EUROPEAN COMMISSION

Brussels, 10 07 2012
C(2012) 4734 *final*

Dear President, Dear Mr. Cash,

The Commission would like to thank the House of Commons for its reasoned Opinion concerning the draft regulation on prudential requirements for credit institutions and investment firms {COM(2011) 452 final} and would like to apologise for the long delay in replying.

The Commission notes that the House of Commons has concluded that the proposal for a Regulation does not respect the principle of subsidiarity. The reasoned opinion focuses on two aspects: procedural obligations under the Treaty on the Functioning of the European Union (TFEU); and the principle of subsidiarity under that Treaty. I will address both issues in this reply.

With regard to the level of explanation and qualitative and quantitative analyses contained in the explanatory memorandum and impact assessment in respect of the abovementioned proposal, I would like to draw your attention in particular to sections 3.6, 5.6, 5.7, and 5.8.3 of the impact assessment in which a number of options in relation to the creation of a single rulebook and the choice of legal instrument are analysed and their impacts assessed. Through this analysis and the extensive consultation and data gathering that preceded it, the Commission considers that it has discharged its procedural obligations and has acted in full compliance with its own principles of better regulation.

Moreover, the ongoing financial crisis has confirmed the Commission's view that prudential supervision is central to the effective functioning of the single market. Rather than reducing financial instability in the EU, the current national application of different prudential rules has served to contribute to it, by adding to uncertainty about the overall adequacy of the solvency and funding situation of financial institutions in the EU.

To remedy this, a clear and uniform set of appropriately robust prudential standards for all credit institutions in the EU is required. This can only be achieved through action at EU level and as such the Commission considers that the proposal is fully in line with the principle of subsidiarity. A maximum harmonisation approach based on a single rule book is also the most effective means of creating a genuine single market in financial services based on uniformly high standards of prudential regulation. This was confirmed by the European Council in June 2009.

Mr William Cash MP
Chairman
European Scrutiny Committee
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Of course, the case for harmonisation must be appropriately balanced against the need for flexibility to react to different national circumstances. We believe that the proposal strikes such a balance. Within the overall context of maximum harmonisation, the Commission proposal, currently discussed by co-legislators, introduces four principal elements of flexibility:

- *the ability to use the countercyclical buffer to address variables other than those relating to credit growth that the competent authority considers to be relevant, including structural variables - Article 126(3)(c), proposal for a Directive*

- *a Pillar 2 approach under which additional capital requirements may be applied to a certain type of institution, rather than only to individual institutions - Article 95, proposal for a Directive;*

- *the ability to adjust the risk weights applied to lending secured by immovable property - Article 119(2) proposal for a Regulation;*

- *the possibility to accelerate the implementation of the new, harmonised rules in respect of the quantity and quality of capital during the transition period – Title I of Part Ten of the proposal for a Regulation.*

The first three elements equip Member States to respond at national level to developments in micro-prudential and macro-prudential risk; the final element ensures they can build upon progress already made to raise prudential standards.

In addition, Article 443 of the proposal for a Regulation empowers the Commission under specific conditions to introduce stricter prudential requirements on a temporary basis across the EU, or in a particular Member State region or sector. The Article includes an explicit link between the recommendations or opinions of the parties responsible for monitoring and managing financial stability in the EU and the use of delegated acts by the Commission. This will help to ensure the efficient and effective use of such powers.

As you may be aware, the question of national flexibility is in the focus of the ongoing interinstitutional negotiations. The Commission is participating actively in these discussions.

I hope that these explanations serve to clarify the points raised in your reasoned Opinion. The Commission looks forward to continuing the political dialogue with the House of Commons.

Yours faithfully,

Maroš Šefčovič
Vice-President