



Council of the
European Union

016575/EU XXVIII. GP
Eingelangt am 03/04/25

Brussels, 3 April 2025
(OR. en)

Interinstitutional File:
2025/0077(COD)

7663/25
ADD 1 REV 1

EF 95
ECOFIN 380
CODEC 367

COVER NOTE

From:	Secretary-General of the European Commission, signed by Ms Martine DEPREZ, Director
To:	Ms Thérèse BLANCHET, Secretary-General of the Council of the European Union
No. Cion doc.:	SWD(2025) 77 final
Subject:	COMMISSION STAFF WORKING DOCUMENT Accompanying the document Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL amending Regulation (EU) No 575/2013 on prudential requirements for credit institutions as regards requirements for securities financing transactions under the net stable funding ratio

Delegations will find attached document SWD(2025) 77 final.



EUROPEAN
COMMISSION

Brussels, 31.3.2025
SWD(2025) 77 final

COMMISSION STAFF WORKING DOCUMENT
Accompanying the document

**Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE
COUNCIL**

**amending Regulation (EU) No 575/2013 on prudential requirements for credit
institutions as regards requirements for securities financing transactions under the net
stable funding ratio**

{COM(2025) 146 final}

Contents

1. INTRODUCTION: POLITICAL AND LEGAL CONTEXT	2
2. PROBLEM DEFINITION	3
2.1. What is the problem and what are the problem drivers?	3
2.1.1. Characteristics of the market and implications for EU competitiveness	3
2.1.2. Implications for financial stability and impacts on monetary policy	6
2.1.3. Transitional prudential treatment under the CRR	7
2.1.4. The European Banking Authority (EBA) report on the end of the transitional treatment	9
2.1.5. The NSFR requirement in third countries	10
2.1.6. Implications for banks active in the EU capital markets	11
2.1.7. Intermediation in the EU government debt market	12
2.1.8. Supporting diversification in the liquidity buffer of banks	12
2.1.9. Concerns raised by other stakeholders	13
2.2. How will the problems evolve?	14
3. OBJECTIVES: WHAT IS TO BE ACHIEVED?	14
3.1. General objectives	14
3.2. Specific objectives	15
4. WHAT ARE THE AVAILABLE POLICY OPTIONS?	16
4.1. What is the baseline on which options are assessed?	16
4.1.1. Volume impacted	17
4.1.2. Additional cost	18
4.2. Description and assessment of policy options	19
5. HOW DO THE DIFFERENT POLICY OPTIONS COMPARE?	21
6. PREFERRED POLICY OPTION	23
7. HOW WILL THE IMPACT BE MONITORED AND EVALUATED?	24

1. INTRODUCTION: POLITICAL AND LEGAL CONTEXT

In response to the 2008 Global Financial Crisis (GFC), the European Union (EU) substantially reformed the prudential framework applicable to banks in order to strengthen their resilience and help prevent a similar crisis from happening again. Those reforms were largely based on international standards that have been adopted since 2010 by the Basel Committee on Banking Supervision (BCBS) ¹. The standards are collectively known as the Basel III standards or the Basel III framework ². Basel III standards aim to ensure domestic and global financial stability, the level playing field for large internationally active banks, the proper functioning of international financial markets, and to support competitiveness and hence economic growth.

The EU prudential framework for banks, consisting of Regulation (EU) No 575/2013 ³ ('Capital Requirements Regulation' or 'CRR') and Directive 2013/36/EU ⁴ ('Capital Requirements Directive' or 'CRD IV'), among others implemented Basel III standards to all banks in the EU. Thanks to these reforms, the EU banking sector has become significantly more resilient to economic shocks. The EU banking sector has been able to withstand the shocks of the COVID-19 crisis, the September 2022 UK Gilt market crisis, and the March 2023 banking crisis.

The CRR lays down liquidity and funding requirements in EU legislation, as set out by the BCBS under the Basel III framework. The Net Stable Funding Ratio (NSFR) requirement aims to ensure that banks have sufficient stable funding sources to support their activities over a one-year horizon, avoiding excessive maturity mismatches between assets and liabilities and a too high reliance on short-term wholesale funding. As a complementary prudential metric to the NSFR, the Liquidity Coverage Ratio (LCR) promotes the short-term resilience of banks by ensuring they have an adequate stock of high-quality liquid assets that can be easily converted into cash to cover potential outflows under stress conditions.

In more detail, the CRR, as amended by Regulation (EU) 2019/876 ('CRR2') ⁵, specifies the NSFR as the ratio of an institution's amount of available stable funding (ASF) to its

¹ Members of the BCBS comprise central banks and bank supervisors from 29 jurisdictions worldwide. Among the EU Member States, Belgium, France, Germany, Italy, Luxembourg, the Netherlands, Spain and Sweden, as well as the European Central Bank are members of the BCBS. The European Commission and the European Banking Authority participate in BCBS meetings as observers.

² The consolidated Basel III framework is available at <https://www.bis.org/bcbs/publ/d462.htm>.

