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THE EUROPEAN PARLIAMENT

THE COUNCIL

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LEGISLATIVE ACTS AND OTHER INSTRUMENTS

Subject: REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulation (EU) No 575/2013 as regards minimum loss coverage for non-performing exposures

REGULATION (EU) 2019/...
OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL

of ...

amending Regulation (EU) No 575/2013
as regards minimum loss coverage for non-performing exposures

(Text with EEA relevance)

THE EUROPEAN PARLIAMENT AND THE COUNCIL OF THE EUROPEAN UNION,

Having regard to the Treaty on the Functioning of the European Union, and in particular Article 114 thereof,

Having regard to the proposal from the European Commission,

After transmission of the draft legislative act to the national parliaments,

Having regard to the opinion of the European Central Bank¹,

Having regard to the opinion of the European Economic and Social Committee²,

Acting in accordance with the ordinary legislative procedure³,

¹ OJ C 79, 4.3.2019, p. 1.

² OJ C 367, 10.10.2018, p. 43.

³ Position of the European Parliament of 14 March 2019 (not yet published in the Official Journal) and decision of the Council of

Whereas:

- (1) The establishment of a comprehensive strategy to address non-performing exposures (NPEs) is an important goal for the Union in its attempt to make the financial system more resilient. While addressing NPEs is primarily the responsibility of banks and Member States, there is also a clear Union dimension to reducing the current high stock of NPEs, to preventing any excessive build-up of NPEs in the future and to preventing the emergence of systemic risks in the non-banking sector. Given the interconnectedness of the banking and financial systems across the Union, where banks operate in multiple jurisdictions and Member States, there is significant potential for spill-over effects for Member States and for the Union as a whole, both in terms of economic growth and financial stability.

- (2) The financial crisis led to the build-up of NPEs in the banking sector. Consumers were significantly affected by the subsequent recession and the drop in housing prices. Safeguarding consumers' rights in line with relevant Union law such as Directives 2008/48/EC¹ and 2014/17/EU² of the European Parliament and of the Council is essential when tackling the issue of NPEs. Directive 2011/7/EU of the European Parliament and of the Council³ encourages prompt payment by both enterprises and public authorities and helps prevent the kind of build-up of NPEs that occurred during the years of the financial crisis.
- (3) An integrated financial system will enhance the resilience of the Economic and Monetary Union to adverse shocks by facilitating cross-border private risk-sharing, while at the same time reducing the need for public risk-sharing. In order to achieve those objectives, the Union should complete the banking union and further develop a capital markets union. Addressing possible future NPE accumulation is essential to strengthening the banking union as it is essential for ensuring competition in the banking sector, preserving financial stability and encouraging lending, so as to create jobs and growth within the Union.

¹ Directive 2008/48/EC of the European Parliament and of the Council of 23 April 2008 on credit agreements for consumers and repealing Council Directive 87/102/EEC (OJ L 133, 22.5.2008, p. 66).

² Directive 2014/17/EU of the European Parliament and of the Council of 4 February 2014 on credit agreements for consumers relating to residential immovable property and amending Directives 2008/48/EC and 2013/36/EU and Regulation (EU) No 1093/2010 (OJ L 60, 28.2.2014, p. 34).

³ Directive 2011/7/EU of the European Parliament and of the Council of 16 February 2011 on combating late payment in commercial transactions (OJ L 48, 23.2.2011, p. 1).

- (4) In its 'Action plan to tackle non-performing loans in Europe' of 11 July 2017, the Council called upon various institutions to take appropriate measures to further address the high number of NPEs in the Union and to prevent their build-up in the future. The action plan sets out a comprehensive approach that focuses on a mix of complementary policy actions in four areas: (i) supervision; (ii) structural reforms of insolvency and debt recovery frameworks; (iii) development of secondary markets for distressed assets; (iv) fostering restructuring of the banking system. Actions in those areas are to be taken at Union and at national level, where appropriate. The Commission announced a similar intention in its 'Communication on completing the Banking Union' of 11 October 2017, which called for a comprehensive package on tackling non-performing loans (NPLs) within the Union.

