

MFSA

MALTA FINANCIAL SERVICES AUTHORITY

BANKING SUPERVISION UNIT

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Amendments to Banking Rule BR/12 ‘The Supervisory Review Process of Credit Institutions authorised under The Banking Act 1994’

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Directive 2013/36/EU (CRD IV) (applicable from 1 January 2014)

Since the relevant provisions in Directive 2013/36/EC are partly being transposed in the Banking Act (the Act), partly in the Banking Act (Supervisory Review) Regulations (Legal Notice), partly in Banking Rule BR/07 and partly in Banking Rule BR/12, credit institutions shall refer to the relevant provisions of Directive 2013/36/EU ([CRD IV](#)) until such time that the local legislation transposing the [CRD IV](#) comes into force.

Credit institutions shall also refer to any relevant articles in the [CRR](#), related [Regulatory/Implementing Technical Standards \(R/ITS\)](#) and [any EBA Guidelines](#) or EU legislation that may be issued from time to time.

Banking Rule BR/12 has been amended as follows:

Main body of Rule:

The reference to article 17D of the Act has been removed in view of the repeal of the said article. References to any relevant [Regulatory/Implementing Technical Standards \(R/ITS\)](#) and [any other Guidelines](#) or EU legislation which has been published or which is currently under development are being introduced.

Section V of Chapter 2 of Title VII (Articles 108 to 110) of the [CRD IV](#) has been transposed in the main body of Banking Rule BR/12 (paragraphs 6 to 6h) and a provision has also been inserted in relation to the required risk management processes and internal control mechanisms which are necessary in order to identify, measure, monitor and control transactions between credit institutions and their parent mixed-activity holding company and subsidiaries appropriately (paragraph 15b).

The *previous* paragraphs 7a, 9, 29a and 31 have been removed, paragraph 10 has been replaced and a new paragraph 8 has been inserted.

The obligations of the authority previously disclosed in Banking Rule BR/12 have now been reflected in the Banking Act (Supervisory Review) Regulations (Legal Notice), whereas the area of offences and penalties has been regulated entirely by the Act and the Administrative Penalties, Measures and Investigatory Powers Regulations (Legal Notice). Until such time these regulations enter into force, credit institutions shall refer to the [CRD IV](#).

List of Appendices and Annexes:

This has been updated to reflect the titles of the Appendices and Annexes.

Appendix 1 Internal Governance:

This Appendix has been replaced in its entirety. Credit institutions have now been referred to Article 91 of the [CRD IV](#), the EBA [Guidelines on Internal Governance \(GL 44\)](#) as well as the EBA [Guidelines on the Assessment of the Suitability of Members of the Management Body and Key Function Holders \(EBA/GL/2012/06\)](#). The *previous* '[Principles on Internal Governance](#)' have been retained on the authority's website for reference purposes only.

Appendix 2 ICAAP:

This Appendix has been replaced in its entirety. Credit institutions have now been referred to *Chapter 2.2 'Guidelines on ICAAP'* of the [Guidelines on the Application of the Supervisory Review Process under Pillar 2 \(GL03\)](#) and, once finalised, to the [Guidelines on Supervisory Review and Evaluation Process \(SREP\) and Pillar 2](#) which are currently being developed by the EBA. The *previous* '[Internal Capital Adequacy Assessment Process – General Framework](#)' has been retained on the authority's website for reference purposes only.

Annex 2A – ICAAP Report – Recommended Structure:

This Annex has been updated in view of the relevant technical standards and guidelines which have been issued by the EBA and in view of Recommendation B of the [Recommendation of the European Systemic Risk Board of 20 December 2012 on funding of credit institutions](#).

In particular, credit institutions have now also been referred to Banking Rule BR/16 on Funding Plans for Credit Institutions authorised under the Banking Act which adopts the requirements prescribed in the EBA [Guidelines on Harmonised Definitions and Templates for Funding Plans of Credit Institutions](#).

Furthermore, as from 1 January 2015, in view of the application of Article 451(1) of the [CRR](#), the ICAAP Report is to include information in relation to the risk of excessive

leverage. A section on Leverage has been introduced in this Annex accordingly, informing credit institutions about the information that should be included in the ICAAP report as from 1 January 2015. Credit institutions have also been referred to the [EBA Final draft Implementing Technical Standards \(ITS\) on Disclosure for Leverage Ratio](#), which will enter into force upon their publication in the Official Journal of the European Union.

A reference to the latest [Principles for the Sound Management of Operational Risk](#) published by the Basel Committee on Banking Supervision has also been inserted.

Annex 2B – Technical Criteria on Organisation & Treatment of Risks:

This Annex has been updated to reflect the obligations imposed on credit institutions by Articles 76 to 88 and 91 of the [CRD IV](#), on the arrangements, process and mechanisms of credit institutions in relation to technical criteria concerning the organisation and treatment of risks and governance.

Annex 2C – List of Definitions:

The definition of ‘Institutions’ has been removed due to the definition of institutions provided by the [CRR](#), which includes investment firms. The definition of ‘model risk’ as per the [CRR](#) has been inserted.

Annex 2D – Principles on Stress Testing:

This Annex has been replaced in its entirety. Credit institutions have now been referred to the [Guidelines on Stress Testing](#) and any reviews and/or updates that may be undertaken to such Guidelines from time to time. The *previous* ‘[Principles on Stress Testing](#)’ have been retained on the authority’s website for reference purposes only.

Annex 2E –Remuneration Principles: Policies, Committee and Elements

This Annex has been replaced in its entirety to reflect the obligations imposed on credit institutions by Articles 92 to 95 of the [CRD IV](#) on remuneration policies, including obligations on credit institutions that benefit from government intervention, variable elements of remuneration and the remuneration committee. Credit institutions have also been referred to the [Commission Delegated Regulation \(EU\) No 604/2014 of 4 March 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards with respect to qualitative and appropriate quantitative criteria to identify categories of staff whose professional activities have a material impact on an institution’s risk profile](#), the [Guidelines on Remuneration Policies](#) which were originally

published by the CEBS and which are to be reviewed and updated by the EBA in light of the requirements laid down in the [CRD IV](#), the EBA [Regulatory Technical Standards \(RTS\) on Classes of Instruments that are Appropriate to be used for the Purposes of Variable Remuneration](#), the [Guidelines on the Data Collection Exercise Regarding High Earners \(EBA/GL/2014/07\)](#), the [Guidelines on the Remuneration Benchmarking Exercise \(EBA/GL/2014/08\)](#), and the [Guidelines on the Applicable Notional Discount Rate for Variable Remuneration](#). The *previous* '[Principles for Remuneration Policies](#)' have been retained on the authority's website for reference purposes only.

Annex 2F – Principles for the Management of Interest Rate Risk in the Banking Book (IRRBB):

This Annex has been replaced in its entirety. Credit institutions have now been referred to the [Guidelines on the Technical Aspects of the Management of Interest Rate Risk Arising from Non-Trading Activities under the Supervisory Review Process](#), which were originally published by CEBS and which are to be reviewed and updated by the EBA. The *previous* '[Principles for the Management of Interest Rate Risk in the Banking Book \(IRRBB\)](#)' have been retained on the authority's website for reference purposes only.

Annex 2G – Principles for the Management of Concentration Risk:

This Annex has been replaced almost in its entirety. The section on *Concentration Risk to the 'Real Estate Sector'* has been retained. Credit institutions have now also been referred to the [Guidelines on the Management of Concentration Risk under the Supervisory Review Process \(GL31\)](#) and to the [Guidelines for Common Procedures and Methodologies for the Supervisory Review and Evaluation Process \(SREP\)](#). The *previous* '[Principles for the Management of Concentration Risk](#)' have been retained on the authority's website for reference purposes only.

Annex 2H – Principles on Risk Management:

No substantial changes have been made to this Annex.

Annex 2I – Principles for the Management of Operational Risk in Market-Related Activities:

This Annex has been replaced in its entirety. Credit institutions have now been referred to the [Guidelines on the Management of Operational Risks in Market-Related Activities](#), which were initially published by CEBS on 12 October 2010, and any reviews and/or updates that may be undertaken to such Guidelines from time to time. The *previous* '[Principles for the](#)

[Management of Operational Risk in Market-Related Activities](#)’ have been retained on the authority’s website for reference purposes only.

Appendix 3 SREP:

This Appendix has been replaced in its entirety. Credit institutions have now been referred to *Chapter 3 ‘Guidance for Supervisory Authorities’* of the [Guidelines on the Application of the Supervisory Review Process under Pillar 2 \(GL03\)](#) and to the [Guidelines for Common Procedures and Methodologies for the Supervisory Review and Evaluation Process \(SREP\)](#). The *previous* [General Framework of the Authority’s Supervisory Review and Evaluation Process](#) has been retained on the authority’s website for reference purposes only.

Annex 3A – SREP – ICAAP interaction process:

This Annex has been replaced in its entirety. Credit institutions have now been referred to *Diagram 1: the Supervisory Review Process* of the [Guidelines on the Application of the Supervisory Review Process under Pillar 2 \(GL03\)](#) and to the [Guidelines for Common Procedures and Methodologies for the Supervisory Review and Evaluation Process \(SREP\)](#). The *previous* [‘SREP-ICAAP Interaction Process’](#) has been retained on the authority’s website for reference purposes only.

Annex 3B – Technical Criteria on SREP:

This Annex has been replaced in its entirety. The provisions previously contained in this Annex are included in the new Banking Act (Supervisory Review) Regulations (Legal Notice). Until such time the said Regulations enter into force, the provisions found in Article 98 of the [CRD IV](#) shall apply. The *previous* [‘Technical Criteria on the Supervisory Review and Evaluation Process as Utilised by the Authority’](#) have been retained on the authority’s website for reference purposes only.

Annex 3C – Prudential Measures:

This Annex has been replaced in its entirety. In order to identify the prudential measures which can be exercised by the authority, credit institutions have now been referred to Article 104 of the [CRD IV](#), which shall apply for the purposes of determining the authority’s supervisory powers until the provisions of the new Banking Act (Supervisory Review) Regulations (Legal Notice) enter into force. The authority shall also be guided by *Chapter 4.2 ‘Guidelines on prudential measures’* of the [Guidelines on the Application of the Supervisory Review Process under Pillar 2 \(GL03\)](#) and to the [Guidelines for Common Procedures and](#)

[Methodologies for the Supervisory Review Process \(SREP\)](#). The *previous* [Prudential Measures](#) have been retained on the authority's website for reference purposes only.

Appendix 4 Obligations of the Authority as Consolidating Supervisor:

This Appendix has been replaced in its entirety. The provisions previously contained in this Appendix shall be included in the new Supervisory Consolidation Regulations (Legal Notice). Until such time the said Regulations enter into force, the provisions found the [CRD IV](#) shall apply. The *previous* '[Obligations of the Authority as Consolidating Supervisor](#)' have been retained on the authority's website for reference purposes only.

Appendix 5 Market Transparency on Asset Encumbrance and Monitoring Thereof:

This Appendix has been added for the purposes of implementing the requirements of Recommendations B and C of the [Recommendation of the European Systemic Risk Board of 20 December 2012 on funding of credit institutions](#). In complying with the requirements prescribed in Appendix 5, credit institutions have been referred to the instructions provided in the [EBA Final draft Implementing Technical Standards \(ITS\) on Supervisory Reporting \(Asset Encumbrance\)](#).

PUBLISHED DECEMBER 2013

Amendments due to CSR6

Main body of Rule: insertion of para 27a to reflect the requirement to allocate additional capital under Pillar II in line with the new 'BR/09/2013 Measures Addressing Credit Risks Arising from the Assessment of the Quality of Asset Portfolios of Credit Institutions authorised under the Banking Act 1994'.

Annex 2G: insertion of new Section F on Concentration Risk to the 'Real Estate Sector'.

Amendments to reflect requirements of MFSA Rule 1 of 2012 'Foreign Currency Lending' and MFSA Rule 2 of 2012 'US Dollar Funding'

Annex 2B: insertion of paragraphs 3d, 10k and 10l.

PUBLISHED JUNE 2013

Directive 2011/89/EU (FICOD I) Amendments (applicable from 10 June 2013)

Appendix 4, para 1: inserted reference to EU parent mixed financial holding company.

Appendix 4, para 5: inserted reference to EU parent mixed financial holding company.

Appendix 4, para 8: inserted reference to EU parent mixed financial holding company.

PUBLISHED APRIL 2012

The European Banking Authority (EBA), on 27th September 2011, published its latest Guidelines on Internal Governance which are aimed at enhancing and consolidating supervisory expectations and to ultimately improve the sound implementation of internal governance arrangements. Effective internal governance is fundamental if individual institutions and the banking system as a whole are to operate in the best possible manner. Accordingly, the MFSA transposed these new Guidelines in Banking Rule BR/12 under Appendix 1.

PUBLISHED MARCH 2012

The Committee of European Banking Supervisors (CEBS), on 10th December 2010, published its revised Guidelines on Remuneration Policies and Practices. Accordingly, in view of the emphasis being placed on the need for sound remuneration policies and practices and requirements in inter alia the EU's Capital Requirements Directive (CRD), the MFSA had taken steps to transpose these Guidelines in Banking Rule BR/12 under Annex 2E.

Moreover, through an amendment to Annex 3C 'The Authority's Prudential Measures', additional text was added to one of the measures available to the Authority, requiring a credit institution to hold own funds and/or Tier 1 capital above the minimum level required by BR/04. This amendment emanated from the recent changes adopted through the CRD III.

PUBLISHED DECEMBER 2011

Directive 2010/76/EU (CRD III) Amendments (applicable from 31 December 2011)

Annex 2B para 11(c): Included the following "*Transitional Provision: Credit institutions shall be required to apply the principles laid down herein to: (i) remuneration due on basis of contracts concluded before 30th December 2010 and awarded or paid after that date; and (ii) for services provided in 2010, remuneration awarded, but not yet paid, before 30th December 2010.*"

Annex 2E 3.1 'The basic principle of risk alignment' para 4: included definition of 'discretionary pension benefits' which means "*enhanced pension benefits granted on a discretionary basis by a credit institution to an employee as part of that employee's variable*

remuneration package, which do not include accrued benefits granted to an employee under the terms of the company pension scheme.”

Annex 3C ‘The Authority’s Prudential Measures’: Included two other measures available to the authority, being, requiring the credit institution to limit variable remuneration as a percentage of total net revenues when it is inconsistent with the maintenance of a sound capital base and requiring the credit institution to use net profits to strengthen its capital base.

Directive 2010/78/EU (OMNIBUS DIRECTIVE) Amendments (applicable from 31 December 2011)

Appendix 4 para 4: included text on EBA referral

Appendix 4 para 5: included text on EBA referral

Appendix 4 para 7: replaced CEBS with EBA

PUBLISHED JANUARY 2011

The Committee of European Banking Supervisors (CEBS) has, on 26th August and 2nd September 2010 respectively, published its revised Guidelines on Stress Testing (GL 32) and on Concentration Risk (GL31). Accordingly, these have been transposed to Banking Rule BR/12 Annex 2D and Annex 2G. These revised principles, which are to be followed by credit institutions when drawing up their ICAAPs have therefore replaced the principles found in the current version of BR/12, and should, in a proportionate manner, form an integral part of every credit institution’s risk management framework.

PUBLISHED OCTOBER 2010

Directive 2009/111/EC (CRD II) and Directive 2009/83/EC Amendments (applicable from 31 December 2010)

Main body of Rule: insertion of new paragraph 29a regarding the duties of the Authority as a consolidating supervisor;

Annex 2B: paragraph 5 to include reference to limits that may be set out by the credit institution in terms of Banking Rule BR/02;

Annex 2B: paragraph 6a on Securitisation Risks to include reference to reputational risks;

Annex 2B: paragraphs 10 (a) and (b) on Liquidity Risk were replaced with paragraphs 10 (a) to (j);

Annex 3B: inclusion of more details to paragraph (1)(e); and

Appendix 4: a new Appendix regarding the obligations of the Authority when acting as the consolidating supervisor.

Directive 2010/76/EU (CRD III) Amendments (applicable from 1 January 2011)

Main body of Rule: insertion of new paragraph 15a to benchmark credit institutions' remuneration trends and practices and collection of information on individuals per credit institution in pay brackets of at least €1 million; and

Annex 2B: inclusion of paragraph 11 containing detailed information on Remuneration Policies.

Banking Supervision Unit - MFSA