³ 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 (<https://eur-lex.europa.eu/eli/reg/2013/575/oj/eng>)

⁴ 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 (<https://eur-lex.europa.eu/eli/dir/2013/36/oj/eng>)

⁵ Regulation (EU) 2019/876 of the European Parliament and of the Council of 20 May 2019 amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements, and Regulation (EU) No 648/2012 (<https://eur-lex.europa.eu/eli/reg/2019/876/oj/eng>)

amount of required stable funding (RSF). The amount of ASF should be calculated by multiplying the institution's various liabilities by appropriate factors that reflect their degree of funding liquidity and thus availability for funding asset exposures. The amount of RSF should be calculated by multiplying the institution's assets and off-balance-sheet commitments by appropriate factors that reflect their liquidity characteristics and residual maturities. The NSFR requirement has been binding on EU banks since 28 June 2021.

The Commission's monitoring of NSFR implementation across jurisdictions shows that other major jurisdictions, notably the United States, the United Kingdom, Switzerland, Canada and Japan, are permanently deviating from the Basel NSFR standard as regards the prudential treatment that applies to securities financing transactions (SFTs) with a residual maturity of less than six months and collateralised by high quality assets. A level playing field is a core feature of the single market, not only in the way it governs economic interactions between Member States, but also for how the EU interacts with third countries. Given that the current treatment does not raise financial stability concerns and in the interest of ensuring an international level playing field, the Commission must act. This document provides a comprehensive overview of the problem, presents possible options to address it, and assesses the impact of the policy options. On the basis of these considerations, a preferred option is presented together with indicators to measure its implementation.

2. PROBLEM DEFINITION

2.1. What is the problem and what are the problem drivers?

2.1.1. Characteristics of the market and implications for EU competitiveness

SFTs are mostly interbank transactions with professional intermediaries. Banks accounted for 52% of SFTs exposures in September 2023. The concentration of the European SFTs market is significant. The first five institutions alone accounted for 49% of the total amount of SFTs exposures in September 2023, and the first 10 accounted for 64%⁶.

SFTs are mainly of very short-term maturity: in 2023, an average of 47% of principal amounts was initially agreed to have an overnight maturity, i.e. a transaction concluded on date T with a maturity date of T+1; in 2022, on average, 21% and 19% of principal amounts matured on the reporting date or the day after (T or T+1), respectively.

EU SFTs are predominantly concentrated in a few Member States, with France being the primary domicile holding 55% of EU borrowing in September 2023. Other counterparties are German (holding 17% of EU borrowing), Italian (7%) and Irish (5%). This concentration may be explained by the central role of Central Counterparty Clearing Houses (CCPs) (LCH, Euronext Clearing and EUREX Clearing) and banks domiciled in those Member States and acting as clearing members. Financial institutions concentrate their exposures in Member States where CCPs operate for more efficient risk management and clearing. CCPs contribute to 20% of SFTs, using SFTs in their cash

⁶ ESMA Market Report on the EU Securities Financing Transactions markets (reference ESMA50-524821-3147), published on 9 April 2024 (https://www.esma.europa.eu/sites/default/files/2024-04/ESMA50-524821-3147_EU_Securities_Financing_Transactions_markets_2024.pdf)

reinvestment strategy. The significant share held by CCP in the SFT market is linked to the progressive entry into application of Regulation (EU) No 648/2012⁷ that aims to reduce systemic counterparty and operational risk in financial systems and implements a central clearing obligation.

SFTs are, among others, used by broker-dealers to conduct market-making activities, ensuring the liquidity of sovereign debt. As a result, any potential change to NSFR requirements for SFTs would affect the management and market-making activity of sovereign debt issued by Member States, and in particular in those Member States where large amounts of sovereign debt are issued. There is a great diversity across Member States in the management and market-making activity of sovereign debt. Any potential change to NSFR requirements for SFTs would likely affect certain Member States more than others, i.e. those where large amounts of sovereign debt are issued (Italy, France, Germany, Spain, Belgium)⁸ and where prime-brokers and broker-dealers conduct market-making activities to ensure the liquidity of their sovereign debt, using SFTs.

More generally, SFTs are crucial tools for funding markets, enabling banks, dealers and investors to get funding for financing their trades. For instance, those willing to purchase securities in a leveraged trade, would pledge securities in a securities borrowing transaction and get the required funding by just committing a small fraction of their own capital funding⁹ to make the trade possible.

Since the 2008 GFC and the collapse of the interbank unsecured markets, SFTs play a major role in short-term funding between banks and market players through collateralised transactions. In the EU, the SFTs market is the largest segment of the money market denominated in euro, with an average daily trading volume of EUR 698 billion in 2021 and 2022 (i.e. 56% of the total EUR 1.3 trillion for the money market in euro) and more than EUR 2 trillion in outstanding amount (i.e. 30% of the total EUR 7 trillion for the money market in euro). The daily turnover more than doubled between 2011 and 2021, while in the same period the interbank unsecured segment shrank to one tenth of its former size.

Securities lending transactions generally involve long intermediation chains where collaterals are repeatedly lent out against cash. Thus, the receiver of collateral does not just hold it, but actively uses it for other purposes, by lending it on to other counterparties, or using it in another SFT, thus gaining additional income. As a result, securities lending transactions are generally rolled over when they mature. In all of this, banks have a central intermediation role.

