Chapter 1

Commission Delegated Regulation (EU) 2016/101

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 105(14) thereof,

01/01/2021

Whereas:

(1) Article 105 of Regulation (EU) No 575/2013 refers to the prudent valuation standards applicable to all trading book positions. However, Article 34 of that Regulation requires institutions to apply the standards of Article 105 to all assets measured at fair value. The combination of the above articles implies that the prudent valuation requirements apply to all fair-valued positions regardless of whether they are held in the trading book or not, where the term "positions" refers solely to financial instruments and commodities.

(2) Where the application of prudent valuation would lead to a lower absolute carrying value for assets or a higher absolute carrying value for liabilities than recognised in accounting, an additional valuation adjustment (AVA) should be calculated as the absolute value of the difference between the two, as the prudent value should always be equal to or lower than the fair value for assets and equal to or higher than the fair value for liabilities.

(3) For valuation positions for which a change in accounting valuation has only a partial or zero impact on Common Equity Tier 1 capital, AVAs should only be applied based on the proportion of the accounting valuation change that impacts Common Equity Tier 1 capital. These include positions subject to hedge accounting, Available-For-Sale positions to the extent their valuation changes are subject to a prudential filter and exactly matching, offsetting positions.

(4) AVAs are determined only for the purpose of calculating adjustments to Common Equity Tier 1 capital, where necessary. AVAs do not affect the determination of the own funds requirements according to Article 92 of Regulation (EU) No 575/2013 (unless the derogation for small trading book business according to Article 94 of that Regulation applies).

(5) In order to provide a consistent framework by which AVAs are calculated by institutions, a clear definition of the target level of certainty and the elements of valuation uncertainty that should be considered when determining a prudent value is necessary together with defined methodologies for achieving the required level of certainty based on current market conditions.

(6) Market price uncertainty, close-out costs and model risk AVAs should be calculated on the basis of Valuation Exposures, which are based on financial instruments or portfolios of financial instruments. For those purposes, financial instruments may be combined to portfolios when, for market price uncertainty and close-out costs AVAs, the instruments are valued on the basis of the same risk factor or when, for model risk AVAs, they are valued on the basis of the same pricing model.

(7) Given that certain AVAs that relate to valuation uncertainty are not additive, an aggregation approach that can take account of diversification benefits should be permitted within certain categories of AVAs for the elements of the AVA that do not relate to an element of expected exit cost that is not included in fair value. For the purpose of aggregating AVAs it should also be made possible to receive diversification benefits on the difference between the expected value and the prudent value so that banks with a fair value which is already more prudent than expected value do not get less diversification benefit than those that use the expected value as the fair value.

(8) Since institutions with small fair value portfolios will typically be subject to limited valuation uncertainty, they should be permitted to apply a simpler approach to estimate AVAs than those institutions with larger fair value portfolios. The size of fair value portfolios, for the purpose of determining whether a simpler approach can be applied, should be assessed at each level at which capital requirements are calculated.

(9) In order for competent authorities to be able to assess those institutions have correctly applied the requirements for assessing the aggregate level of AVAs required, appropriate documentation, systems and controls should be maintained by institutions.

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

(11) 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: