fact, Article 119 of 2006/48/EC and Article 28(3) of 2006/49/EC require a more in-depth review of the existing requirements "together with any appropriate proposals" to be submitted to the European Parliament and to the Council.

The current CRD provisions show several shortcomings: high costs for the industry including unwarranted compliance costs for certain types of investment firms, lack of clarity and a level

[1] Recommendation 87/62/EEC on monitoring and controlling large exposures of credit institutions.
[2] Directive on the monitoring and control of large exposures of credit institutions 92/121/EEC.

playing field. In addition, the current regime does not effectively address market failure pertaining to certain exposure types (e.g. exposures to institutions), implying a higher burden for taxpayers and capital inefficiencies. These shortcomings are addressed by deleting national discretions where possible, exempting certain types of investment firms from the regime, aligning applied methods closer to methods applied for capital adequacy purposes, strengthening legal certainty by clarifying definitions and adjusting the treatment of certain types of exposures, (e.g. exposures to institutions).

6.2.1. Definitions (Article 4 point 45 and article 106 of Directive 2006/48/EC)

As to the concept of connected clients defined in Article 4, until now, the supervisory authorities have focused only on the asset side of the entities in question in order to identify whether one entity may encounter repayment difficulties because of the financial problems of the other entity. The recent market developments have shown that two or more undertakings can be financially dependant (and pose significant risks) because they are funded by the same vehicle. As a result, this proposal takes into account not only the risk that derives from the business and assets of two entities but also from their liability or funding side.

6.2.2. Simplification of the large exposures regime (Chapter 2 Section 5 of Directive 2006/48/EC)

Reporting requirements in Article 110 have been simplified and harmonised. This was one of the major industry complaints about the current regime. The requirement for interim reporting has been removed and institutions making use of the IRB approach have to report their 20 largest, not exempted, exposures on a consolidated basis.

The current limits for large exposures are manifold. This structure is simplified in Article 111 into a single limit of 25%.

The list of exemptions in Article 113 is currently long and creates burdensome differences across member states and the lack of a level playing field. The only exemptions which remain are exposures to sovereigns and regional governments and local authorities, those reflecting the typical nature of cooperative banks, intra-group exposures if exempted under the solvency regime, exposures secured by certain collateral and exposures arising from undrawn credit facilities provided that the credit facility actually drawn does not exceed the prescribed limit.

The current use of different calculation methods and risk mitigation methods has not enhanced the transparency of the results to be assessed by financial firms and their supervisors. In Articles 114, 115 and 117 the methods are clarified and aligned as much as possible to the methods applied for the capital adequacy regime. In order to increase firms' flexibility, the current national discretions to apply the respective methods have been transformed into options for the institutions themselves.

6.2.3. Interbank exposures (Article 111 of Directive 2006/48/EC)

Inter-bank exposures pose a significant risk as banks, although regulated, can fail. A failure of one institution can cause a failure of other institutions with the possibility of causing systemic crisis. For this reason, large inter-bank exposures require very prudent management. As a traumatic loss from an exposure to an institution can be as severe as from any other exposure, the Commission has concluded that the current regime, based on a complex mix of risk weights and differentiation on maturity, is not sufficiently prudent. Against this background, the Commission, having reflected on the outcome of the analysis investigating costs and benefits of several available regulatory approaches, has concluded that there is a merit to treat inter-bank exposures as any other exposures, regardless of their maturity. The Commission has addressed specific concerns by allowing an alternative threshold of EUR 150 million and waivers for banks operating in networks, savings banks under certain conditions and certain types of exposures related to clearing and settlement transactions.

6.2.4. Waiver for certain investment firms (Article 28 of Directive 2006/49/EC)

The current regime imposes unwarranted compliance cost burdens on investment firms without delivering any apparent societal benefits. Therefore, it is proposed to waive investment firms 'with limited license' and 'limited activities' from the large exposure regime in Directive 2006/49/EC.

6.3. Supervisory arrangements

6.3.1. Information exchange and cooperation – Articles 40, 42a, 42b, 49 and 50 of Directive 2006/48

In emergency situations, smooth and unfettered multilateral exchange of information is of particular relevance. This is why it is proposed to improve information rights of host country supervisors of systemically relevant branches in Article 42a and to specify in Article 49 and 50 the legal framework for transmitting information to ministries of finance and central banks.

The proposal provides for a definition of 'systemically relevant branches' in Article 42a. Access to relevant information would be facilitated by the involvement of supervisors of systemically relevant branches in colleges of supervisors. This participation will be decided by the consolidating supervisor depending on the issues to be discussed.

By requesting authorities to have regard to the implication of their decisions on the financial stability in other Member States, Article 40(3) outlines a European dimension in supervisory decisions which is key to underpinning cooperation between authorities.

6.3.2. Colleges of supervisors - Articles 42a, 129 and 131a (new) of Directive 2006/48

The suggested amendments aim at reinforcing the efficiency and effectiveness of supervision of cross-border banking groups by requiring:

- the establishment of colleges of supervisors to facilitate the tasks of the consolidating supervisor and host supervisors,

- a joint decision on two key supervisory aspects for group supervision (Pillar 2 and reporting requirements) with a last say for the consolidating supervisors. This is coupled with a mediation mechanism in case of disagreement.

- the competent authorities involved in the supervision of a group to consistently apply within a banking group the prudential requirements under the Directive.

The consolidating supervisors will be required to inform CEBS on the activities of colleges to develop consistent approaches across colleges. Colleges will also be required for supervisors overseeing cross-border entities that do not have subsidiaries in other Member States but that do have systemically important branches.

6.4. Technical amendments

6.4.1. Derogations for credit institutions affiliated to a central institution (Article 3 of Directive 2006/48/EC)

In Article 3 of Directive 2006/48/EC, it is proposed to delete the time limits (dates of 15 December 1977 and of 15 December 1979) that restrict its application. The recent accession of new Member States revealed the need to make the derogations in this Article available to all Member States and not only to those that have joined the EU three decades ago.

6.4.2. Capital requirements for investments in Collective Investment Undertakings (Article 87 of Directive 2006/48/EC)

Credit institutions felt that the capital requirements for investments in Collective Investment Undertakings (CIU) such as mutual funds were too strict under the IRB approach in those cases where banks cannot or do not want to provide internal rating for the exposure held by the CIU. The proposal considerably lowers the capital requirements for less risky assets held by the CIU but maintains high capital charges where the assets are either high risk or the actual risk is not known. This also continues to provide a disincentive to hide unknown risks on a bank's balance sheet behind investments in CIU without adequate capital requirements.

6.4.3. Securitisation (new Article 122a of Directive 2006/48/EC)

Potential conflicts of interest in the "originate to distribute" model must be addressed by making sure that originators and sponsors of the more opaque credit risk transfer instruments retain a proportion of the risk that is being transferred to investors. For this reason, it should be required from investors to make sure that originators and sponsors retain a material share (not less than 5 per cent) of the risks so that effectively, equally originators and sponsors that are regulated by this directive and those that are not regulated by this directive will have to retain a share of the risks for their own account. This requirement should be complemented by ensuring that investors have a thorough understanding of the underlying risks and the complex structural features of what they are buying. To enable informed decisions, detailed information has to be available to investors.

6.4.4. Counterparty credit risk (Annex III and Article 150 of Directive 2006/48/EC

This Annex lays out the details of the methods to calculate capital requirements for counterparty credit risk. The technical amendments proposed aim at ironing out a number of difficulties identified during the transposition phase of the CRD. The changes do not materially alter the content of the annex but clarify and streamline its application.

Future technical amendments of Annex III should be adopted under the comitology procedure. Currently, the powers of execution do not explicitly refer to this annex.

6.4.5. Liquidity risk (Annexes V and XI of Directive 2006/48/EC)

The current market turmoil has highlighted the fact that liquidity is a key determinant of the soundness of the banking sector.

The proposed changes implement the work conducted by CEBS and the Basel Committee on Banking Supervision to develop sound principles for liquidity risk management. The proposed changes to Annex V highlight the need for the board of directors to set an appropriate level of liquidity risk tolerance. The proposed changes to Annex XI aim at ensuring a proper incentive for banks to better understand their liquidity risk profile. It requires national supervisors to facilitate firms' understanding of their liquidity risk profiles, and does not exclude the possibility of relying to some extent on internal methodologies for supervisory purposes.

Given the significant changes introduced by these modifications, it is appropriate to include these amendments in this proposal.

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amending Directives 2006/48/EC and 2006/49/EC as regards banks affiliated to central institutions, certain own funds items, large exposures, supervisory arrangements, and crisis management

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty establishing the European Community, and in particular Article 47(2) thereof,

Having regard to the proposal from the Commission[3],

Having regard to the opinion of the European Economic and Social Committee[4],

Having regard to the opinion of the European Central Bank[5],

Having regard to the opinion of the Committee of the Regions[6],

Acting in accordance with the procedure laid down in Article 251 of the Treaty[7],

Whereas:

(1) Article 3 of Directive 2006/48/EC of the European Parliament and of the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions[8] allows Member States to provide for special prudential regimes for credit institutions which are permanently affiliated to a central body since 15 December 1977, provided that those regimes were introduced in national laws no later than 15 December 1979. Those time limits prevent Member States, especially those which have acceded to the European Union since 1980, to introduce the same regimes for similar affiliations of credit institutions which have been set up later on their territories. It is therefore appropriate to remove the time limits set out in Article 3, in order to ensure equal conditions for competition between credit institutions in Member States. The Committee of European Banking Supervisors should provide for non-binding guidelines in order to enhance the convergence of supervisory practices in this regard.

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3 OJ C , , p. .
4 OJ C , , p. .
5 OJ C , , p. .
6 OJ C , , p. .
7 OJ C , , p. .
8 OJ L 177, 30.6.2006, p. 1.

(2) Hybrid capital instruments play an important role in the ongoing capital management of credit institutions. Those instruments allow credit institutions to achieve a diversified capital structure and to access a wide range of financial investors. On 28 October 1998, the Basel Committee on Banking Supervision adopted an agreement on both the eligibility criteria and limits to inclusion of certain types of hybrid capital instruments into original own funds of credit institutions.

(3) Therefore, it is important to lay down criteria for those capital instruments to be eligible for original own funds of credit institutions and to align the provisions in Directive 2006/48/EC to that agreement. The amendments to Annex XII to Directive 2006/48/EC result directly from the establishment of those criteria. The eligibility criteria should refer to the most subordinated instruments of a credit institution that does not have proprietors or shareholders under national law, such as certain members' certificates of cooperative banks, insofar as the respective capital has been paid up and ranks after all other claims.

(4) In order to avoid disruption of markets and to ensure continuity in overall levels of own funds it is appropriate to provide for specific transitional arrangements for the new regime on hybrid capital instruments.

(5) For the purpose of strengthening the crisis management framework of the Community, it is essential that competent authorities coordinate their actions with other competent authorities and where appropriate with central banks in an efficient way. In order to strengthen the efficiency of prudential supervision of parent credit institutions authorised in the Community and to allow competent authorities to better carry out the supervision of a banking group on a consolidated basis, supervisory activities should be coordinated in a more effective manner. Therefore, Colleges of Supervisors should be established. The establishment of colleges should not affect the rights and responsibilities of the competent authorities under Directive 2006/48/EC. Their establishment should be an instrument for stronger cooperation whereby competent authorities reach agreement on key supervisory tasks. The colleges should facilitate the handling of ongoing supervision and emergency situations. The consolidating supervisor may, in association with the other members of the college, decide to organise meetings or activities that are not of general interest and therefore streamline the attendance as appropriate.

(6) The mandates of competent authorities should take into account a Community dimension. Competent authorities should therefore take into account the effect of their decisions on the stability of the financial system in all other Member States.

(7) Competent authorities should be able to participate in colleges established for the supervision of credit institutions the parent institution of which is situated in a third country. The Committee of European Banking Supervisors should provide, where necessary, for non-binding guidelines and recommendations in order to enhance the convergence of supervisory practices pursuant to Directive 2006/48/EC.

(8) Information deficits between the home and the host competent authorities may prove detrimental to the financial stability in host Member states. The information rights of host supervisors, in particular in a crisis of systemically relevant branches, should therefore be reinforced. For that purpose, systemically relevant branches should be defined. Competent authorities should transmit information which is essential for the

pursuance of tasks of central banks and of Ministries of Finance with respect to financial crises.

(9) Excessive concentration of exposures to a single client or group of connected clients may result in an unacceptable risk of loss. Such a situation can be considered prejudicial to the solvency of a credit institution. The monitoring and control of large exposures of credit institution should therefore be an integral part of its supervision.

(10) The current large exposure regime dates back to 1992. Therefore, the existing requirements on large exposure set out in Directive 2006/48/EC and Directive 2006/49/EC of the European Parliament and of the Council of 14 June 2006 on the capital adequacy of investment firms and credit institutions[9] should be reviewed.

(11) Since credit institutions in the internal market are engaged in direct competition, the essential rules for monitoring and control of large exposures of credit institutions should be further harmonised. In order to reduce administrative burden for credit institutions the number of options for Members States as far as large exposures are concerned should be reduced.

(12) In determining the existence of a group of connected clients and thus exposures constituting a single risk, it is important to take into account also risks arising from a common source of significant funding provided by the credit institution or investment firm itself, its financial group or its connected parties.

(13) While it is desirable to base the calculation of the exposure value on that provided for the purposes of minimum own funds requirements, it is appropriate to adopt rules for the monitoring of large exposures without applying risk weightings or degrees of risk. Moreover, the credit risk mitigation techniques applied in the solvency regime were designed with the assumption of a well-diversified credit risk. In case of large exposures, dealing with single name concentration risk, credit risk is not well-diversified. Therefore effects of those techniques should be subject to prudential safeguards. In this context, it is necessary to provide for an effective recovery of the credit protection for the purposes of large exposures.

(14) Since a loss arising from an exposure to a credit institutions or an investment firm can be as severe as a loss from any other exposure, such exposures should be treated and reported as any other exposures.

(15) It is important to remove misalignment between the interest of firms that 're-package' loans into tradable securities and other financial instruments (originators) and firms that invest in these securities or instruments (investors). It is therefore important for originators to retain exposure to the risk of the loans in question. In particular where credit risk is transferred by securitisation, investors should make their decisions only after conducting thorough due diligence, for which they need adequate information about the securitisations.

(16) Annex III to Directive 2006/48/EC should be adapted in order to clarify certain provisions with a view to enhance convergence of supervisory practices.

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9 OJ L 177, 30.6.2006, p. 201.

(17) Recent market developments have highlighted the fact that liquidity risk management is a key determinant of the soundness of credit institutions. The criteria set out in Annex V and XI to Directive 2006/48/EC should be reinforced in order to align those provisions to the work conducted by the Committee of European Banking Supervisors and the Basel Committee on Banking Supervision.

(18) The measures necessary for the implementation of Directive 2006/48/EC should be adopted in accordance with Council Decision 1999/468/EC of 28 June 1999 laying down the procedures for the exercise of implementing powers conferred on the Commission[10].

(19) In particular the Commission should be empowered to amend Annex III of Directive 2006/48/EC in order to take account of developments on financial markets or in accounting standards or requirements which take account of Community legislation, or with regard to convergence of supervisory practice and to alter the percentage specified in Article 111(1) of that Directive to take account of developments on financial markets. Since those measures are of general scope and are designed to amend non-essential elements of Directive 2006/48/EC, they must be adopted in accordance with the regulatory procedure with scrutiny provided for in Article 5a of Decision 1999/468/EC.

(20) Since the objectives of the proposed action, namely the introduction of rules concerning the taking up and pursuit of the business of credit institutions, and their prudential supervision, cannot be sufficiently achieved by the Member States because it requires the harmonisation of a multitude of different rules existing in the legal systems of the various Member States and can therefore be better achieved at Community level, the Community may adopt measures, in accordance with the principle of subsidiarity as set out in Article 5 of the Treaty. In accordance with the principle of proportionality, as set out in that Article, this Directive does not go beyond what is necessary in order to achieve those objectives.

(21) Directives 2006/48/EC and 2006/49/EC should therefore be amended accordingly,

HAVE ADOPTED THIS DIRECTIVE:

Article 1

Amendments to Directive 2006/48/EC

Directive 2006/48/EC is amended as follows:

1. Article 3(1) is amended as follows:

(a) The introductory phrase in the first subparagraph is replaced by the following:

"One or more credit institutions situated in the same Member State and which are permanently affiliated to a central body which supervises them and which is

[10] OJ L184, 17.7.1999, p. 23.

established in the same Member State, may be exempted from the requirements of Articles 7 and 11(1) if national law provides that:"

(b) The second and third subparagraphs are deleted.

2. Article 4 is amended as follows:

(a) Point (6) is replaced by the following:

"(6) 'institutions' for the purposes of Sections 2, 3 and 5 of Title V, Chapter 2, means institutions as defined in Article 3(1)(c) of Directive 2006/49/EC;"

(b) Point (45)(b) is replaced by the following:

"(b) two or more natural or legal persons between whom there is no relationship of control as set out in point (a) but who are to be regarded as constituting a single risk because they are so interconnected that, if one of them were to experience financial problems, in particular funding or repayment difficulties, the other or all of the others would be likely to encounter funding or repayment difficulties."

(c) Point (48) is added:

"(48) 'consolidating supervisor' means the competent authority responsible for the exercise of supervision on a consolidated basis of EU parent credit institutions and credit institutions controlled by EU parent financial holding companies."

3. In Article 40 the following paragraph 3 is added:

"3. The competent authorities in one Member State shall take into account to the potential impact of their decisions on the stability of the financial system in all other Member States concerned and, in particular, in emergency situations."

4. The following Article 42a is inserted:

"Article 42a

1. The competent authorities of a host Member State may make a request to the consolidating supervisor where Article 129 (1) applies or to the competent authorities of the home Member State, for a branch of a credit institution to be considered as systemically relevant.

The request shall provide reasons for considering the branch to be systemically relevant with particular regard to the following:

(a) whether the market share of the branch of a credit institution in terms of deposit exceeds 2% in the host Member State;

(b) the likely impact of a suspension or closure of the operations of the credit institution on the payment and clearing and settlement systems in the host Member State;

(c) the size and the importance of the branch in terms of number of clients within the context of banking or financial system of the host Member State.

The competent authorities of the home and the host Member State, and the consolidating supervisor where Article 129(1) applies, shall do everything within their power to reach a joint decision on the designation of branches as being systemically relevant.

If no joint decision is reached within two months of receipt of a request under the first subparagraph, the competent authorities of the host Member State shall take their own decision within a further period of two months on whether the branch is systemically relevant. In taking its decision, it shall take into account any views and reservations of the consolidating supervisor or the competent authorities of the home Member State.

The decisions referred to in the third and fourth subparagraph shall be set out in a document containing the fully reasoned decision, transmitted to the competent authorities concerned, recognised as determinative and applied by the competent authorities in the Member States concerned.

The designation of a branch as being systemically relevant shall not affect the rights and responsibilities of the competent authorities under this Directive.

2. The competent authorities of the home Member State shall communicate to the competent authorities of a host Member State where a systemically relevant branch is established the information referred to in Article 132(1)(c) and (d) and carry out the tasks referred to in Article 129(1)(c) in cooperation with the competent authorities of the host Member State.

If a competent authority of a home Member State becomes aware of an emergency situation within a credit institution as referred to in Article 130(1), it shall alert as soon as practicable the authorities referred to in the fourth paragraph of Article 49 and in Article 50.

3. Where Article 131a does not apply, the competent authorities supervising a credit institution with systemically relevant branches in other Member States shall establish and chair a college of supervisors to facilitate the cooperation under Article 42 and paragraph 2 of this Article. The establishment and functioning of the college shall be based on written arrangements determined, after consultation with competent authorities concerned, by the competent authorities of the home Member State."

5. The following Article 42b is inserted:

"Article 42b

1. In the exercise of their duties, competent authorities shall take into account the convergence in respect of supervisory tools and supervisory practices in the application of the laws, regulations and administrative requirements adopted pursuant to this Directive. For that purpose, Member States shall ensure that the competent authorities participate in the activities of the Committee of European Banking Supervisors and take into account its non-binding guidelines and recommendations.

2. The Committee of European Banking Supervisors shall report to the Council, the European Parliament and the European Commission on the progress made towards supervisory convergence every three years starting from 31 December 2010."

6. Article 49 is amended as follows:

(a) In the first paragraph, point (a) is replaced by the following:

"(a) central banks and other bodies with a similar function in their capacity as monetary authorities when this information is relevant for the exercise of their respective statutory tasks, including the conduct of monetary policy, the oversight of payments and securities settlement systems, and the safeguarding of financial stability ; and"

(b) The following paragraph is added:

"In an emergency situation as referred to in Article 130(1), Member States shall allow competent authorities to communicate information to central banks in the Community when this information is relevant for the exercise of their respective statutory tasks, including the conduct of monetary policy, the oversight of payments and securities settlement systems, and the safeguarding of financial stability."

7. In Article 50, the following paragraph is added:

"In an emergency situation as referred to in Article 130(1), Member States shall allow competent authorities to disclose information to the departments referred to in the first paragraph in all Member States concerned."

8. Article 57 is amended as follows:

(a) Point (a) is replaced by the following:

"(a) capital within the meaning of Article 22 of Directive 86/635/EEC, in so far as it has been paid up, plus the related share premium accounts, it fully absorbs losses in going concern situations, and in the event of bankruptcy or liquidation ranks after all other claims."

(b) The following point (ca) is inserted:

"(ca) "instruments other than those referred to in point (a), which meet the requirements set out in points (a), (c), (d) and (e) of Article 63 (2) and in Article 63a;"

9. The first paragraph of Article 61 is replaced by the following:

"The concept of own funds as defined in points (a) to (h) of Article 57 embodies a maximum number of items and amounts. Member States may decide on the use of those items and on the deduction of items other than those listed in points (i) to (r) of Article 57."

10. In Article 63(2), the following subparagraph is added:

"Instruments referred to in point (ca) of Article 57 shall comply with the requirements set out in points (a), (c), (d) and (e) of this Article."

11. The following Article 63a is inserted:

"Article 63a

"1. Instruments referred to in point (ca) of Article 57 shall comply with the requirements set out in paragraph 2 to 5 of this Article.

2. The instruments shall be undated or have an original maturity of at least 30 years. Those instruments may include one or more call options at the sole discretion of the issuer, but they shall not be redeemed before five years after the date of issue. If the statutory or contractual provisions governing undated instruments provide for a moderate incentive for the credit institution to redeem as determined by the competent authorities, such incentive shall not occur before ten years after the date of issue.

Dated and undated instruments may be called or redeemed only with the prior consent of the competent authorities. The competent authorities may grant permission provided the request is made at the initiative of the credit institution and either financial or solvency conditions of the credit institution are not unduly affected. The competent authorities may require institutions to replace the instrument by items of the same or better quality referred to in point (ca) of Article 57.

The competent authorities shall require the suspension of the redemption for dated instruments if the credit institution does not comply with the capital requirements set out in Article 75.

The competent authority may grant permission at any time for an early redemption of dated and undated instruments in the event that there is a change in the applicable tax treatment or regulatory classification which was unforeseen at the date of issue."

3. The statutory or contractual provisions governing the instrument shall allow the credit institution to cancel, when necessary, the payment of interest or dividends for an unlimited period of time, on a non-cumulative basis.

However, the credit institution shall cancel such payments if it does not comply with the capital requirements set out in Article 75.

The competent authorities may require the cancellation of such payments based on the financial and solvency situation of the credit institution. Such cancellation shall not prejudice the right of the credit institution to substitute the payment of interest or dividend by a payment in the form of an instrument referred to in point (a) of Article 57, provided that any such mechanism allows the credit institution to preserve financial resources. Such substitution may be subject to specific conditions established by the competent authorities.

4. The statutory or contractual provisions governing the instrument shall provide for principal, unpaid interest or dividend to be such as to absorb losses and to not hinder the recapitalisation of the credit institution.

5. In the event of the bankruptcy or liquidation of the credit institution, the instruments shall rank after the items referred to in Article 63(2).

6. The Committee of European Banking Supervisors shall elaborate guidelines for the convergence of supervisory practices with regard to the instruments referred to in paragraph 1 and shall monitor their application. By January 2012, the Commission shall review the application of this Article and shall report to the Parliament and the Council."

12. In Article 65(1), point (a) is replaced by the following:

"(a) any minority interests within the meaning of Article 21 of Directive 83/349/EEC, where the global integration method is used. Any instruments referred to in point (ca) of Article 57, which give rise to minority interests shall meet the requirements under Articles 63a, 66, and points (a), (c), (d) and (e) of Article 63(2);"

13. Article 66 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. The items referred to in points (d) to (h) of Article 57 shall be subject to the following limits:

(a) the total of the items in points (d) to (h) of Article 57 may not exceed a maximum of 100 % of the items in points (a) to (ca) minus (i), (j) and (k) that Article; and

(b) the total of the items in points (g) to (h) of Article 57 may not exceed a maximum of 50 % of the items in points (a) to (ca) minus (i), (j) and (k) of that Article."

(b) The following paragraph 1a is inserted:

"1a. Notwithstanding paragraph 1, the total of the items in point (ca) of Article 57 shall be subject to the following limits:

(a) instruments that must be converted during emergency situations into items referred to in point (a) of Article 57 within a pre-determined range, and capital that has been paid up, fully absorbs losses in going concern situations, and in the event of bankruptcy or liquidation ranks after all other claims shall in total not exceed a maximum of 50% of the items in points (a) to (ca) minus (i), (j) and (k) of Article 57;

(b) within the limit referred to in point (a) of this paragraph, all other instruments shall not exceed a maximum of 35% of the items in points (a) to (ca) minus (i), (j) and (k) of Article 57;

(c) within the limits referred to in points (a) and (b) of this paragraph, dated instruments and any instrument, whose statutory or contractual provisions provide for an incentive for the credit institution to redeem shall not exceed a maximum of 15% of the items in points (a) to (ca) minus (i), (j) and (k) of Article 57.

(d) the amount of items exceeding the limits set out in points (a), (b) and (c) shall be subject to the limit set out in paragraph 1."

(c) Paragraph 2 is replaced by the following:

"2. The total of the items in points (l) to (r) of Article 57 shall be deducted half from the total of the items (a) to (ca) minus (i), (j) and (k) of that Article, and half from the total of the items (d) to (h) of that Article, after application of the limits laid down in paragraph 1 of this Article. To the extent that half of the total of the items (l) to (r) of Article 57 exceeds the total of the items (d) to (h) of that Article, the excess shall be deducted from the total of the items (a) to (ca) minus (i), (j) and (k) of that Article. Items in point (r) of Article 57 shall not be deducted if they have been included in the calculation of risk-weighted exposure amounts for the purposes of Article 75 as referred to in Annex IX, Part 4."

(d) Paragraph 4 is replaced by the following:

"4. The competent authorities may authorise credit institutions to exceed the limits laid down in paragraphs 1 and 1a temporarily during emergency situations."

14. Article 87 is amended as follows:

(a) Paragraph 11 is replaced by the following:

"11. Where exposures in the form of a collective investment undertaking (CIU) meet the criteria set out in Annex VI, Part 1, points 77 and 78 and the credit institution is aware of all or parts of the underlying exposures of the CIU, the credit institution shall look through to those underlying exposures in order to calculate risk-weighted exposure amounts and expected loss amounts in accordance with the methods set out in this Subsection. Paragraph 12 shall apply to the part of the underlying exposures of the CIU the credit institution is not aware of and could not reasonably be aware of.

Where the credit institution does not meet the conditions for using the methods set out in this Subsection for all or parts of the underlying exposures of the CIU, risk weighted exposure amounts and expected loss amounts shall be calculated in accordance with the following approaches:

(a) for exposures belonging to the exposure class referred to in point (e) of Article 86(1), the approach set out in Annex VII, Part 1, points 19 to 21.

(b) for all other underlying exposures, the approach set out in Articles 78 to 83, subject to the following modifications:

(i) for exposures subject to a specific risk weight for unrated exposures or subject to the highest credit quality step for a given exposure class, the risk weight shall be multiplied by a factor of 2 but cannot be higher than 1250%;

(ii) for all other exposures, the risk weight shall be multiplied by a factor of 1.1 and subject to a minimum of 5%."

If, for the purposes of point (a), the credit institution is unable to differentiate between private equity, exchange-traded and other equity exposures, it shall treat the exposures concerned as other equity exposures. Where these exposures, taken together with the credit institution's direct exposures in this exposure class, are not material within the meaning of Article 89(2), Paragraph 1 of that Article may be applied subject to the approval of the competent authorities."

(b) In paragraph 12, the second subparagraph is replaced by the following:

"Alternatively to the method described in the first subparagraph, credit institutions may calculate themselves or may rely on a third party to calculate and report the average risk weighted exposure amounts based on the CIU's underlying exposures in accordance with the approaches referred to in points (a) and (b) of paragraph 11, provided that the correctness of the calculation and the report is adequately ensured."

15. In Article 89, the introductory phrase of point (d) is replaced by the following:

"(d) exposures to central governments of the Member States and their regional governments, local authorities and administrative bodies provided that"

16. Article 106 is amended as follows:

(a) Paragraph 2 is replaced by the following:

"2. Exposures shall not include any of the following:

(a) in the case of foreign exchange transactions, exposures incurred in the ordinary course of settlement during the 48 hours following payment;

(b) in the case of transactions for the purchase or sale of securities, exposures incurred in the ordinary course of settlement during the five working days following payment or delivery of the securities, whichever is the earlier; or

(c) in the case of the provision of money transmission or securities clearing and settlement services to clients, delayed receipts in funding and other exposures arising from client activity, which do not last longer than the following business day."

(b) Paragraph 3 is added:

"3. In order to determine the existence of a group of connected clients, in respect of exposures referred to in points (m), (o) and (p) of Article 79(1), where there is an exposure to underlying assets, a credit institution shall assess the scheme and its underlying exposures. For that purpose, a credit institution shall evaluate the economic substance and the risks inherent in the structure of the transaction."

17. Article 107 is replaced by the following:

"Article 107

For the purposes of calculating the value of exposures in accordance with this Section, the term 'credit institution' shall also cover any private or public undertaking, including its branches, which meets the definition of 'credit institution' and has been authorised in a third country."

18. Article 110 is replaced by the following:

"Article 110

1. A credit institution shall report the following information about every large exposure to the competent authorities, including large exposures exempted from the application of Article 111(1):

(a) the identification of the client or the group of connected clients to which a credit institution has a large exposure;

(b) the exposure value before taking into account the effect of the credit risk mitigation, to the extent possible;

(c) where used, the type of funded or unfunded credit protection;

(d) the exposure value after taking into account the effect of the credit risk mitigation calculated for the purpose of Article 111(1).

If a credit institution is subject to Articles 84 to 89, its 20 largest exposures on a consolidated basis, excluding those exempted from the application of Article 111(1), shall be made available to the competent authorities.

2. Member States shall provide that reporting is to be carried out at least twice a year.

3. Member States shall require credit institutions to analyse, to the extent possible, their exposures to collateral issuers and providers of unfunded credit protection for possible concentrations and where appropriate take action and report any significant findings to their competent authority."

19. Article 111 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. A credit institution may not incur an exposure, after taking into account the effect of the credit risk mitigation in accordance with Articles 112 to 117, to a client or group of connected clients the value of which exceeds 25% of its own funds.

Where that client is an institution or where a group of connected clients includes one or more institutions, this value may not exceed 25% of the credit institution's own funds or the amount of EUR 150 million, whichever is higher, provided that the sum of exposure values, after taking into account the effect of the credit risk mitigation in accordance with Articles 112 to 117, to all connected clients that are not institutions does not exceed 25% of the credit institution's own funds.

Member States may set a lower limit than EUR 150 million and shall inform the Commission."

(b) Paragraphs 2 and 3 are deleted.

(c) Paragraph 4 is replaced by the following:

"4. A credit institution shall at all times comply with the limit laid down in paragraph 1. If in an exceptional case exposures exceed this limit, the value of the exposure shall be reported without delay to the competent authorities which may, where the circumstances warrant it, allow the credit institution a limited period of time in which to comply with the limit."

20. Article 112 is amended as follows:

(a) Paragraph 2 is replaced by the following:

"2. Subject to paragraph 3, where, under Articles 113 to 117, the recognition of funded or unfunded credit protection is permitted, this shall be subject to compliance with the eligibility requirements and other minimum requirements, set out in Articles 90 to 93."

(b) The following paragraph 4 is added:

"4. For the purpose of this Section, a credit institution shall not take into account the collateral referred to in Annex VIII, Part 1, points 20 to 22, unless permitted under Article 115."

21. Article 113 is amended as follows:

(a) Paragraphs 1 and 2 are deleted.

(b) Paragraph 3 is amended as follows:

(i) The introductory phrase is replaced by the following:

"3. The following exposures shall be exempted from the application of Article 111(1):"

(ii) Points (e) and (f) are replaced by the following:

"(e) asset items constituting claims on regional governments and local authorities of Member States where those claims would be assigned a 0 % risk weight under Articles 78 to 83 and other exposures to or guaranteed by such governments and authorities claims on which would be assigned a 0 % risk weight under Articles 78 to 83.

(f) exposures to counterparties referred to in paragraph 7 or paragraph 8 of Article 80 if they would be assigned a 0% risk weight under Articles 78 to 83; exposures that do not meet these criteria, whether exempted from Article 111(1) or not, shall be treated as exposures to a third party."

(iii) Point (i) is replaced by the following:

"(i) exposures arising from undrawn credit facilities that are classified as low risk off-balance sheet items in Annex II and provided that an agreement has been concluded with the client or group of connected clients under which the facility may be drawn only if it has been ascertained that it will not cause the limit applicable under Article 111(1) to be exceeded."

(iv) Points (j) to (t) are deleted.

(c) The third, fourth and fifth subparagraphs are deleted.

(d) The following paragraph 4 is added:

"4. Member States may fully or partially exempt the following exposures from the application of Article 111(1):

(a) covered bonds falling within the terms of Annex VI, Part 1, points 68, 69 and 70;

(b) asset items constituting claims on regional governments and local authorities of Member States where those claims would be assigned a 20% risk weight under Articles 78 to 83 and other exposures to or guaranteed by such governments and authorities claims on which would be assigned a 20% risk weight under Articles 78 to 83;

(c) notwithstanding point (f) of paragraph 1 of this Article, exposures incurred by a credit institution to its parent undertaking, to other subsidiaries of that parent undertaking or to its own subsidiaries, in so far as those undertakings are covered by the supervision on a consolidated basis to which the credit institution itself is subject, in accordance with this Directive or with equivalent standards in force in a third country; exposures that do not meet these criteria, where exempted from Article 111(1) or not, shall be treated as exposures to a third party;

(d) asset items constituting exposures to or participations or other kind of holdings in regional or central credit institutions with which the lending credit institution is associated in a network in accordance with legal or statutory provisions and which are responsible, under those provisions, for cash-clearing operations within the network;

(e) asset items constituting claims on and other exposures to credit institutions incurred by credit institutions operating on a non-competitive basis providing loans under legislative programmes or their statutes to promote specified sectors of the economy under some form of government oversight and restrictions on the use of the loans provided that the respective exposures arise from such loans that are passed on to the beneficiaries via other credit institutions.

(f) asset items constituting claims on and other exposures to institutions, provided that these exposures do not constitute such institutions' own funds, do not last longer than the following business day and are denominated in a currency of the Member State exercising this option, provided that such currency is not the euro."

22. Article 114 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. Subject to paragraph 3, for the purposes of calculating the value of exposures for the purposes of Article 111(1) a credit institution may use the 'fully adjusted exposure value' as calculated under Articles 90 to 93, taking into account the credit risk mitigation, volatility adjustments, and any maturity mismatch (E*)."

(b) Paragraph 2 is amended as follows:

(i) The first subparagraph is replaced by the following:

"Subject to paragraph 3, a credit institution permitted to use own estimates of LGDs and conversion factors for an exposure class under Articles 84 to 89 shall be permitted, where it is able to the satisfaction of the competent authorities to estimate the effects of financial collateral on their exposures separately from other LGD-relevant aspects, to recognise such effects in calculating the value of exposures for the purposes of Article 111(1)."

(ii) The fourth subparagraph is replaced by the following:

"Credit institutions permitted to use own estimates of LGDs and conversion factors for an exposure class under Articles 84 to 89 which do not calculate the value of their exposures using the method referred to in the first subparagraph may use the Financial Collateral Comprehensive Method or the approach set out in Article 117(1)(b) for calculating the value of exposures."

(c) Paragraph 3 is amended as follows:

(i) The first subparagraph is replaced by the following:

"A credit institution that makes use of the Financial Collateral Comprehensive Method or is permitted to use the method described in paragraph 2 in calculating the value of exposures for the purposes of Article 111(1), shall conduct periodic stress tests of their credit-risk concentrations, including in relation to the realisable value of any collateral taken."

(ii) The fourth subparagraph is replaced by the following:

"In the event that such a stress test indicates a lower realisable value of collateral taken than would be permitted to be taken into account while making use of the Financial Collateral Comprehensive Method or the method described in paragraph 2 as appropriate, the value of collateral permitted to be recognised in calculating the value of exposures for the purposes of Article 111(1) shall be reduced accordingly."

(iii) In the fifth subparagraph, point (b) is replaced by the following:

"(b) policies and procedures in the event that a stress test indicates a lower realisable value of collateral than taken into account while making use of the Financial Collateral Comprehensive Method or the method described in paragraph 2; and"

(d) Paragraph 4 is deleted.

23. Article 115 is replaced by the following:

"*Article 115*

1. For the purpose of this Section, a credit institution may reduce the exposure value by up to 50% of the value of the residential property concerned, if either of the following conditions is met:

(a) the exposure is secured, by mortgages on residential property or by shares in Finnish residential housing companies, operating in accordance with the Finnish Housing Company Act of 1991 or subsequent equivalent legislation;

(b) the exposure relates to a leasing transaction under which the lessor retains full ownership of the residential property leased for as long as the lessee has not exercised his option to purchase.

The value of the property shall be calculated, to the satisfaction of the competent authorities, on the basis of strict valuation standards laid down by law, regulation or administrative provisions. Valuation shall be carried out at least once a year.

Residential property shall mean a residence to be occupied or let by the owner.

2. For the purpose of this Section, a credit institution may reduce the exposure value by up to 50% of the value of the commercial property concerned, only if the following exposures would receive a 50% risk weight under Articles 78 to 83:

(a) exposures secured by mortgages on offices or other commercial premises, or by shares in Finnish housing companies, operating in accordance with the Finnish Housing Company Act of 1991 or subsequent equivalent legislation, in respect of offices or other commercial premises; or

(b) exposures related to property leasing transactions concerning offices or other commercial premises.

Commercial property shall be fully constructed, fully leased and produce appropriate rental income."

24. Article 116 is deleted.

25. Article 117 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. Where an exposure to a client is guaranteed by a third party, or secured by collateral issued by a third party, a credit institution may:

(a) treat the portion of the exposure which is guaranteed as having been incurred to the guarantor rather than to the client provided that the unsecured exposure to the guarantor would be assigned an equal or lower risk weight than a risk weight of the unsecured exposure to the client under Articles 78 to 83;

(b) treat the portion of the exposure collateralised by the market value of recognised collateral as having been incurred to the third party rather than to the client, if the exposure is secured by collateral and provided that the collateralised portion of the exposure would be assigned an equal or lower risk weight than a risk weight of the unsecured exposure to the client under Articles 78 to 83.

The approach referred to in point (b) shall not be used by a credit institution where there is a mismatch between the maturity of the exposure and the maturity of the protection.

For the purpose of this Section, a credit institution may use both the Financial Collateral Comprehensive Method and the treatment provided for in point (b) of the first subparagraph only where it is permitted to use both the Financial Collateral Comprehensive Method and the Financial Collateral Simple Method for the purposes of Article 75(a)."

(b) In paragraph 2, the introductory phrase is replaced by the following:

"Where a credit institution applies point (a) of paragraph 1:"

26. Article 119 is deleted.

27. The following Section 7 is added to Chapter 2:

"Section 7

Exposures to transferred credit risk

Article 122a

1. A credit institution shall only be exposed to the credit risk of an obligation or potential obligation or a pool of obligations or potential obligations where it was not involved in directly negotiating, structuring and documenting the original agreement which created the obligations or potential obligations, if:

(a) the persons or entities that directly negotiated, structured and documented the original agreement with the obligor or potential obligor; or alternatively and where applicable,

(b) the persons or entities that manage and purchase such obligations or potential obligations directly or indirectly on behalf of the credit institution,

have issued an explicit commitment to the credit institution to maintain, on an ongoing basis, a material net economic interest and in any event not less than 5 per cent in positions having the same risk profile as the one that the credit institution is exposed to.

2. Paragraph 1 shall not apply to obligations or potential obligations that constitute claims or contingent claims on or guaranteed by:

(a) central governments or central banks;

(b) institutions to which a credit quality step of 3 or better applies according to Annex VI, Part 1, point 29; and

(c) multilateral development banks.

Paragraph 1 shall not apply either to syndicated loans or credit default swaps where these instruments are not used to package and/or hedge an obligation that is covered by paragraph 1

3. Paragraphs 1 and 2 shall apply to exposures incurred by the credit institution after 1 January 2011. Competent authorities may decide to temporarily suspend the requirements during periods of general market liquidity stress.

4. Before investing and on an ongoing basis, credit institutions shall be able to demonstrate at all times to the competent authorities for each of their individual securitisation positions that they have a comprehensive and thorough understanding of and have implemented formal policies and procedures for analysing and recording, in writing:

(a) the commitment, under paragraph 1, of originators and/or sponsors to maintain a net economic interest in the securitisation and the period for which such commitment is given;

(b) the risk characteristics of the individual securitisation position;

(c) the risk characteristics of the exposures underlying the securitisation position;

(d) the reputation and loss experience in earlier securitisations of the originators in the relevant exposure classes underlying the securitization position;

(e) the statements made by the originators and sponsors about the due diligence undertaken by them on the obligors and, where applicable, on the collateral quality of the exposures underlying the securitization position;

(f) where applicable, the methodologies and concepts on which the valuation of collateral supporting the exposures underlying the securitization position is based and the policies adopted by the originators to ensure the independence of the valuer; and

(g) all the structural features of the securitisation that can materially impact the performance of the credit institution's securitisation position. To this end, credit institutions shall prior to investing and regularly thereafter perform and record appropriate stress tests, such stress tests to be conducted independently of the ECAI or ECAIs who have rated the securitisation and to be based on all relevant information provided by the originator for this purpose.

5. Credit institutions shall establish formal procedures to monitor on an ongoing basis and in a timely manner performance information on the exposures underlying their securitisation positions. Where relevant, this shall include, at a minimum: the exposure type, the length of time the exposures have been held by the originator including the percentage held by the originator for less than 2 years, the percentage of loans more than 30, 60 and 90 days past due, default rates, prepayment rates, loans

in foreclosure, collateral type and occupancy, frequency distribution of credit scores or other measures of credit worthiness across underlying exposures, industry and geographical diversification, frequency distribution of loan to value ratios with band widths that facilitate adequate sensitivity analysis. Where the underlying exposures are themselves securitisation positions, the requirements to monitor and be able to access information shall apply to the exposures underlying these securitisation positions. Where the requirements in paragraph 4and in this paragraph are not met, credit institutions shall apply a risk weight of 1250% to these securitisation positions under Annex IX, part 4.

6. Sponsor and originator credit institutions shall apply the same sound and well-defined criteria for credit-granting in accordance with the requirements of Annex V, point 3 to exposures to be securitised as they apply to exposures to be held on their own non-trading book. To this end the same processes for approving and, where relevant, amending, renewing and re-financing credits shall be applied by the originator and sponsor credit institutions. Credit institutions shall also apply the same standards of analysis to participations and/or underwritings in securitization issues purchased from third parties whether such participations and/or underwritings are to be held on their trading or non-trading book.

7. Sponsor and originator credit institutions shall disclose to investors the level of their commitment under paragraph 1 to maintain a net economic interest in the securitisation. Sponsor and originator credit institutions shall ensure that prospective investors have readily available access to all materially relevant data on the credit quality and performance of the individual underlying exposures, cash flows and collateral supporting a securitization exposure as well as such information that is necessary to conduct comprehensive and well informed stress tests on the cash flows and collateral values supporting the underlying exposures. Where these requirements and those in paragraph 6 are not met, Article 95 (1) shall not be applied by an originator credit institution which will not be allowed to exclude the securitised exposures from the calculation of its capital requirements under this Directive.

8. Paragraphs 4 to 7 shall apply to securitisations issued from the date that this Directive comes into effect and to existing securitisations where new underlying exposures are added or substituted after that date.

9. Competent authorities shall disclose publicly at least annually:

(a) the methodologies adopted to review the compliance with paragraphs 1 to 7;

(b) a description and the number of the measures undertaken to review the compliance with paragraphs 1 to 7 during the past 12 months; and

(c) the number and a summary description of the cases of non-compliance with paragraphs 1 to 7 identified during the past 12 months.

This requirement is subject to the second subparagraph of Article 144.

10. The Committee of European Banking Supervisors will report annually to the Commission about the compliance by competent authorities with this Article. The Commission shall, no later than December 2014, report to the European Parliament

and the Council on the application and effectiveness of this Article in the light of market developments."

28. Article 129 is amended as follows:

(a) Paragraph 1 is amended as follows:

(i) Point (b) is replaced by the following:

"(b) planning and coordination of supervisory activities in going concern situations, including in relation to the activities referred to in Articles 123, 124, 136, in Chapter 5 and in Annex V, in cooperation with the competent authorities involved;

(ii) The following point (c) is added:

(c) planning and coordination of supervisory activities in cooperation with the competent authorities involved, and if necessary with central banks, in preparation of and during emergency situations, including adverse developments in credit institutions or in financial markets.

The planning and coordination of supervisory activities referred to in point (c) includes exceptional measures referred to in Article 132(3)(b), the preparation of joint assessments, the implementation of contingency plans and communication to the public."

(b) The following paragraph 3 is added:

"3. The consolidating supervisor and the competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company in a Member State shall do everything within their power to reach a joint decision:

(a) on the application of Articles 123 and 124 to determine the adequacy of the consolidated level of own funds held by the group with respect to its financial situation and risk profile and consequently, the required level of own funds for the application of Articles 136(2) to each entity within the banking group and on a consolidated basis;

(b) on uniform formats, frequencies and dates of reporting for the application of Article 74(2) to all entities within the banking group.

For the purposes of point (a), the joint decision shall be reached six months after submission by the consolidating supervisor of a report containing the risk assessment of the group in accordance with Articles 124 and 123 to the other relevant competent authorities.

For the purposes of point (b), the joint decision shall be reached by 30 June 2011.

The joint decision referred to in the first subparagraph shall be set out in a document containing the fully reasoned decision which shall be provided to the EU parent credit institution by the consolidating supervisor. In case of disagreement, the consolidating supervisor shall at the request of any of the other competent authorities concerned consult the Committee of European Banking Supervisors. The consolidating supervisor may consult the Committee of European Banking Supervisors on its own initiative.

In the absence of such a joint decision between the competent authorities within six months, the consolidating supervisor shall make its own decision on the application of Articles 74(2), 123, 124 and 136(2). The decision shall be set out in a document containing the fully reasoned decision and shall take into account the views and reservations of the other competent authorities expressed during the six months period. The decision shall be provided to the other competent authorities by the consolidating supervisor.

Where the Committee of European Banking Supervisors has been consulted, the consolidating supervisor shall consider such advice, and explain any significant deviation there from.

The joint decision referred to in the first subparagraph and the decision referred to in the sixth subparagraph shall be recognised as determinative and applied by the competent authorities in the Member State concerned."

29. Article 130 paragraph 1 is replaced by the following:

"1. Where an emergency situation, including adverse developments in financial markets, arises, which potentially jeopardises the stability of the financial system in any of the Member States where entities of a group have been authorised or where systemically relevant branches as referred to in Article 42a are established, the consolidating supervisor shall, subject to Chapter 1, Section 2**,** alert as soon as is practicable, the authorities referred to in the fourth subparagraph of Article 49 and in Article 50, and shall communicate all information that is essential for the pursuance of their tasks. These obligations shall apply to all competent authorities under Articles 125 and 126 and to the competent authority identified under Article 129(1).

If the authority referred to in the fourth subparagraph of Article 49 becomes aware of a situation described in the first subparagraph of this paragraph, it shall alert as soon as is practicable the competent authorities referred to in Articles 125 and 126.

Where possible, the competent authority and the authority referred to in the fourth subparagraph of Article 49 shall use existing defined channels of communication."

30. The following Article 131a is inserted:

"Article 131a

1. The consolidating supervisor shall establish colleges of supervisors to facilitate the exercise of the tasks referred to in Articles 129 and 130(1).

Colleges of supervisors shall provide a framework for the consolidating supervisor and the other competent authorities concerned to carry out the following tasks:

(a) exchange information;

(b) agree on voluntary entrustment of tasks and delegation of responsibilities;

(c) determine supervisory examination programmes based on a risk assessment of the group in accordance with Article 124;

(d) increase the efficiency of supervision by removing unnecessary duplication of supervisory requirements, including in relation to the information requests referred to in Articles 130(2) and 132(2);

(e) consistently apply the prudential requirements under this Directive across all entities within a banking group.

(f) apply 129(1)(c) taking into account the work of other forums that may be established in this area.

The competent authorities participating in the college of supervisors shall cooperate closely. The confidentiality requirements under Chapter 1, Section 2 shall not prevent competent authorities from exchanging confidential information within colleges of supervisors. The establishment of colleges of supervisors shall not affect the rights and responsibilities of the competent authorities under this Directive.

2. The establishment and functioning of the college shall be based on written arrangements referred to in Article 131, determined after consultation with competent authorities concerned by the consolidating supervisor.

The Committee of European Banking Supervisors shall elaborate guidelines for the operational functioning of colleges.

The competent authorities responsible for the supervision of subsidiaries of an EU parent credit institution or an EU parent financial holding company and the competent authorities of a host country where systemically relevant branches as referred to in Article 42a are established, and authorities of third countries where appropriate, may participate in colleges of supervisors.

The consolidating supervisor shall chair the meetings of the college and shall decide which competent authorities participate in a meeting or in an activity of the college. The consolidating supervisor shall keep all members of the college fully informed of the organisation of such meetings and activities and decisions taken in those meetings.

The decision of the consolidating supervisor shall take account of the relevance of the supervisory activity to be planned or coordinated for those authorities, and the obligations referred to in Articles 40(3) and 42a(2).

The consolidating supervisor, subject to the confidentiality requirements under Chapter 1, Section 2, shall inform the Committee of European Banking Supervisors of the activities of the college of supervisors, including in emergency situations, and communicate to that Committee all information that is of particular relevance for the purposes of supervisory convergence."

31. Article 132 is amended as follows:

(a) In point (d) of paragraph 1 the reference to Article 136 is replaced by the reference to Article 136(1).

(b) In point (b) of paragraph 3 the reference to Article 136 is replaced by the reference to Article 136(1).

32. Article 150 is amended as follows:

(a) Paragraph 1 is amended as follows:

(ii) Points (k) and (l) are replaced by the following:

"(k) the list and classification of off-balance sheet items in Annexes II and IV;

(l) adjustment of the provisions in Annexes III and V to XII in order to take account of developments on financial markets (in particular new financial products) or in accounting standards or requirements which take account of Community legislation, or with regard to convergence of supervisory practice; or"

(ii) the following point (m) is added:

"(m) alteration of the amount and the percentage specified in Article 111(1) to take account of developments on financial markets."

(b) In paragraph 2, point (c) is replaced by the following:

"(c) clarifications of exemptions provided for in Article 113;"

33. In Article 154, the following paragraphs 8 and 9 are added:

"8. Credit institutions which do not comply by [*the date referred to in Article 4 - to be inserted if known*] with the limits set out in Article 66(1a) shall develop strategies and processes under Article 123 on the necessary measures to resolve this situation before the dates set out in paragraph 9.

Thse measures shall be reviewed under Article 124.

9. Instruments that by [*the date referred to in Article 4 - to be inserted if known.*] , according to national law were deemed equivalent to the items referred to in points (a), (b) and (c) of Article 57 but do not fall within point (a) of Article 57 or do not comply with the criteria set out in Article 63a, shall continue tobe deemed equivalent until [*30 years after the date referred to in Article 4 - to be inserted if known*] , for an amount up to:

(a) 20% of the sum of points (a) to (ca) of Article 57, less the sum of points (i), (j) and (k) of Article 57 [*between 10 and 20 years after the date referred to in Article 4 - to be inserted if known*];

(b) 10% of the sum of points (a) to (ca) of Article 57, less the sum of points (i), (j) and (k) of Article 57 [*between 20 and 30 years after the date referred to in Article 4 - to be inserted if known*];

34. Annex III is amended as follows:

(a) In part 1, point 5, the following text is added:

"Under the method set out in Part 6 of this Annex (IMM), all netting sets with a single counterparty may be treated as single netting set if negative simulated market values of the individual netting sets are set to 0 in the estimation of expected exposure (EE)."

(b) In part 2, point 3 is replaced by the following:

"3. When a credit institution purchases credit derivative protection against a non-trading book exposure, or against a CCR exposure, it may compute its capital requirement for the hedged asset in accordance with Annex VIII, Part 3, points 83 to 92, or subject to the approval of the competent authorities, in accordance with Annex VII, Part 1, point 4 or Annex VII, Part 4, points 96 to 104.

In these cases, and where the option in the second sentence of point 11 in Annex II of Directive 2006/49/EC is not applied, the exposure value for CCR for these credit derivatives is set to zero.

However, an institution may choose to consistently include for the purposes of calculating capital requirements for counterparty credit risk all credit derivatives not included in the trading book and purchased as protection against a non-trading book exposure or against a CCR exposure where the credit protection is recognised under this Directive."

(c) In part 5, point 15 is replaced by the following:

"15. There is one hedging set for each issuer of a reference debt instrument that underlies a credit default swap. 'Nth to default' basket credit default swaps shall be treated as follows:

(a) the size of a risk position in a reference debt instrument in a basket underlying an 'nth to default' credit default swap is the effective notional value of the reference debt instrument, multiplied by the modified duration of the 'nth to default' derivative with respect to a change in the credit spread of the reference debt instrument;

(b) there is one hedging set for each reference debt instrument in a basket underlying a given 'nth to default' credit default swap; risk positions from different 'nth to default' credit default swaps shall not be included in the same hedging set;

(c) the CCR multiplier applicable to each hedging set created for one of the reference debt instruments of an 'nth to default' derivative is 0.3% for reference debt instruments that have a credit assessment from a recognised ECAI equivalent to credit quality step 1 to 3 and 0.6% for other debt instruments."

35. Annex V is amended as follows:

(a) Point 14 is replaced by the following:

"14. Robust strategies, policies, processes and systems shall exist for the identification, measurement and management of liquidity risk over an appropriate set of time horizons, including intra-day, so as to ensure that credit institutions maintain adequate levels of liquidity buffers. These strategies, policies, processes and systems shall be tailored to business lines, currencies and legal entities and shall include adequate liquidity cost allocation mechanisms."

(e) The following point 14a is inserted:

"14a. The strategies, policies, processes and systems referred to in point 14 shall be proportionate to the complexity, risk profile, scope of operation of the firm and risk tolerance set by the management body and reflect the credit institution's systemic relevance in each Member State, in which it carries on business."

(f) Point 15 is replaced by the following:

"15. Credit institutions shall develop methodologies for the identification, measurement, management and monitoring of funding positions, in particular through a system of limits. These shall include cash-flows arising from assets, liabilities, off-balance-sheet items, including contingent liabilities and the possible impact of reputational risk."

(g) The following points 16 to 22 are added:

"16. Credit institutions shall distinguish between pledged and unencumbered assets that are available at all times, in particular during emergency situations. They shall also take into account the legal entity in which assets reside, as well as their eligibility and timely mobilisation.

17. Credit institutions shall also have regard to existing legal, regulatory and operational limitations to potential transfers of liquidity and unencumbered assets amongst legal entities, both within and outside the EEA.

18. A credit institution shall consider different liquidity risk mitigation tools, including liquidity buffers in order to be able to withstand a range of different stress events and an adequately diversified funding structure and access to funding sources. These arrangements shall be reviewed regularly.

19. Alternative scenarios on liquidity positions and on risk mitigants shall be considered and the assumptions underlying decisions concerning the funding position shall be reviewed regularly. For these purposes, alternative scenarios shall address, in particular, off-balance sheet items and other contingent liabilities, including those of SSPEs or other special purpose entities, in relation to which the credit institution acts as sponsor or provides material liquidity support.

20. Credit institutions shall consider the potential impact of institution-specific, market-wide and combined alternative scenarios. Different time horizons and varying degrees of stressed conditions shall be considered.

21. Credit institutions shall adjust their strategies, internal policies and limits on liquidity risk and develop effective contingency plans, taking into account the outcome of the alternative scenarios referred to in point 19.

22. In order to deal with liquidity crises, credit institutions shall have in place contingency plans setting out adequate strategies and proper implementation measures in order to address possible liquidity shortfalls. These plans shall be regularly tested, updated on the basis of the outcome of the alternative scenarios set out in point 16, be reported to and approved by senior management, so that internal policies and processes can be adjusted accordingly."

36. Annex XI is amended as follows:

(a) Point 1(e) is replaced by the following:

"(e) the exposure to, measurement and management of liquidity risk by the credit institutions, including the development of alternative scenario analyses, the management of risk mitigants (in particular the level, composition and quality of liquidity buffers) and effective contingency plans;

(b) The following point 1a is inserted:

"1a. For the purposes of point 1(e), the competent authorities shall regularly carry out a comprehensive assessment of the overall liquidity risk management by credit institutions and promote the development of sound internal methodologies. While conducting these reviews, the competent authorities shall have regard to the role played by credit institutions in the financial markets. The competent authorities in one Member State shall also have regard to the potential impact of their decisions on the stability of the financial system in all other Member States concerned."

37. Annex XII, part 2, points 3 (a) and (b) are replaced by the following:

"(a) summary information on the terms and conditions of the main features of all own funds items and components thereof, including instruments referred to in point (ca) of Article 57, instruments the statutory or contractual provisions of which provide an incentive for the credit institution to redeem them, and instruments subject to Article 154(9);

(b) the amount of the original own funds, with separate disclosure of all positive items and deductions; the overall amount of instruments referred to in point (ca) of Article 57 and instruments the statutory or contractual provisions of which provide an incentive for the credit institution to redeem them, shall also be disclosed separately; those disclosures shall each specify instruments subject to Article 154(9);"

Article 2

Amendments to Directive 2006/49/EC

Directive 2006/49/EC is amended as follows:

(1) In Article 12, the first subparagraph is replaced by the following:

"'Original own funds' means the sum of points (a) to (ca), less the sum of points (i), (j) and (k) of Article 57 of Directive 2006/48/EC.

(2) Article 28 is amended as follows:

(a) Paragraph 1 is replaced by the following:

"1. Institutions, except investment firms that fulfil the criteria set out in paragraph (2) or (3) of Article 20 of this Directive, shall monitor and control their large exposures in accordance with Articles 106 to 118 of Directive 2006/48/EC."

(b) Paragraph 3 is deleted.

(3) Article 30(4) is deleted.

(4) Article 31 is amended as follows:

(a) In the first paragraph, points (a) and (b) are replaced by the following:

"(a) the exposure on the non-trading book to the client or group of clients in question does not exceed the limit laid down in Article 111(1) of Directive 2006/48/EC, this limit being calculated with reference to own funds as specified in that Directive, so that the excess arises entirely on the trading book;

(b) the institution meets an additional capital requirement on the excess in respect of the limit laid down in Article 111(1) of Directive 2006/48/EC, that additional capital requirement being calculated in accordance with Annex VI to this Directive;"

(b) In the first paragraph, point (e) is replaced by the following:

"(e) institutions shall report to the competent authorities every three months all cases where the limit laid down in Article 111(1) of Directive 2006/48/EC has been exceeded during the preceding three months."

(c) The second paragraph is replaced by the following:

"In relation to point (e), in each case in which the limit has been exceeded, the amount of the excess and the name of the client concerned shall be reported."

(5) In Article 32(1), the first subparagraph is replaced by the following:

"1. The competent authorities shall establish procedures to prevent institutions from deliberately avoiding the additional capital requirements that they would otherwise incur, on exposures exceeding the limit laid down in Article 111(1) of Directive 2006/48/EC once those exposures have been maintained for more than 10 days, by means of temporarily transferring the exposures in question to another company, whether within the same group or not, and/or by undertaking artificial transactions to close out the exposure during the 10-day period and create a new exposure."

(6) In Article 38, the following paragraph is added:

"3. Article 42a, with the exception of point (a) of Directive 2006/48/EC shall apply *mutatis mutandis* to the supervision of investment firms unless the investment firms fulfil the criteria set out in Article 20(2), 20(3) or 46(1) of this Directive.

(7) In Article 45(1) the date "31 December 2010" is replaced by "31 December 2012".

(8) In Article 48(1) the date "31 December 2010" is replaced by "31 December 2012".

Article 3

Transposition

1. Member States shall bring into force the laws, regulations and administrative provisions necessary to comply with this Directive by 31 January 2010 at the latest. They shall forthwith communicate to the Commission the text of those provisions and a correlation table between those provisions and this Directive.

They shall apply those provisions from 31 March 2010.

When Member States adopt those provisions, they shall contain a reference to this Directive or be accompanied by such a reference on the occasion of their official publication. Member States shall determine how such reference is to be made.

2. Member States shall communicate to the Commission the text of the main provisions of national law which they adopt in the field covered by this Directive.

Article 4

Entry into force

This Directive shall enter into force on the twentieth day following that of its publication in the *Official Journal of the European Union*.

Article 5

Addressees

This Directive is addressed to the Member States.

Done at Brussels,

For the European Parliament	*For the Council*
The President	*The President*