Short-term SFTs with financial counterparties backed by very-High Quality Liquid Assets (Level 1 HQLA), such as sovereign bonds, as set out in Delegated Regulation

⁷ Regulation (EU) No 648/2012 of the European Parliament and of the Council of 4 July 2012 on OTC derivatives, central counterparties and trade repositories Text with EEA relevance (https://eur-lex.europa.eu/legal-content/EN/TXT/?toc=OJ%3AL%3A2012%3A201%3ATOC&uri=uriserv%3AOJ.L_.2012.201.01.0001.01.ENG)

⁸ ESMA Market Report on the EU Securities Financing Transactions markets (reference ESMA50-524821-3147), published on 9 April 2024 (https://www.esma.europa.eu/sites/default/files/2024-04/ESMA50-524821-3147_EU_Securities_Financing_Transactions_markets_2024.pdf)

⁹ That fraction corresponds to the portion of the pledged securities that is not recognised by the bank as collateral and that remains funded directly by the client.

(EU) 2015/61 supplementing Regulation (EU) No 575/2013¹⁰, represent the largest money market segment (87% of overall collateral of SFTs)¹¹. The European Central Bank (ECB) reports euro-denominated repurchase (repo) activity¹² of the largest euro area banks under the Money Market Statistical Reporting (MMSR) data. According to this data, cash lending repo transactions with financial counterparties, with maturities of less than six months, represent about EUR 450-600 billion of outstanding volumes. In addition, as explained in the ECB's 2022 Euro Money Market Study¹³, the SFTs market, in particular the repo market, plays a primary role in the transmission of monetary policy (see Section 2.1.2 for further details) and the repo and sovereign bond markets are tightly linked.

A report from the European Securities and Markets Authority (ESMA) on the EU SFTs market¹⁴, published in April 2024, shows that during 2023, in the case of EU transactions, EU sovereign bonds accounted for 65% of sovereign bonds used as collateral. In contrast, US Treasuries and UK Gilts accounted for an average sovereign bond collateral share of 22% and 8%, respectively.

SFTs activity is prone to international competition in wholesale markets¹⁵. In the EU, 59% of the SFTs amounts are with non-EU counterparties. Counterparties are often from the UK (12% of repo and 9% of reverse-repos, in September 2023). Counterparties from the US are also common (7% of repo and 5% of reverse-repos). Counterparties from other third countries account for 12% of repos and 15% of reverse-repos. Considering that 59% of SFTs amounts involve a non-EU counterparty and non-EU banks also have a material market share on primary dealing activities, a unilateral increase by the EU in the prudential charge that applies to funds due from SFTs, under the NSFR, could lead to a shift of this activity to non-EU banks that may operate from non-EU capital markets. A shift of SFTs to non-EU capital markets could impact the market making activity on EU sovereign debt and on other collateral, undermining the market liquidity of these assets and widening bid-ask spreads, with potential higher costs for market players. It will significantly and negatively affect the perspective to develop capital markets in the EU and increase the dependency of EU market players to non-EU banks and financial intermediaries.

The share of short-term SFTs with financial counterparties, backed by assets other than Level 1 HQLA (i.e. in practice other than sovereign debt), amounts to only around 3% of the outstanding volume. The non-Level 1 HQLA market segment is characterised not

¹⁰ Commission Delegated Regulation (EU) 2015/61 of 10 October 2014 to supplement Regulation (EU) No 575/2013 of the European Parliament and the Council with regard to liquidity coverage requirement for Credit Institutions (https://eur-lex.europa.eu/eli/reg_del/2015/61/oj/eng)

¹¹ ESMA Market Report on EU Securities Financing Transactions markets 2024 (reference ESMA50-524821-3147) (https://www.esma.europa.eu/sites/default/files/2024-04/ESMA50-524821-3147_EU_Securities_Financing_Transactions_markets_2024.pdf)

¹² Repurchase (repo) and reverse-repurchase (reverse-repo) transactions are the most prominent type of SFTs.

¹³ See Euro money market study 2022 (<https://www.ecb.europa.eu/pub/euromoneymarket/html/ecb.euromoneymarket202204.en.html>)

¹⁴ ESMA Market Report on the EU Securities Financing Transactions markets 2024 (reference ESMA50-524821-3147) published on 9 April 2024 (https://www.esma.europa.eu/sites/default/files/2024-04/ESMA50-524821-3147_EU_Securities_Financing_Transactions_markets_2024.pdf)

¹⁵ See Table MR-SFT.5 on "Repo borrowing and lending by jurisdiction domicile" of the ESMA Market Report on EU Securities Financing Transactions markets 2024 ([ESMA50-524821-3147 EU Securities Financing Transactions markets 2024](https://www.esma.europa.eu/sites/default/files/2024-04/ESMA50-524821-3147_EU_Securities_Financing_Transactions_markets_2024.pdf))

only by a lower overall volume and by higher margins but also by a diverse range of collateral types used.

SFTs and unsecured transactions

SFTs are an important segment as regards both the asset and liability side of bank balance sheets, and are thus relevant for the calculation of the NSFR. These wholesale financial transactions are defined under Article 4(1), point 139 of the CRR as encompassing different secured transaction types in which assets (collateral) are temporarily exchanged for cash: (i) repurchase (repos) and reverse-repurchase (reverse-repos), (ii) securities lending, (iii) buy-sell-back, and (iv) margin lending. Repos and reverse-repos make up the largest share of SFTs, accounting for 68% of the total, followed by securities lending (23%), buy-sell-back (8%), and margin lending (1%) (September 2023 data) ¹⁶.