- (5) Regulation (EU) No 575/2013 of the European Parliament and of the Council¹ forms, together with Directive 2013/36/EU of the European Parliament and of the Council², the legal framework governing the prudential rules for credit institutions and investment firms (referred to collectively as 'institutions'). Regulation (EU) No 575/2013 contains, *inter alia*, provisions directly applicable to institutions for determining their own funds. It is therefore necessary to complement the existing prudential rules in Regulation (EU) No 575/2013 relating to own funds with provisions requiring a deduction from own funds where NPEs are not sufficiently covered by provisions or other adjustments. Such requirement would effectively amount to creating a prudential backstop for NPEs that would apply uniformly to all institutions in the Union, and would also cover institutions which are active on the secondary market.

¹ 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 (OJ L 176, 27.6.2013, p. 1).

² Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC (OJ L 176, 27.6.2013, p. 338).

- (6) The prudential backstop should not prevent competent authorities from exercising their supervisory powers in accordance with Directive 2013/36/EU. Where competent authorities ascertain on a case-by-case basis that, despite the application of the prudential backstop for NPEs established by this Regulation, the NPEs of a specific institution are not sufficiently covered, it should be possible for them to make use of the supervisory powers provided for in Directive 2013/36/EU, including the power to require institutions to apply a specific provisioning policy or treatment of assets in terms of own funds requirements. Therefore, it is possible, on a case-by-case basis, for the competent authorities to go beyond the requirements laid down in this Regulation for the purpose of ensuring sufficient coverage for NPEs.

- (7) For the purposes of applying the prudential backstop, it is appropriate to introduce in Regulation (EU) No 575/2013 a clear set of conditions for the classification of NPEs. As Commission Implementing Regulation (EU) No 680/2014¹ already lays down criteria concerning NPEs for the purposes of supervisory reporting, it is appropriate that the classification of NPEs build on that existing framework. Implementing Regulation (EU) No 680/2014 refers to defaulted exposures as defined for the purpose of calculating own funds requirements for credit risk and impaired exposures pursuant to the applicable accounting framework. As forbearance measures might influence whether an exposure is classified as non-performing, the classification criteria are complemented by clear criteria on the impact of forbearance measures. Forbearance measures should aim to return the borrower to a sustainable performing repayment status and should comply with Union consumer protection law and in particular with Directives 2008/48/EC and 2014/17/EU, but might have different justifications and consequences. It is therefore appropriate to provide that a forbearance measure granted to a non-performing exposure should not discontinue the classification of that exposure as non-performing unless certain strict discontinuation criteria are fulfilled.

¹ Commission Implementing Regulation (EU) No 680/2014 of 16 April 2014 laying down implementing technical standards with regard to supervisory reporting of institutions according to Regulation (EU) No 575/2013 of the European Parliament and of the Council (OJ L 191, 28.6.2014, p. 1).

- (8) The longer an exposure has been non-performing, the lower the probability for the recovery of its value. Therefore, the portion of the exposure that should be covered by provisions, other adjustments or deductions should increase with time, following a pre-defined calendar. NPEs purchased by an institution should therefore be subject to a calendar that starts to run from the date on which the NPE was originally classified as non-performing, and not from the date of its purchase. For that purpose, the seller should inform the buyer of the date of the classification of the exposure as non-performing.
- (9) Partial write-offs should be taken into account when calculating the specific credit risk adjustments. In order to avoid any double counting of the write-off, it is necessary to use the original exposure value prior to the partial write-off. The inclusion of partial write-offs in the list of items that can be used to meet the requirements of the backstop should encourage institutions to recognise write-offs in a timely manner. For NPEs purchased by an institution at a price lower than the amount owed by the debtor, the purchaser should treat the difference between the purchase price and the amount owed by the debtor in the same way as a partial write-off for the purpose of the prudential backstop.

- (10) Secured NPEs are generally expected to result in a less significant loss than unsecured NPEs, as the credit protection securing the NPE gives the institution a specific claim on an asset or against a third party in addition to the institution's general claim against the defaulted borrower. In the case of an unsecured NPE, only the general claim against the defaulted borrower would be available. Given the higher loss expected on unsecured NPEs, a stricter calendar should be applied.
- (11) An exposure which is only partly covered by eligible credit protection should be considered as secured for the covered part, and as unsecured for the part which is not covered by eligible credit protection. In order to determine which parts of NPEs are to be treated as secured or unsecured, the eligibility criteria for credit protection and for fully and completely securing mortgages used for the purposes of the calculation of own funds requirements should be applied in accordance with the relevant approach under Regulation (EU) No 575/2013, including applicable value adjustment.

- (12) The same calendar should be applied irrespective of the reason for which the exposure is non-performing. The prudential backstop should be applied at an exposure-by-exposure level. A calendar of three years should apply for unsecured NPEs. In order to allow institutions and Member States to improve the efficiency of restructuring or of enforcement proceedings, as well as to recognise that NPEs secured by immovable collateral and residential loans guaranteed by an eligible protection provider as defined in Regulation (EU) No 575/2013 will have a remaining value for a longer period of time after the loan has been classified as non-performing, it is appropriate to provide for a calendar of nine years. For other secured NPEs a calendar of seven years should apply in order to build up full coverage.

- (13) It should be possible to take forbearance measures into account for the purpose of applying the relevant coverage factor. More precisely, the exposure should continue to be classified as non-performing but the coverage requirement should remain stable for one additional year. Therefore, the factor that would be applicable during the year in which the forbearance measure has been granted should be applicable for two years. Where, upon the expiry of the additional year, the exposure is still non-performing, the applicable factor should be determined as if no forbearance measure had been granted, taking into account the date on which the exposure was originally classified as non-performing. Given that granting forbearance measures should not lead to any arbitrage, that additional year should only be permitted in respect of the first forbearance measure that has been granted since the classification of the exposure as non-performing. In addition, the one-year period during which the coverage factor remains unchanged should not lead to the extension of the provisioning calendar. As a result, any forbearance measure granted in the third year after the classification as NPE for unsecured exposures, or in the seventh year after the classification as NPE for secured exposures, should not delay the full coverage of the NPE.

- (14) In order to ensure that the credit protection valuation of institutions' NPEs follows a prudent approach, the European Supervisory Authority (European Banking Authority) (EBA) should consider the need for, and if necessary develop, a common methodology, in particular regarding assumptions pertaining to recoverability and enforceability, and possibly including minimum requirements for re-valuation of the credit protection in terms of timing.
- (15) In order to facilitate a smooth transition towards the new prudential backstop, the new rules should not be applied in relation to exposures originated prior to ... [the date of entry into force of this amending Regulation].
- (16) In order to ensure that the amendments to Regulation (EU) No 575/2013 introduced by this Regulation apply in a timely manner, this Regulation should enter into force on the date following that of its publication in the Official Journal of the European Union.
- (17) Regulation (EU) No 575/2013 should therefore be amended accordingly,

HAVE ADOPTED THIS REGULATION:

Article 1

Regulation (EU) No 575/2013 is amended as follows:

(1) in Article 36(1), the following point is added:

'(m) the applicable amount of insufficient coverage for non-performing exposures.';

(2) the following Articles are inserted:

'Article 47a

Non-performing exposures

1. For the purposes of point (m) of Article 36(1), exposure shall include any of the following items, provided they are not included in the trading book of the institution:
 - (a) a debt instrument, including a debt security, a loan, an advance and a demand deposit;
 - (b) a loan commitment given, a financial guarantee given or any other commitment given, irrespective of whether it is revocable or irrevocable, with the exception of undrawn credit facilities that may be cancelled unconditionally at any time and without notice, or that effectively provide for automatic cancellation due to deterioration in the borrower's creditworthiness.

2. For the purposes of point (m) of Article 36(1), the exposure value of a debt instrument shall be its accounting value measured without taking into account any specific credit risk adjustments, additional value adjustments in accordance with Articles 34 and 105, amounts deducted in accordance with point (m) of Article 36(1), other own funds reductions related to the exposure or partial write-offs made by the institution since the last time the exposure was classified as non-performing.

For the purposes of point (m) of Article 36(1), the exposure value of a debt instrument that was purchased at a price lower than the amount owed by the debtor shall include the difference between the purchase price and the amount owed by the debtor.

For the purposes of point (m) of Article 36(1), the exposure value of a loan commitment given, a financial guarantee given or any other commitment given as referred to in point (b) of paragraph 1 of this Article shall be its nominal value, which shall represent the institution's maximum exposure to credit risk without taking account of any funded or unfunded credit protection. The nominal value of a loan commitment given shall be the undrawn amount that the institution has committed to lend and the nominal value of a financial guarantee given shall be the maximum amount the entity could have to pay if the guarantee is called on.

The nominal value referred to in the third subparagraph of this paragraph shall not take into account any specific credit risk adjustment, additional value adjustments in accordance with Articles 34 and 105, amounts deducted in accordance with point (m) of Article 36(1) or other own funds reductions related to the exposure.

3. For the purposes of point (m) of Article 36(1), the following exposures shall be classified as non-performing:
 - (a) an exposure in respect of which a default is considered to have occurred in accordance with Article 178;
 - (b) an exposure which is considered to be impaired in accordance with the applicable accounting framework;
 - (c) an exposure under probation pursuant to paragraph 7, where additional forbearance measures are granted or where the exposure becomes more than 30 days past due;
 - (d) an exposure in the form of a commitment that, were it drawn down or otherwise used, would likely not be paid back in full without realisation of collateral;

- (e) an exposure in form of a financial guarantee that is likely to be called by the guaranteed party, including where the underlying guaranteed exposure meets the criteria to be considered as non-performing.

For the purposes of point (a), where an institution has on-balance-sheet exposures to an obligor that are past due by more than 90 days and that represent more than 20 % of all on-balance-sheet exposures to that obligor, all on- and off-balance-sheet exposures to that obligor shall be considered to be non-performing.

- 4. Exposures that have not been subject to a forbearance measure shall cease to be classified as non-performing for the purposes of point (m) of Article 36(1) where all the following conditions are met:
 - (a) the exposure meets the exit criteria applied by the institution for the discontinuation of the classification as impaired in accordance with the applicable accounting framework and of the classification as defaulted in accordance with Article 178;
 - (b) the situation of the obligor has improved to the extent that the institution is satisfied that full and timely repayment is likely to be made;
 - (c) the obligor does not have any amount past due by more than 90 days.

5. The classification of a non-performing exposure as non-current asset held for sale in accordance with the applicable accounting framework shall not discontinue its classification as non-performing exposure for the purposes of point (m) of Article 36(1).
6. Non-performing exposures subject to forbearance measures shall cease to be classified as non-performing for the purposes of point (m) of Article 36(1) where all the following conditions are met:
 - (a) the exposures have ceased to be in a situation that would lead to their classification as non-performing under paragraph 3;
 - (b) at least one year has passed since the date on which the forbearance measures were granted and the date on which the exposures were classified as non-performing, whichever is later;
 - (c) there is no past-due amount following the forbearance measures and the institution, on the basis of the analysis of the obligor's financial situation, is satisfied about the likelihood of the full and timely repayment of the exposure.

Full and timely repayment shall not be considered likely unless the obligor has executed regular and timely payments of amounts equal to either of the following:

- (a) the amount that was past due before the forbearance measure was granted, where there were amounts past due;
 - (b) the amount that has been written-off under the forbearance measures granted, where there were no amounts past due.
7. Where a non-performing exposure has ceased to be classified as non-performing pursuant to paragraph 6, such exposure shall be under probation until all the following conditions are met:
- (a) at least two years have passed since the date on which the exposure subject to forbearance measures was re-classified as performing;
 - (b) regular and timely payments have been made during at least half of the period that the exposure would be under probation, leading to the payment of a substantial aggregate amount of principal or interest;
 - (c) none of the exposures to the obligor is more than 30 days past due.

Article 47b

Forbearance measures

1. Forbearance measure is a concession by an institution towards an obligor that is experiencing or is likely to experience difficulties in meeting its financial commitments. A concession may entail a loss for the lender and shall refer to either of the following actions:
 - (a) a modification of the terms and conditions of a debt obligation, where such modification would not have been granted had the obligor not experienced difficulties in meeting its financial commitments;
 - (b) a total or partial refinancing of a debt obligation, where such refinancing would not have been granted had the obligor not experienced difficulties in meeting its financial commitments.

2. At least the following situations shall be considered forbearance measures:
 - (a) new contract terms are more favourable to the obligor than the previous contract terms, where the obligor is experiencing or is likely to experience difficulties in meeting its financial commitments;

- (b) new contract terms are more favourable to the obligor than contract terms offered by the same institution to obligors with a similar risk profile at that time, where the obligor is experiencing or is likely to experience difficulties in meeting its financial commitments;
- (c) the exposure under the initial contract terms was classified as non-performing before the modification to the contract terms or would have been classified as non-performing in the absence of modification to the contract terms;
- (d) the measure results in a total or partial cancellation of the debt obligation;
- (e) the institution approves the exercise of clauses that enable the obligor to modify the terms of the contract and the exposure was classified as non-performing before the exercise of those clauses, or would be classified as non-performing were those clauses not exercised;
- (f) at or close to the time of the granting of debt, the obligor made payments of principal or interest on another debt obligation with the same institution, which was classified as a non-performing exposure or would have been classified as non-performing in the absence of those payments;
- (g) the modification to the contract terms involves repayments made by taking possession of collateral, where such modification constitutes a concession.

3. The following circumstances are indicators that forbearance measures may have been adopted:
 - (a) the initial contract was past due by more than 30 days at least once during the three months prior to its modification or would be more than 30 days past due without modification;
 - (b) at or close to the time of concluding the credit agreement, the obligor made payments of principal or interest on another debt obligation with the same institution that was past due by 30 days at least once during the three months prior to the granting of new debt;
 - (c) the institution approves the exercise of clauses that enable the obligor to change the terms of the contract, and the exposure is 30 days past due or would be 30 days past due were those clauses not exercised.

4. For the purposes of this Article, the difficulties experienced by an obligor in meeting its financial commitments shall be assessed at obligor level, taking into account all the legal entities in the obligor's group which are included in the accounting consolidation of the group, and natural persons who control that group.

Article 47c

Deduction for non-performing exposures

1. For the purposes of point (m) of Article 36(1), institutions shall determine the applicable amount of insufficient coverage separately for each non-performing exposure to be deducted from Common Equity Tier 1 items by subtracting the amount determined in point (b) of this paragraph from the amount determined in point (a) of this paragraph, where the amount referred to in point (a) exceeds the amount referred to in point (b):
 - (a) the sum of:
 - (i) the unsecured part of each non-performing exposure, if any, multiplied by the applicable factor referred to in paragraph 2;
 - (ii) the secured part of each non-performing exposure, if any, multiplied by the applicable factor referred to in paragraph 3;
 - (b) the sum of the following items provided they relate to the same non-performing exposure:
 - (i) specific credit risk adjustments;
 - (ii) additional value adjustments in accordance with Articles 34 and 105;

- (iii) other own funds reductions;
- (iv) for institutions calculating risk-weighted exposure amounts using the Internal Ratings Based Approach, the absolute value of the amounts deducted pursuant to point (d) of Article 36(1) which relate to non-performing exposures, where the absolute value attributable to each non-performing exposure is determined by multiplying the amounts deducted pursuant to point (d) of Article 36(1) by the contribution of the expected loss amount for the non-performing exposure to total expected loss amounts for defaulted or non-defaulted exposures, as applicable;
- (v) where a non-performing exposure is purchased at a price lower than the amount owed by the debtor, the difference between the purchase price and the amount owed by the debtor;
- (vi) amounts written-off by the institution since the exposure was classified as non-performing.

The secured part of a non-performing exposure is that part of the exposure which, for the purpose of calculating own funds requirements pursuant to Title II of Part Three, is considered to be covered by a funded credit protection or unfunded credit protection or fully and completely secured by mortgages.

The unsecured part of a non-performing exposure corresponds to the difference, if any, between the value of the exposure as referred to in Article 47a(1) and the secured part of the exposure, if any.

2. For the purposes of point (a)(i) of paragraph 1, the following factors shall apply:
 - (a) 0,35 for the unsecured part of a non-performing exposure to be applied during the period between the first and the last day of the third year following its classification as non-performing;
 - (b) 1 for the unsecured part of a non-performing exposure to be applied as of the first day of the fourth year following its classification as non-performing.

3. For the purposes of point (a)(ii) of paragraph 1, the following factors shall apply:
 - (a) 0,25 for the secured part of a non-performing exposure to be applied during the period between the first and the last day of the fourth year following its classification as non-performing;
 - (b) 0,35 for the secured part of a non-performing exposure to be applied during the period between the first and the last day of the fifth year following its classification as non-performing;

- (c) 0,55 for the secured part of a non-performing exposure to be applied during the period between the first and the last day of the sixth year following its classification as non-performing;
- (d) 0,70 for the part of a non-performing exposure secured by immovable property pursuant to Title II of Part Three or that is a residential loan guaranteed by an eligible protection provider as referred to in Article 201, to be applied during the period between the first and the last day of the seventh year following its classification as non-performing;
- (e) 0,80 for the part of a non-performing exposure secured by other funded or unfunded credit protection pursuant to Title II of Part Three to be applied during the period between the first and the last day of the seventh year following its classification as non-performing;
- (f) 0,80 for the part of a non-performing exposure secured by immovable property pursuant to Title II of Part Three or that is a residential loan guaranteed by an eligible protection provider as referred to in Article 201, to be applied during the period between the first and the last day of the eighth year following its classification as non-performing;

- (g) 1 for the part of a non-performing exposure secured by other funded or unfunded credit protection pursuant to Title II of Part Three to be applied as of the first day of the eighth year following its classification as non-performing;
 - (h) 0,85 for the part of a non-performing exposure secured by immovable property pursuant to Title II of Part Three or that is a residential loan guaranteed by an eligible protection provider as referred to in Article 201, to be applied during the period between the first and the last day of the ninth year following its classification as non-performing;
 - (i) 1 for the part of a non-performing exposure secured by immovable property pursuant to Title II of Part Three or that is a residential loan guaranteed by an eligible protection provider as referred to in Article 201, to be applied as of the first day of the tenth year following its classification as non-performing.
4. By way of derogation from paragraph 3, the following factors shall apply to the part of the non-performing exposure guaranteed or insured by an official export credit agency:
- (a) 0 for the secured part of the non-performing exposure to be applied during the period between one year and seven years following its classification as non-performing; and

- (b) 1 for the secured part of the non-performing exposure to be applied as of the first day of the eighth year following its classification as non-performing.
5. EBA shall assess the range of practices applied for the valuation of secured non-performing exposures and may develop guidelines to specify a common methodology, including possible minimum requirements for re-valuation in terms of timing and ad hoc methods, for the prudential valuation of eligible forms of funded and unfunded credit protection, in particular regarding assumptions pertaining to their recoverability and enforceability. Those guidelines may also include a common methodology for the determination of the secured part of a non-performing exposure, as referred to in paragraph 1.

Those guidelines shall be issued in accordance with Article 16 of Regulation (EU) No 1093/2010.

6. By way of derogation from paragraph 2, where an exposure has, between one year and two years following its classification as non-performing, been granted a forbearance measure, the factor applicable in accordance with paragraph 2 on the date on which the forbearance measure is granted shall be applicable for an additional period of one year.

By way of derogation from paragraph 3, where an exposure has, between two and six years following its classification as non-performing, been granted a forbearance measure, the factor applicable in accordance with paragraph 3 on the date on which the forbearance measure is granted shall be applicable for an additional period of one year.

This paragraph shall only apply in relation to the first forbearance measure that has been granted since the classification of the exposure as non-performing.';

(3) in the first sub-paragraph of Article 111(1), the introductory text is replaced by the following:

- '1. The exposure value of an asset item shall be its accounting value remaining after specific credit risk adjustments in accordance with Article 110, additional value adjustments in accordance with Articles 34 and 105, amounts deducted in accordance with point (m) Article 36(1) and other own funds reductions related to the asset item have been applied. The exposure value of an off-balance sheet item listed in Annex I shall be the following percentage of its nominal value after reduction of specific credit risk adjustments and amounts deducted in accordance with point (m) Article 36(1):';

(4) Article 127(1) is replaced by the following:

1. The unsecured part of any item where the obligor has defaulted in accordance with Article 178, or in the case of retail exposures, the unsecured part of any credit facility which has defaulted in accordance with Article 178 shall be assigned a risk weight of:
 - (a) 150 %, where the sum of specific credit risk adjustments and of the amounts deducted in accordance with point (m) Article 36(1) is less than 20 % of the unsecured part of the exposure value if those specific credit risk adjustments and deductions were not applied;
 - (b) 100 %, where the sum of the specific credit risk adjustments and of the amounts deducted in accordance with point (m) Article 36(1) is no less than 20 % of the unsecured part of the exposure value if those specific credit risk adjustments and deductions were not applied.';

- (5) Article 159 is replaced by the following:

'Article 159

Treatment of expected loss amounts

Institutions shall subtract the expected loss amounts calculated in accordance with Article 158(5), (6) and (10) from the general and specific credit risk adjustments in accordance with Article 110, additional value adjustments in accordance with Articles 34 and 105 and other own funds reductions related to those exposures except for the deductions made in accordance with point (m) Article 36(1). Discounts on balance sheet exposures purchased when in default in accordance with Article 166(1) shall be treated in the same manner as specific credit risk adjustments. Specific credit risk adjustments on exposures in default shall not be used to cover expected loss amounts on other exposures. Expected loss amounts for securitised exposures and general and specific credit risk adjustments related to those exposures shall not be included in that calculation.';

- (6) point (b) of Article 178(1) is replaced by the following:

'(b) the obligor is more than 90 days past due on any material credit obligation to the institution, the parent undertaking or any of its subsidiaries. Competent authorities may replace the 90 days with 180 days for exposures secured by residential property or SME commercial immovable property in the retail exposure class, as well as exposures to public sector entities. The 180 days shall not apply for the purposes of point (m) Article 36(1) or Article 127.';

(7) the following Article is inserted:

'Article 469a

Derogation from deductions from Common Equity Tier 1 items for non-performing exposures

By way of derogation from point (m) Article 36(1), institutions shall not deduct from Common Equity Tier 1 items the applicable amount of insufficient coverage for non-performing exposures where the exposure was originated prior to ... [the date of entry into force of this amending Regulation].

Where the terms and conditions of an exposure which was originated prior to ... [the date of entry into force of this amending Regulation] are modified by the institution in a way that increases the institution's exposure to the obligor, the exposure shall be considered as having been originated on the date when the modification applies and shall cease to be subject to the derogation provided for in the first subparagraph.'

Article 2

This Regulation shall enter into force on the day following that of its publication in the *Official Journal of the European Union*.

This Regulation shall be binding in its entirety and directly applicable in all Member States.

Done at ...,

For the European Parliament
The President

For the Council
The President
