

European Commission  
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Financial Institutions

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## Response by the Swedish Authorities to the Commission Consultation Document on Countercyclical Capital Buffers

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*Sveriges Riksbank, the Swedish Financial Supervisory Authority and the Swedish Ministry of Finance (the Swedish Authorities) have decided to submit a common response to the Commission Consultation Document on Countercyclical Capital Buffers.*

**1. Could the general orientations indicated above foster a build-up in bank capital in good times and facilitate its release in bad times? Would you prefer the approach to determining the bank-specific buffer add-on as set out in paragraph 12, or would you prefer the alternatives set out under A. and B? Please give reasons for your answer.**

*The Swedish Authorities believe that the general construction of the countercyclical capital buffer as described in the Basel Committee proposals fosters a build-up of capital in good times which could be released in bad times. However, the decision to release the buffer in bad times should be supported by principles, which needs to be developed within the EU. We realize that such principles will be challenging to develop. Therefore, the harmonized principles must give room for national flexibility. Additionally, we believe that the construction of the buffer could provide the market with confidence that banks can use the released capital without jeopardising their solvency in times of stress.*

*Nevertheless, if bad times are coupled with higher market expectations on bank capital, we believe it is difficult to know ex ante the extent to which the released capital levels actually can and will be used for the intended purpose, i.e. provision of credit to the economy.*

*The Swedish Authorities support the approach for determining the bank-specific buffer that is set out in paragraph 12. We believe that this approach provides a level playing field for banks operating in the same Member State, regardless of organizational structure (branch or subsidiary). In order to achieve a harmonised global standard, we also believe that the implementation of new capital requirements in the EU through CRD IV should closely follow the BCBS proposals.*

**2. Would the approach for dealing with internationally active banks set out in paragraphs 12 to 20 help ensuring a level playing field between domestic and foreign**

**(located in other Member States and third countries) banks? Which of the three alternatives reduces the chances of regulatory arbitrage? Are there other ways in which potential regulatory arbitrage could be mitigated?**

*The Swedish Authorities believe that a level playing field is best kept with the proposal set out in paragraph 12, as it reflects the geographic location of their credit exposures. This proposal ensures that domestic and foreign banks will face the same buffer requirements for credit exposures located in the same Member State.*

*Adopting a common international regulation such as the Basel Committee's proposals facilitates international consistency, transparency and market understanding of countercyclical buffer decisions.*

**Could there be an incentive for regulatory arbitrage since credit institutions may gain benefits from booking exposures in jurisdictions with lower capital add-ons?**

*There is always a possibility that banks will try to gaming the buffer by shifting their credit exposures to jurisdictions with the lowest prevailing buffer. However, the Swedish Authorities agree with the opinion of the Basel Committee that this is expected only to have a marginal effect of the overall geographic allocation of individual bank credit exposures, not only because larger multinational companies often obtain a significant share of their financing through capital markets, but also since countercyclical buffers are far from constant and most of their time expected to be off or at very low levels.*

**3. Should the buffer requirement apply at a solo, sub-consolidated and consolidated basis (i.e. in accordance with the scope of application laid down in Articles 68 to 72 of 2006/48/EU)? Should supervisors be entitled to require credit institutions to hold the countercyclical buffer on a solo basis?**

*According to our opinion is it reasonable to deal with the buffer requirements according to the same principles as those laid down in Article 68-72 of 2006/48/EC. We do not have any objections against giving the Authority responsible for supervision of an individual institution the right to in an individual case refrain from holding the counter cyclical buffer on a solo basis, in order to allow for centralized capital management in cross-border banks. Article 131 of Directive 2006/48/EC could then be taken as a starting point.*

**4. Could a ceiling of 2.5% for the countercyclical buffer limit unduly the ability of national authorities to ensure the resilience of their banking system and constrain excessive credit growth? Please explain your views on the basis of expected costs and benefits.**

There is a strong need for consistent application of the countercyclical buffer requirements across different jurisdictions. As with other capital requirements in the CRD, the Swedish Authorities believe that the levels of countercyclical buffers should be considered as a minimum level of harmonized standard. However, if a competent authority would like to set a higher level than 2.5 %, that decision should be based on the same clear and well communicated principles as other buffer decisions.

**5. Should decisions for the EU countercyclical buffer be made transparent, explained and communicated to the market? Do you see a role for the ESRB in this regard? Please, explain the reasons for your reply.**

*Financial regulation should be as transparent and predictable as possible. This enhances effectiveness and is also important with regard to legal certainty. In the same vein, decisions concerning the countercyclical buffer should be transparent as well as clearly explained and communicated in a consistent way to financial markets.*

*The responsibility for communicating decisions on the national countercyclical buffer rests with the competent national authority. The overall principles for communication policy should be stated in the CRD in order to ensure a broad consistent view in this matter. The EBA – in consultation with the ESRB –, could have a role in establishing certain technical minimum requirements for information to markets.*

*The ESRB could have a role in explaining the rationale for the countercyclical buffer and how it affects the overall financial stability within the EU. In this way, it could contribute to a broader understanding of the purpose and acceptance of the countercyclical buffer.*

*In addition, the ESRB could also serve as an information hub, regularly collecting as stated in the ESRB regulation, summarizing and publishing information about the relevant buffer levels in EU countries. Furthermore, it could provide information about the buffer levels in 3rd country jurisdictions.*

**6. What are your views on the following potential roles for the ESRB and the EBA?**

*Decisions about the use of the countercyclical buffer are national. However, the risks that the buffers are supposed to limit may extend across national borders. Therefore, the possible risks to the financial system at EU level might not always be fully reflected in the national calculations or decisions. This clearly gives a rationale for discussing national buffers at EU-level. The ESRB, with responsibility for macro-prudential oversight at the EU-level, should have a prominent role in developing and monitoring the use of this macro-prudential instrument. Furthermore, a good cooperation between the EBA and the ESRB is necessary, in order to ensure a consistent application of buffer decisions and the availability of both macro- and micro-information in the analysis.*

*The Swedish Authorities support the division of labour outlined in the paper, which follows logically from the frameworks established in the ESRB and EBA regulations.*

**(a) The development of principles and technical standards as regards the exchange of information and promotion of consistency of the buffer decisions?**

*The division of labour between the EBA and the ESRB must be in line with the frameworks established in the ESRB and EBA regulations. Both the ESRB and the EBA should promote consistency of buffer decisions.*

*As stated in the Basel proposal, the credit/GDP gap would often have been a useful guide in taking buffer decisions in the past, but it does not always work well. Hence, there is a clear need to also analyse other macroeconomic and financial conditions and, in the end, to apply judgement. When designing a process for making such judgement at EU-level, a careful balance will need to be struck between the value of predictability and the need for flexibility. The value of predictability would speak in favour of a rather stringent evaluation process with clear benchmarks and thresholds. At the same time there must be reasonable room for flexibility as there are a number of conditions, beside the credit/GDP gap, which could and should be able to influence the decision on the buffer levels. In addition, economic and*

*financial structures differ between countries, requiring somewhat different analytical frameworks.*

*Weighing all these aspects together, it seems to be difficult to formulate very strict and precise decision rules. However, it would be valuable to formulate guidelines for the application of the buffer, in order to improve predictability. As a complement to general principles in the CRD, the ESRB should develop guide-lines concerning what relevant macroeconomic and financial conditions to analyse when deciding on buffer levels as well as the conditions for imposing and releasing the buffers from a European macro-prudential perspective. A good cooperation between the ESRB and the EBA would be necessary to ensure a consistent framework. Further guidance can be expected from the Basel Committee in this respect. The ESRB – with its macro-prudential perspective – is a natural place for discussion of such principles. To the extent that it is deemed valuable and feasible to formulate binding technical standards for specific conditions/factors, they should be developed by the EBA, in consultation with ESRB.*

*The EBA also has a natural overview role in the evaluation of the national implementation of buffer decisions, and its relation to the other parts of the capital adequacy framework, including its technical standards, as well as the arising home-host issues of ensuring that supervisors take buffer decisions of other Member States into account in setting requirements for cross-border banks.*

*Regarding the exchange of information, good cooperation is essential. The ESRB and EBA regulations establish a mutual duty of cooperation and provision of information. They should both provide each other with the information necessary for the achievement of their tasks in a timely manner. The practical forms for this should be developed shortly.*