A repo is a collateralised and generally short-term borrowing transaction (i.e. cash comes in, while collateral goes out). A reverse-repo is a collateralised lending transaction, reverse mirroring a repo transaction, where a bank (the lender) temporarily purchases securities or commodities (i.e. collateral) from a counterparty (the borrower) in exchange for cash (i.e. cash goes out, while collateral comes in), with a commitment to sell the collateral back in the future at a predetermined price.

Conversely, unsecured lending transactions are loans that are not secured by any collateral. They are based on the borrower's creditworthiness and promise to repay.

Since the GFC, there is very little unsecured interbank lending. By contrast, ever since, SFTs play a crucial role in the circulation of short-term funding between banks and market players through collateralised transactions.

SFT market activity also links the short-term money market to the longer-term capital market by serving as funding market instrument for the purchase of longer-dated financial instruments. The bulk of SFTs are collateralised by sovereign debt, where they are characterised as a high-volume, low-margin business activity for large banks. Importantly, SFTs are subject to significant international competition, also evidenced by the cross-border nature of many of these transactions. As profit margins in repo trading are low, even a small change in the regulatory treatment can have an impact on liquidity and traded volumes. Repo and sovereign bond markets are also tightly linked.

2.1.2. Implications for financial stability and impacts on monetary policy

The 2008 GFC highlighted that SFTs may trigger financial stability concerns due to a lack of transparency, excessive leverage, over-reliance on short-term funding, poor collateral quality, interconnectedness/contagion, and haircut procyclicality. Before its collapse, Lehman Brothers was funding approximately a quarter of its balance sheet with

¹⁶ ESMA Market Report on the EU securities financing transactions (SFT) markets (reference ESMA50-524821-3147), published on 9 April 2024 (https://www.esma.europa.eu/sites/default/files/2024-04/ESMA50-524821-3147_EU_Securities_Financing_Transactions_markets_2024.pdf).

overnight SFTs. A halt in SFTs trades was instrumental in causing its failure in 2008, prompting the launch of international reflections on setting up funding prudential risk metrics and requirements for banks.

To address this issue, the Basel standards were reformed to include liquidity requirements in the form of the NSFR and the LCR, which have contributed to making banks more resilient to liquidity risks, including to a potential disruption of the SFTs market ¹⁷.

The EU implemented these Basel requirements for liquidity and funding risks in the CRR. Further than the NSFR, other prudential requirements for banks aim to avoid excessive concentration risk on transactions with wholesale counterparties, in particular the large exposure framework and the additional liquidity monitoring metrics. The LCR is also more prone than the NSFR to capture the risk raised by short term transactions. Also, the asset encumbrance framework permits to have a clear view on assets, when used as collateral. Beyond micro-prudential measures, the prudential framework for banks empowers competent authorities to address macro-prudential and systemic risks with quantitative and qualitative measures.

In addition, Regulation (EU) 2015/2365 ¹⁸ (the ‘Securities Financing Transactions Regulation’ or ‘SFTR’) improved the transparency and monitoring of SFTs and the early identification of the risks inherent to these transactions, thereby strengthening the EU financial system.

Before the review of the prudential requirements for banks under the CRR with the introduction of the NSFR and of sound principles for SFTs under the SFTR, there were some episodes of worsening conditions. For instance, during the 2010–2012 euro area sovereign debt crisis, market liquidity deteriorated across all segments, and SFT rate volatility for Italian and Spanish collateral increased much more than in the German and French collateral segments. In December 2011 the ECB introduced Long-Term Refinancing Operations (LTROs) and other extraordinary measures to stabilize the banking system and ensure a smooth monetary policy transmission. As a result, liquidity returned to normal levels, and the dispersion of volatility across segments declined.

With the launch of ECB’s Public Sector Purchase Programme (PSPP) in March 2015, rate volatility increased, particularly for the German collateral segment, reflecting the scarcity of collateral and the strong link between the SFTs market and the market for collateral used in these transactions.

During the prolonged period of low interest rates, accommodative monetary policy provided ample central bank liquidity to the market. At the same time, central bank asset purchases and CCP collateral requirements reduced the quantity of high-quality collateral available in many Member States.

¹⁷ As mentioned in the introduction, those reforms enabled European banks to withstand the COVID-19 crisis, the September 2022 UK Gilt crisis and the March 2023 banking crisis, in a resilient way.

¹⁸ Regulation (EU) 2015/2365 of the European Parliament and of the Council of 25 November 2015 on transparency of securities financing transactions and of reuse and amending Regulation (EU) No 648/2012 (<https://eur-lex.europa.eu/eli/reg/2015/2365/oj/eng>)

As regards monetary policy, in a context of normalisation, SFTs and unsecured transactions are key capital market instruments. The gradual unwinding of central bank support through the quantitative tightening of monetary policy and the return of collateral to the market have already pushed many banks back into the SFTs market to obtain financing.

As monetary policy conditions have normalised, the importance of the SFTs market is set to increase in the coming years, supporting the redistribution of liquidity and collateral between banks and other market participants through secured transactions.

While less prominent since the 2008 GFC, unsecured funding transactions complement secured transactions to redistribute liquidity among financial intermediaries, to support capital markets liquidity and an adequate financing of the real economy.

2.1.3. Transitional prudential treatment under the CRR

The prudential treatment of short term SFTs is subject to a conservative approach under the Basel NSFR standard. It incorporates an asymmetric treatment between liabilities with a residual maturity of less than six months provided by financial customers and assets resulting from transactions with a residual maturity of less than six months, with financial customers. It is conservative because: (i) short term liabilities from financial customers are not recognised as a stable source of funding for the borrowing banks and (ii) a small share of short-term lending, in particular contractual inflows due from SFTs are considered to be long-term commitment for the lending bank, taking into account the frequent practice to prolong funding support to its clients (by rolling-over the loan), as it is expected that lending banks should contribute to maintaining an active SFTs market, at all times.

Under the Basel standard for the NSFR, when collateralised by Level 1 HQLA, such as sovereign bonds, a 10% RSF requirement applies to funds due from SFTs with financial counterparts and with a residual maturity of less than six months. This RSF requirement amounts to 15% when funds due from SFTs with a residual maturity of less than six months, with financial counterparts, are collateralised by assets other than Level 1 HQLA (i.e. not sovereign bonds). The RSF requirement of 15% also applies to funds due from the nowadays less used unsecured transactions, with financial clients, with a residual maturity of less than six months.

No available stable funding is recognised for borrowings with financial customers, with a residual maturity of less than six months, and hence under the NSFR a 0% ASF requirement applies to these transactions.

In its proposal amending the CRR, published on 23 November 2016¹⁹, the European Commission suggested a permanent use of lower RSF factors for short-term SFTs (5% if collateralised by Level 1 HQLA and 10% otherwise) and unsecured lending (10%) with

¹⁹ Proposal for a Regulation of the European Parliament and of the Council amending Regulation (EU) No 575/2013 as regards the leverage ratio, the net stable funding ratio, requirements for own funds and eligible liabilities, counterparty credit risk, market risk, exposures to central counterparties, exposures to collective investment undertakings, large exposures, reporting and disclosure requirements and amending Regulation (EU) No 648/2012 (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=COM%3A2016%3A0850%3AFIN>)

financial counterparties, than the ones set out in the Basel standard. The analysis supporting this proposal is available in the impact assessment accompanying it ²⁰. The Commission concluded at the time that ‘it seems reasonable to bring limited changes to the treatment of both short-term transactions with financial institutions, and of HQLA Level 1 [in order] not to hinder the good functioning of EU financial and repo markets’. The Commission also considered that the asymmetric treatment applicable to short-term SFTs could undermine the necessary market makers’ inventory management ²¹, which would contradict the objectives of efficient banking and capital markets. The arguments and analysis leading to this approach and the impact assessment accompanying the Commission 2016 proposal are still valid.

The co-legislators modified the Commission proposal and the final CRR2 provided for an even lower transitional RSF requirement of 0% - instead of the required 10% RSF set by the Basel standards for funds due from SFTs with maturities up to six months, when collateralised with Level 1 HQLA, such as sovereign debt. As a result, during the transitional phase lasting until 28 June 2025, no stable funding requirement applies to symmetrical securities borrowing and securities lending transactions with a residual maturity of less than six months when collateralised by Level 1 HQLA. This provision was however of transitional nature and is set to expire at the end of June 2025 when the calibration set out in the Basel standard (10% RSF) would start to apply to these transactions.

Similar transitional provisions were also agreed for funds due from SFTs collateralised by assets other than Level 1 HQLA with a residual maturity below six months, and for short-term unsecured transactions with financial customers. While very important for the market liquidity of other collateral than sovereign bonds, for the diversification of the liquidity buffer of banks and for the distribution of liquidity across the real economy, these exposures are nowadays relatively small in banks’ balance sheets compared to funds due from SFTs collateralised by Level 1 HQLA. The co-legislators agreed under the transitional phase lasting until 28 June 2025 to lower the RSF factors for funds due from SFTs collateralised by assets other than Level 1 HQLA from 15% to 5% and for short-term unsecured loans to financial counterparties from 15% to 10%. No ASF is recognised for the funding transactions, even with the same characteristics in terms of encumbered collateral and maturity.

These provisions aimed to give banks sufficient time to adapt to the more conservative requirement imposed by the Basel standards and to further assess and mitigate negative effects on the sovereign debt and capital markets.

The current requirements have proven to be prudentially sound since their entry into application in mid-2021 and have not raised financial stability concerns so far, including during recent stress episodes (March 2023 banking turmoil, UK Gilt crisis, Russian aggression) albeit these stress episodes did not reach the magnitude of the GFC or the

²⁰ Commission staff working document and impact assessment accompanying the proposal amending Regulation (EU) No 575/2013 on prudential requirements for credit institutions and investment firms (<https://eur-lex.europa.eu/legal-content/EN/TXT/?uri=SWD%3A2016%3A0377%3AFIN>)

²¹ To provide liquidity, market makers carry inventories and bear inventory risk. They manage their inventory risk by directly adjusting bid and ask prices to obtain the optimal level of inventory or by hedging against inventory risk. Both policies play an important role in determining asset prices and liquidity. Hedging the risk of holding undesired inventory is very important for market makers.

euro area sovereign debt crisis and took place in an environment of high excess liquidity. EU banks are characterised by significant NSFR buffers above their minimum requirements and their funding capacity is being supervised on a continuous basis.

Nevertheless, after 28 June 2025, the RSF requirements for SFTs with a residual maturity of less than six months and from short-term unsecured transactions with financial customers are set to go up, consistently with the Basel standard, while the ASF requirement for the symmetrical transactions, would remain at 0%.

2.1.4. The European Banking Authority (EBA) report on the end of the transitional treatment

Under Article 510(4), (6) and (9) of the CRR2, the EBA was mandated to evaluate the prudential treatment of several items under the NSFR framework. Under this mandate the EBA analysed the impact on the NSFR level of ending the transitional RSF requirements applicable to SFTs and unsecured funding transactions of less than six months, with financial counterparties.

The EBA report on specific aspects of the NSFR framework ²² (the ‘EBA report’), published on 16 January 2024, concludes that the end of the transitional treatment only will have a limited impact on the NSFR levels of EU banks.

The EBA report is based on qualitative analysis informed by expert judgement, supplemented by some materiality and sensitivity analyses using supervisory reporting data from more than 2 300 institutions, including both major and small/local institutions.

As of 30 June 2024, 1 695 banks had reported exposures to SFTs or from unsecured transactions of less than six months, with financial counterparties. The increase in the RSF factor would decrease the NSFR ratio of the banks concerned on average from 128.6% to 127.4% (-1.2pp), which is well above the minimum threshold of a 100% NSFR.

According to the EBA, banks’ management buffers for net stable funding can absorb the end of the transitional treatment, with very limited impacts on the NSFR ratio. The EBA concludes that changes to the current legislation are not necessary.

While the EBA report’s conclusions are a valuable contribution to assessing the implications of the end of the transitional treatment, the Commission considers that other factors should also be considered, as developed below.

²² The EBA publishes an analysis of specific aspects of the net stable funding ratio framework (<https://www.eba.europa.eu/sites/default/files/2024-01/8d7c0d40-2d79-4763-bd9c-ad66c0bf4076/Report%20on%20specific%20aspects%20of%20the%20NSFR%20framework%20under%20Art%20510%20CRR.pdf>)

2.1.5. The NSFR requirement in third countries

Maintaining a level playing field at international level is a key consideration for the Basel framework and the EU's implementation of it. The Basel NSFR standard was designed as a globally consistent regulatory requirement, aiming to foster convergence across jurisdictions and eliminate opportunities for cross-border regulatory arbitrage.

The Commission's monitoring of NSFR implementation across jurisdictions shows that other major jurisdictions, notably the United States, the United Kingdom, Switzerland, Canada and Japan, are permanently deviating from the Basel NSFR standard as regards the calibration of stable funding requirements applicable to SFTs with a residual maturity of less than six months and collateralised by high quality collateral.

The US agencies argue that 'the 0% RSF factor assignment was made based on the determination that Level 1 HQLA pose minimal liquidity risk and contribute importantly to the good functioning of short-term funding markets, i.e. that a non-zero RSF factor on Level 1 HQLA could discourage intermediation in US Treasury and repo markets' ²³.

The transitional treatment set by the CRR2 keeps the EU funding requirements aligned with other key jurisdictions. Maintaining this treatment will avoid any unilateral departure from the international consensus that may affect the level playing field for EU banks in an area which is particularly prone to international competition. In other words, if the EU followed the international standards, while major non-EU jurisdictions did not, the result could be an uneven international playing field with negative effect as regards the competitive situation of EU banks active in the SFTs market, that may impair the effective development and the well-functioning of capital markets in the EU, in particular on sovereign bonds. UK and US banks could have an undue competitive advantage in providing reverse repos to EU banks. (via EU CCPs or via the provision of direct banking services to EU banks from their home jurisdiction).

2.1.6. Implications for banks active in the EU capital markets

Banks have called on the Commission to maintain the transitional treatment and avoid increasing the RSF factor. They raised concerns about their need to maintain, after June 2025, the same level of NSFR management buffers. The end of the transitional treatment and the subsequent impact on the level of the NSFR could therefore oblige them to raise additional long-term stable funding on capital markets and to pass the funding charge increase to their clients.

According to regulatory common reporting (CoRep) data, for banks supervised in the EU at Q2-2024, the end of the transitional treatment on 28 June 2025 would result in a cumulative longer-term funding need of approximatively EUR 300 billion (0.9% of total EU banking assets), to offset the impact ²⁴. This estimate represents an upper limit to the

²³ See the July 2023 [BCBS assessment of Basel NSFR regulations - United States](#). To note that the US is deemed "largely compliant", despite the permanent deviation.

²⁴ EUR 179.4 billion, in case of an increase of the RSF from 0% to 10% for SFTs collateralised by Level 1 HQLA. EUR 84.2 billion, in case of an increase of the RSF from 5% to 15% for SFTs collateralised by

impact, as banks are likely to adjust their NSFR and the volume of their SFT business in response to increased RSF factors, thereby lowering the additional funding needs.

The magnitude of the impact varies across bank business models. Large EU corporate and investment banks would be more affected than local retail credit institutions. There would also be an impact on subsidiaries of non-EU banking groups based in the EU²⁵ and for subsidiaries of EU banking groups operating in non-EU countries, considering the risk profile of some of these institutions operating on wholesale transactions as primary dealers for governments bonds and as broker-dealers on capital markets.

Another concern raised by banks is a risk of SFTs activity shifting to non-EU countries that apply lower RSF factors than what the EU could apply after June 2025. For third country banking groups operating in the EU, SFTs are normally carried out by EU subsidiaries, which would be subject to the same NSFR requirements as the ones that apply to EU banking groups. However, third country banking groups might be able to shift those activities to EU branches or cross-border operations, and as such neutralise the increase in the RSF in the EU. This situation would, without specific EU action, lead to an uneven international playing field where non-EU banks may gain market share over EU banks.

Shifting activity to an entity based in a non-EU country could be a feasible option for a banking group which is not consolidated in the EU, to avoid higher regulatory costs. As a result, if RSF factors are raised in the EU but stay below the Basel requirement in some non-EU countries, banks from those countries could have a competitive advantage. In practice, the incentive to enter the market for third country banking groups will depend on how much EU banks pass on the increase in the prudential cost that is expected after June 2025 in the bid-ask spread.

It is important to recall that third country banking groups already have significant market shares in EU primary dealing markets.

2.1.7. Intermediation in the EU government debt market

Section 2.1.1. underlines that the SFTs market and the sovereign bonds market are interlinked. EU sovereign bonds account for 65% of sovereign bonds used as collateral.

An increase in the RSF level applicable to SFTs could discourage EU banks from intermediating in government debt and affect the liquidity in the collateral markets concerned. This could also lead to higher bid-ask spreads and an increase in funding costs for Member States in a period of normalised monetary policy when central banks are expected to reduce their market presence and private market players are expected to take over.

other assets (i.e. non-Level 1 HQLA). EUR 36.2 billion, in case of an increase of the RSF from 10% to 15% for unsecured financing transactions with financial counterparties.

²⁵ According to ad-hoc EBA analysis, under certain conditions, two subsidiaries of third-country banking groups may be particularly affected by the end of the transitional treatment.

2.1.8. Supporting diversification in the liquidity buffer of banks

The LCR aims to make sure banks have a buffer of liquid assets that can be easily transformed into cash through SFTs or by monetising liquid assets in a 30-day liquidity stress scenario. As such, SFTs are crucial capital market instruments for making the LCR prudential ratio work smoothly.

Maintaining the transitional treatment for funds due from SFTs collateralised by assets other than Level 1 HQLA (i.e. other than sovereign bonds) would also support the liquidity and diversity of assets that are also eligible for the liquidity buffer of banks under the LCR. As such, maintaining such a treatment would also contribute to mitigating the sovereign-bank nexus, through a better liquidity and an increased availability of collateral assets other than sovereign bonds. In consequence, it is useful to maintain the current prudential requirements for those assets as well.

An increase in the RSF factor for unsecured transactions would have a negligible impact on the NSFR levels on aggregate. This can be interpreted in two ways: On the one hand, it could allow banks to absorb the impact with small effects on their unsecured lending activities. On the other hand, it would not materially strengthen the prudential profile of banks²⁶, while it may disincentivise the use of unsecured funding transactions that may prove helpful in a period of monetary policy tightening. Indeed, a non-zero RSF factor already applies to short-term unsecured transactions under the NSFR. Keeping the RSF factor that applies since June 2021 to short-term unsecured transactions with financial customers will contribute to the use of these transactions in a context of monetary policy tightening, as a complement to SFTs to redistribute liquidity across market players. This would in turn support overall capital markets liquidity and ultimately an adequate financing of the real economy.

SFTs and unsecured transactions support monetary policy transmission and liquid and deep bond and collateral markets that are essential for the build-up and the efficiency of the liquid buffer of banks.

2.1.9. Concerns raised by other stakeholders

The Commission has conducted a call for evidence²⁷ between 10 February and 10 March 2025. 27 stakeholders²⁸ answered the call for evidence. The respondents are mostly bank associations (13) and banks (8), but other stakeholders (public authorities (1), non-bank associations (3) and private companies (2)) also contributed to share intelligence on the targeted amendment to the CRR envisaged by the European Commission for the

²⁶ The EBA publishes an analysis of specific aspects of the net stable funding ratio framework (<https://www.eba.europa.eu/sites/default/files/2024-01/8d7c0d40-2d79-4763-bd9c-ad66c0bf4076/Report%20on%20specific%20aspects%20of%20the%20NSFR%20framework%20under%20Art%20510%20CRR.pdf>)

²⁷ Net Stable Funding Ratio – prudential treatment of short-term securities financing transactions (amending regulation) (<https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/14518-Net-Stable-Funding-Ratio-prudential-treatment-of-short-term-securities-financing-transactions-amending-regulation-en>)

²⁸ Respondents from 11 Member States (Austria, Belgium, Denmark, France, Germany, Italy, Netherlands, Poland, Romania, Spain and Sweden) and from one third country (Switzerland).

prudential treatment of short term SFTs and unsecured transactions with financial counterparties under the NSFR. The ECB also published a staff response to the call for evidence on its website ²⁹.

