

Chapter 1

Commission Delegated Regulation (EU) No 528/2014

Preamble

THE EUROPEAN COMMISSION,

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

Having regard to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012, and in particular the third subparagraph of Article 329(3), the third subparagraph of Article 352(6) and the third subparagraph of Article 358(4) thereof.

01/01/2021

Whereas:

(1) In light of the mandate contained in Regulation (EU) No 575/2013 to develop a range of methods to reflect other risks, apart from delta risk, in the own funds requirements of institutions, "in a manner proportionate to the scale and complexity of institutions' activities in options and warrants", it is appropriate to design approaches with different levels of sophistication and risk sensitivity which may be suitable for different profiles of institutions. It is, therefore, appropriate to provide for the following three approaches in order of increasing complexity to measure non-delta risks of options and warrants: (i) the simplified approach; (ii) the delta-plus approach; and (iii) the scenario approach. This framework based on three approaches largely implements the non-delta-risk framework provided for by the Basel Committee for Banking Supervision (BCBS), with the necessary adjustments to take into account Regulation (EU) No 575/2013. That has the added benefit of ensuring consistency between Union rules and internationally agreed minimum standards.

(2) Given it is necessary to provide institutions that apply the delta-plus approach the possibility of treating non-continuous options in a more risk-sensitive way, institutions should be able to combine the approaches provided for the measurement of the risk of options and warrants under certain conditions, not only within groups but also within single legal entities. Nevertheless, in order to avoid the possibility of selective application of approaches by institutions with the view to minimizing their own funds requirements, the combination of approaches on an individual basis should only be allowed on the condition that institutions specify the scope of application of each approach before beginning to use it, so as to apply it consistently over time.

(3) Non-delta risks related to options and warrants can include, but are not limited to, risks arising from changes in the instrument's gamma referred to as "gamma risk" or

"convexity risk" as set out in Article 4(1)(a) of this Regulation, risks arising from changes in its vega referred to as "vega risk" or "volatility risk" as set out in Article 4(1)(b) of this Regulation, risks arising from changes in interest rates referred to as "interest rate risk" or "rho risk", nonlinearities which cannot be captured by gamma risk and the risk of implied correlation on basket options or warrants. Of those risks, only the gamma and vega risks are of such materiality that justify the imposition of own funds capital requirements, even for the more complex institutions and, therefore, only those types of risks should be covered in the calculation of own funds requirements. Regulation (EU) No 575/2013 requires institutions to obtain prior permission from their competent authority to use an internal model to calculate delta. However, the use of non-delta risk approaches is to be monitored and assessed under the supervisory review and evaluation process of institutions set out by the provisions of Directive 2013/36/EU of the European Parliament and of the Council. Furthermore, the greater complexity of the scenario approach necessitates closer monitoring by competent authorities and hence, its use by institutions should be subject to specified conditions of application, both prior to its first use and on an on-going basis.

(4) Given that Article 330 of Regulation (EU) No 575/2013 concerning the treatment of fixed-to-floating interest-rate swaps applies only for interest rate risk purposes, it should not be taken into consideration for certain financial instruments such as swaptions.

(5) The provisions in this Regulation are closely linked, since they all deal with the measurement of non-delta risks of options and warrants related to different underlyings. To ensure coherence between those provisions, which should enter into force at the same time, and to facilitate a comprehensive view and compact access to them by persons subject to those obligations, it is desirable to include all the regulatory technical standards required by Regulation (EU) No 575/2013 on this matter in a single Regulation.

(6) This Regulation is based on the draft regulatory technical standards submitted by the European Banking Authority to the Commission.

(7) The European Banking Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the opinion of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council,

HAS ADOPTED THIS REGULATION: