



HM Treasury, 1 Horse Guards Road, London, SW1A 2HQ

Sir William Cash  
Chair  
European Scrutiny Committee  
14 Tothill Street  
House of Commons  
London  
SW1H 9NB

11<sup>th</sup> October 2018

Dear Sir Bill,

7064/18: Proposal for a DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the issue of covered bonds and covered bond public supervision and amending Directive 2009/65/EC and Directive 2014/59/EU

7066/18: Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on amending Regulation (EU) No 575/2013 as regards exposures in the form of covered bonds

Thank you for your letter of 18 July on the EU covered bonds proposal, following our Explanatory Memorandum of 11 April 2018.

I am writing to provide you an update on the progress of these negotiations on the Commission's proposal which seeks to create a minimum-harmonising framework for EU covered bonds whilst avoiding disruption to the current national regimes and well-functioning markets. Under the ongoing negotiations in Council, Member States have agreed to this objective and have worked towards this overall aim.

On **third country equivalence**, we have noted the position taken in the European Parliament's draft report and welcome the approach taken here. In Council, a majority of Member States have agreed with the Commission approach, which is to wait for the EU implementation before considering extending the framework to third countries. If the current European Parliament approach is adopted in their final position, this will therefore be an issue for trilogue negotiations.

On the issue of **eligibility of assets**, Member States have successfully balanced the aim of introducing harmonised requirements to ensure that high quality assets serve as collateral whilst considering the specificities and differences across national covered bond regimes.

Some Member States have also been successful in introducing a new waiver on the use of derivative counterparts qualifying for a lower credit rating (credit quality step 3). This is to accommodate national specificities when Member States do not have enough credit institutions qualifying for higher ratings (credit quality step 1 or credit quality step 2). The use of such derivatives will only be available under specific conditions. Similarly, the eligibility of exposures for the purposes of the liquidity buffer is extended to credit quality step 3 institutions. Member States will have the ability to exclude such assets in their national framework to ensure that a high quality of covered bonds is maintained.

Another issue identified by the Commission's proposal relates to the overlap between the liquidity buffer and the Liquidity Coverage Requirement (LCR) in the Capital Requirements Regulation, whereby the same assets cannot count towards both buffers. This creates unnecessary complexity and disproportionate burdens for firms, who will unnecessarily need to meet duplicative requirements. To address this, the Commission proposed a Member State discretion to "not apply" the covered bond liquidity buffer requirement when other Union law applies.

On the issue of transposition, a majority of Member States have requested a longer period for them to transpose the Directive into their national framework whilst also providing enough time for firms to adjust to the domestic transposition they operate under. The Presidency has therefore proposed a longer transposition period of 18 months.

In terms of timing, the Rapporteur has published his draft report and has presented this to the Economic and Monetary Affairs Committee which should vote on it later next month. It is expected that, if negotiations continue at the current pace, trilogue negotiations could start under the current Austrian Presidency.

I am copying this letter to Lord Boswell of Aynho, Chair of the House of Lords European Union Committee; and copying this letter to Foeke Noppert, Clerk to the Commons Committee; Christopher Johnson, Clerk to the Lords Committee; Les Saunders, Department for Exiting the EU; Barbara Armstrong and Daniel Jones, HM Treasury.

*with very best regards*

*John*

JOHN GLEN  
ECONOMIC SECRETARY TO THE TREASURY