**(b) Issuance by the ESRB, on the basis of its regular risk assessments, of specific recommendations on the levels of countercyclical buffers established by national authorities?**

*As mentioned earlier, the ESRB shall contribute to the prevention or mitigation of systemic risks to financial stability in **the EU as a whole**. National authorities can be expected to consider systemic risks primarily from a **national perspective**. The ESRB should, therefore, regularly analyse whether national authorities do take the EU perspective fully into account in their calculations of buffer levels. When the ESRB judges that this is not the case, and that the national calculations of the buffers are not reflecting the risks to financial stability at EU level, it would be reasonable that it issues recommendations on national buffers.*

*The ESRB can thus be expected to issue a recommendation, as stated in the ESRB regulation, on a specific buffer level when it judges a country or region to have an excessive credit growth and to not use the countercyclical buffer in a way that accounts for the increased risk to EU financial stability from this development. In order for the ESRB to be able to make such recommendations, it should be given access to the statistics used by national authorities in their calculations of national buffers.*

*National authorities might of course disagree with the ESRB recommendation, arguing that it does not reflect the country's contribution to the risks of the financial system in the EU. In accordance with the ESRB regulation, the country concerned will, in such a situation, in the end decide what national buffer to apply. However, there would be an ESRB discussion of the matter and the country concerned would be required to explain the rationale for its decision (according to the comply-or-explain mechanism outlined in the ESRB regulation).*

**(c) Oversight by the EBA to ensure that buffer decisions are implemented in an efficient and harmonised way?**

*The Swedish Authorities support giving the EBA an overview role in the evaluation of the national implementation of buffer decisions, and its relation to the other parts of the capital adequacy framework, including its technical standards. In relation to the arising home-host issues, the EBA should have an important role in ensuring that supervisors take buffer decisions of other Member States into account in setting requirements for cross-border banks.*

**(d) What are your views on the possible interaction between the respective roles of the ESRB and the EBA?**

*The Swedish Authorities find it important that the ESRB and the EBA cooperate closely, in accordance with the structure outlined in their respective regulations. The most reasonable division of labour regarding the countercyclical buffer would be the one outlined above.*

**7. What type of own fund instruments should be used to meet the countercyclical buffer requirement and why?**

*During the crisis, it became clear in the markets and during government interventions that common equity was superior in absorbing losses. The Swedish Authorities are therefore supportive of the BCBS proposals and are of the opinion that the countercyclical buffer should be met with only common equity. This will ensure that the buffer is built up by fully loss absorbing instruments.*

**8. How should "exposures" be weighed to meet the objectives of the countercyclical buffer (nominal or on the basis of Risk Weighted Assets)?**

*The Swedish Authorities believe that exposures should be weighted on the basis of risk, i.e. risk weighted assets. The buffer should be an integrated part of the risk weighted capital standard.*

**9. Should the countercyclical buffer apply to all exposures or be limited to certain types of exposures and if yes which? Please support your answer with reasons.**

*The buffer should apply to all exposures. If credit growth or other relevant risk factors are characteristic to certain asset classes other measures may be used in a future macro-prudential tool box.*

**10. In your view, should investment firms be excluded from the countercyclical buffer capital requirement? Please support your answer with expected costs and benefits.**

*The Swedish Authorities believe that investment firms should be included. Although, investments firms do not contribute to the build up of excessive leverage to a large extent, they might need a buffer in a future financial crisis. By applying the same rules for credit institutions and investment firms the risk of regulatory arbitrage would also be reduced. The Swedish Authorities would welcome a European impact assessment on how the buffer requirements would affect the investment firms if applied.*

**11. Do you have other comments or suggestions?**

- *The optimal timing for implementation of the proposals would be as soon as possible.*
- *The Swedish Authorities have a strong preference for adhering closely to the BCBS proposals in the implementation of new capital requirements in the EU. We believe it would be unwise to open up the Basel agreement by adding new alternatives, such as A and B options in this consultation, in each part of the standard.*
- *Many EU countries are in the process of establishing a macro-prudential policy framework, including allocation of mandates and tools. These processes will most likely result in different governance structures in different countries. It is, therefore, important that the Commission, when formulating the legal framework, allows for such differences. In other words, the framework must enable both for central banks as well as supervisory authorities to be the authority in charge of the conduct of national macro-prudential policy.*

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