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Commission Delegated Regulation (EU) 2017/390 of 11 November 2016 supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on certain prudential requirements for central securities depositories and designated credit institutions offering banking-type ancillary services (Text with EEA relevance)

COMMISSION DELEGATED REGULATION (EU) 2017/390

of 11 November 2016

supplementing Regulation (EU) No 909/2014 of the European Parliament and of the Council with regard to regulatory technical standards on certain prudential requirements for central securities depositories and designated credit institutions offering banking-type ancillary services

(Text with EEA relevance)

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 909/2014 of the European Parliament and of the Council of 23 July 2014 on improving securities settlement in the European Union and on central securities depositories and amending Directives 98/26/EC and 2014/65/EU and Regulation (EU) No 236/2012[(1)], and in particular the third subparagraph of Article 47(3), the third subparagraph of Article 54(8) and the third subparagraph of Article 59(5) thereof,

Whereas:

(1) Regulation (EU) No 909/2014 establishes prudential requirements for central securities depositories (CSDs) to ensure that they are safe and sound and comply at all times with capital requirements. Such capital requirements ensure that a CSD is at all times adequately capitalised against the risks to which it is exposed and that it is able to conduct an orderly winding-down or restructuring of its activities if necessary.

(2) Given that the provisions of Regulation (EU) No 909/2014 concerning credit and liquidity risks relating to CSDs and designated credit institutions explicitly require that their internal rules and procedures allow them to monitor, measure and manage exposures and liquidity needs not only with respect to the individual participants but also with respect to participants that belong to the same group and who are counterparties of the CSD, such provisions should apply to groups of undertakings consisting of a parent undertaking and its subsidiaries.

(3) For the purposes of this Regulation, the relevant recommendations of the Principles for Financial Market Infrastructures issued by the Committee on Payment and Settlement Systems and the International Organization of Securities Commissions ('CPSS-IOSCO Principles')[(2)] have been taken into account. The treatment of capital of credit institutions under Regulation (EU) No 575/2013 of the European Parliament and of

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the Council[3] has also been taken into account given that CSDs are to a certain extent exposed to risks that are similar to the risks incurred by credit institutions.

(4) It is appropriate for the definition of capital in this Regulation to mirror the definition of capital laid down in Regulation (EU) No 648/2012 of the European Parliament and of the Council[4] (EMIR). Such a definition is the most suitable in relation to the regulatory requirements given that the definition of capital in Regulation (EU) No 648/2012 was specifically designed for market infrastructures. CSDs authorised to provide banking-type ancillary services under Regulation (EU) No 909/2014 are required to meet capital requirements under this Regulation and own funds requirements under Regulation (EU) No 575/2013 simultaneously. They are required to meet the own funds requirements laid down in Regulation (EU) No 575/2013 with instruments that meet the conditions of that Regulation. In order to avoid conflicting or duplicative requirements and considering that the methodologies used for the calculation of the additional capital surcharge for CSDs under Regulation (EU) No 909/2014 are closely related to the ones provided in Regulation (EU) No 575/2013, CSDs offering banking-type ancillary services should be allowed to meet the additional capital requirements of this Regulation with the same instruments meeting the requirements laid down in either Regulation (EU) No 575/2013 or Regulation (EU) No 909/2014.

(5) In order to ensure that, if required, a CSD would be able to organise the restructuring of its activities or an orderly winding-down, a CSD should hold capital together with retained earnings and reserves that are sufficient, at all times, to withstand operational expenses over a period of time during which the CSD is able to reorganise its critical operations, including by recapitalising, replacing management, revising its business strategies, revising cost or fee structures and restructuring the services that it provides. Given that during the winding-down or restructuring of its activities, a CSD still needs to continue its usual operations and even though the actual expenses during a wind-down or restructuring of the operations of a CSD may be significantly higher than the gross annual operational expenses because of the restructuring or wind-down costs, the use of gross annual operational expenses as a benchmark for calculating the capital required should be an appropriate approximation of the actual expenses during the winding-down or restructuring of the operations of a CSD.

(6) Similarly to point (a) of Article 36(1) of Regulation (EU) No 575/2013, which requires institutions to deduct losses for the current financial year from the Common Equity Tier 1 capital, the role of net income in covering or absorbing the risks arising from adverse changes in the business conditions should also be recognised in this Regulation. Therefore, only in cases where the net income is insufficient to cover losses arising from the crystallisation of business risk, those losses have to be covered by own funds. Expected figures for the current year to take into account new circumstances should also be considered where data from the previous year are not available, such as in the case of newly established CSDs. In line with similar provisions in Commission Delegated Regulation (EU) No 152/2013[5], CSDs should be required to hold a minimum prudential amount of capital against business risk in order to guarantee a minimum prudential treatment.

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(7) In accordance with the CPSS-IOSCO Principles, tangible and intangible assets' amortisation and depreciation costs can be deducted from gross operational expenses for the calculation of the capital requirements. Since those costs do not generate actual cash flows that need to be backed by capital, such deductions should be applicable to the capital requirements for business risk and to those covering winding-down or restructuring.

(8) Since the time necessary for an orderly winding-down or restructuring strictly depends on the services provided by any individual CSD and on the market environment in which it operates, in particular on the possibility that another CSD can take on part or all of its services, the number of months required for restructuring of its activities or winding-down should be based on the CSD's own estimate. However, this period of time should not be less than the minimum number of months required for restructuring or winding-down provided for in Article 47 of Regulation (EU) No 909/2014 in order to ensure a prudent level of capital requirements.

(9) A CSD should design scenarios for restructuring of its activities or winding-down that are adapted to its business model. However, in order to obtain a harmonised application of the requirements on restructuring or winding-down in the Union and to ensure that prudentially sound requirements are satisfied, the discretion on the design of such scenarios should be limited by well-defined criteria.

(10) Regulation (EU) No 575/2013 is the relevant benchmark for the purpose of establishing the capital requirements for CSDs. In order to ensure consistency with that Regulation, the methodologies for the calculation of operational risk laid down in this Regulation should also be understood as covering legal risk for the purposes of this Regulation.

(11) Where there is a failure in the safekeeping of securities on behalf of a participant, such a failure would materialise as either a cost to the participant or as a cost for the CSD that would face legal claims. Therefore, rules for the calculation of the regulatory capital for operational risk already take into account the custody risk. For the same reasons, custody risk for securities held through a link with another CSD should not be subject to any additional regulatory capital charge but should be considered as part of the regulatory capital for operational risk. Similarly, custody risk faced by a CSD on own assets held by a custodian bank or other CSDs should not be double-counted and no additional regulatory capital should be required.

(12) A CSD may also face investment risks with regard to the assets that it owns or with regard to the investments that it makes using collateral, participants' deposits, loans to the participants or any other exposure under the allowed banking-type ancillary services. Investment risk is the risk of loss faced by a CSD when it invests its own or its participants' resources, such as collateral. Provisions set out in Directive 2013/36/EU of the European Parliament and of the Council[6], Regulation (EU) No 575/2013 and Delegated Regulation (EU) No 152/2013 are the appropriate benchmark for the purpose of establishing capital requirements to cover credit risk, counterparty credit risk and market risks that may arise from the investments of a CSD.

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(13) Given the nature of the activities of CSDs, a CSD assumes business risk due to potential changes in general business conditions that are likely to impair its financial position following a decline in its revenues or an increase in its expenses and that result in a loss that should be charged against its capital. Given that the level of business risk is highly dependent on the individual situation of each CSD and it can be caused by various factors, the capital requirements of this Regulation should be based on a CSD's own estimate and the methodology used by a CSD for such an estimate should be proportional to the scale and complexity of the CSD's activities. A CSD should develop its own estimate of the capital required against business risk under a set of stress scenarios in order to cover the risks that are not already captured by the methodology used for operational risk. In order to ensure a prudent level of the capital requirements for business risk when making a calculation based on self-designed scenarios, a minimum level of capital, should be introduced in the form of a prudential floor. The minimum level of required capital for business risk should be aligned to similar requirements for other market infrastructures in related Union Acts such as Commission Delegated Regulation on capital requirements for central counterparties ('CCPs').

(14) The additional capital surcharge for risks related to banking-type ancillary services should cover all the risks related to the provision of intraday credit to participants or other CSD users. Where overnight or longer credit exposures result from the provision of intraday credit, the corresponding risks should be measured and addressed by using the methodologies already laid down in Part Three, Title II, Chapter 2, for the Standardised Approach, and Chapter 3, for the Internal Ratings Based Approach (IRB Approach), of Regulation (EU) No 575/2013, given that that Regulation provides prudential rules for measurement of credit risk resulting from overnight or longer credit exposures. Intraday credit risks, however, require special treatment since the methodology for their measurement is not explicitly provided for in Regulation (EU) No 575/2013 or other applicable Union legislation. As a result, the methodology that specifically addresses intraday credit risk should be sufficiently risk-sensitive to take into account the quality of the collateral, the credit quality assessment of the participants and the actual observed intraday exposures. At the same time, the methodology should provide proper incentives to the providers of banking-type ancillary services, including the incentive to collect the highest quality of collateral and select creditworthy counterparties. Although providers of banking-type ancillary services have the obligation to properly assess and test the level and value of collateral and haircuts, the methodology used to determine the additional capital surcharge for intraday credit risk should nevertheless cater to and provide enough capital for the case where a sudden decrease in the value of the collateral exceeds estimates and results in partially uncollateralised residual credit exposures.

(15) The calculation of the capital surcharge for risks arising from providing banking-type ancillary services requires taking into account past information on intraday credit exposures. As a result, in order to be able to calculate that capital surcharge, entities that provide banking-type ancillary services to users of CSD services in accordance with Article 54(2) of Regulation (EU) No 909/2014 ('CSD-banking service providers')

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should record at least one year of data concerning their intraday credit exposures. Otherwise they are not able to identify the relevant exposures based on which the calculation is done. Consequently, CSD-banking service providers should not be required to meet the own funds requirement corresponding to the capital surcharge until after they are able to collect all the information necessary to perform the calculation of the surcharge.

(16) Article 54(8) of Regulation (EU) No 909/2014 requires the development of rules to determine the additional capital surcharge referred to in point (d) of Article 54(3) and point (e) of Article 54(4) of that Regulation. Further, Article 54 of that Regulation requires that additional surcharge reflects the intra-day credit risk resulting from the activities under Section C of the Annex to Regulation (EU) No 909/2014, and in particular the provisions of intraday credit to participants in a securities settlement system or other users of CSD services. Therefore, intraday credit risk exposure should also include the loss that a CSD-banking service provider would face if a borrowing participant were to default.

(17) Point (d) of Article 59(3) of Regulation (EU) No 909/2014 relating to the credit risk of a CSD-banking service provider requires the collection of 'highly liquid collateral with minimal credit and market risk'. Point (d) of Article 59(4) of Regulation (EU) No 909/2014 relating to the liquidity risk of a CSD-banking service provider, requires availability of 'qualifying liquid resources'. One such qualifying liquid resource is 'highly liquid collateral'. While it is understandable that the terminology used in each of the two cases is different, given the different nature of the risks involved and the correspondence to different concepts in the regulation of credit and liquidity risk, they both relate to a similarly high quality of providers or assets. Therefore, it would be appropriate to require that the same conditions are met before a collateral or a liquidity resource in the form of collateral can qualify as pertaining to either the 'highly liquid collateral with minimal credit and market risk' category', or to the 'qualifying liquid resources' category, respectively.

(18) Point (d) of Article 59(3) of Regulation (EU) No 909/2014 requires that a CSD-banking service provider accepts highly liquid collateral with minimal credit and market risk to manage its corresponding credit risk. The same allows for other types of collateral than highly liquid collateral with minimal credit and market risk to be used in specific situations, with the application of an appropriate haircut. To facilitate this, a clear hierarchy of the collateral quality should be set in order to distinguish which collateral should be acceptable to fully cover credit risk exposures, which collateral is acceptable as liquidity resource and which collateral, although remaining acceptable for mitigating credit risk, requires qualifying liquidity sources. Collateral providers should not be impeded from freely substituting collateral depending on their availability of resources or their asset-liability management strategies. Thus, common collateral practices, such as the reliance on participants' pledge accounts, where the collateral is deposited by the participant in its pledged accounts in order to fully cover any credit exposure should be allowed to be used for substituting collateral as long as the quality and liquidity of the collateral is monitored and complies with the requirements of this Regulation. Under such pledge account arrangements, the collateral is deposited by the participant in his