Respondents broadly concur with the Commission's understanding of the situation and support the initiative to submit a targeted proposal to the co-legislators.

All respondents stress that the absence of a proposal will create an unequal prudential treatment for identical business activities in the EU and in third country jurisdictions, with detrimental impact on the EU market.

They call on the European Commission to submit a legislative proposal to the European Parliament and to the Council shortly after the call for evidence, for a swift adoption of the proposal. They ask to avoid a discontinuation in the current NSFR treatment, which would carry the risk of sudden and erratic changes in the prudential treatment of banks exposures to the transactions concerned, with impacts on short term liquidity markets and bonds markets in a context of growing government financing needs (green and digital transition, defence, etc.). Market players also underline that short term SFTs and unsecured transactions contribute to the smooth functioning of money markets and to the transmission of the monetary policy.

A majority of stakeholders ask to make the treatment permanent beyond 28 June 2025. In a scenario of a prolongation of the transitional treatment, some respondents support the perspective to mandate the EBA to deliver a recurrent report. Others do not see the benefit of the mandate for the EBA to deliver a regular monitoring report in addition to the ongoing supervision by competent authorities and the market monitoring by central banks. Few respondents suggest a time-limited extension of the transitional treatment. Legal certainty for market players and putting EU market players on an equal footing compared to their peers in third country major jurisdictions are important considerations for respondents that also underline the importance for the EU to build efficient banking and capital markets.

A couple of stakeholders also underline that maintaining the transitional treatment for SFTs and unsecured transactions under the NSFR will contribute to the competitiveness of the EU, that the European Commission is placing at the heart of its economic agenda.

Very few respondents suggest a wider review of the NSFR or of the CRR, more generally. It should be noted that going beyond the targeted nature of the proposal would impair the capacity to ensure its swift adoption.

2.2. How will the problems evolve?

The fact that other major jurisdictions have not implemented the Basel NSFR standard suggests that there could be negative effects associated with higher RSF factors for SFTs.

²⁹ ECB staff response to the European Commission's call for evidence on a targeted amendment to the prudential treatment of securities financing transactions under the net stable funding ratio. (https://www.ecb.europa.eu/press/letters/pdf/ecb.letter202503_treatmentSFTsNSFR~1a87de9de5.en.pdf)

SFTs are key transactions for the good functioning of the short-term funding markets and for the liquidity of the underlying assets used as collateral, in particular sovereign bonds.

A reduction in the liquidity of the EU capital markets could be a consequence of a unilateral increase by the EU of the funding charge being applied to transactions intermediated by EU banks. Third country institutions that already intermediate 59% of the amount of SFTs in the EU could profit from regulatory arbitrage and move part of their activity to non-EU markets if bid-ask spreads for transactions in the EU are negatively impacted by the increase in the prudential charge, while it will not be the case in non-EU markets. Non-EU banks may gain market share over the few EU banks active on this market, based on an unlevel international playing field.

More conservative RSF could lead to higher bid-ask spreads for EU sovereign bonds and other underlying collateral with implications for issuers and for securities inventory. The reduced attractiveness and liquidity of SFTs could negatively affect the liquidity of high-quality liquid assets eligible to the LCR liquidity buffer of EU banks.

The transmission of monetary policy to the real economy could be negatively affected since the attractiveness of SFTs and unsecured funding transactions would be reduced by the stricter RSF requirements for such transactions in a period of normalised monetary policy, when central banks are expected to reduce their market presence and private market players are expected to take over.

3. OBJECTIVES: WHAT IS TO BE ACHIEVED?

3.1. General objectives

This initiative has **two general objectives**.

1. Ensure an international level playing field for prudential requirements

The prudential requirements applicable in the EU since June 2021 have not raised supervisory concerns for banks, even in periods of stress. EU banks have built up strong NSFR buffers, beyond minimum requirements. EU banks are also subject to an ongoing supervision.

The decision made by other jurisdictions for a permanent symmetric treatment for SFTs collateralised by Level 1 HQLA poses minimal liquidity risk and contributes significantly to the good functioning of short-term funding markets.

A de facto level playing field is created by aligning with the treatment in third-country jurisdictions. Absent compelling reasons, the EU should not unilaterally tighten the prudential treatment for transactions that are subject to significant international competition. That being said, as for other jurisdictions, deviating from the Basel NSFR standard may impact the overall assessment of the EU's compliance with Basel NSFR standard. This will however depend on the materiality of the impact on the level of the NSFR, so a future adjustment of the compliance assessment remains uncertain. In any case the EU would remain aligned with the approach of other jurisdictions (de facto international level playing field).

2. **Avoid damaging the banking and capital markets in the EU**

The EU economy heavily relies on financing provided by the banking sector. While not materially strengthening the level of the NSFR buffer for EU banks, increasing the level of the RSF factor will increase the charge for funding due from SFTs and unsecured transactions and may undermine banks' market-making activities.

SFTs play a crucial role in funding markets, linking the short-term money market to the longer-term capital market. The SFTs market could become less active and liquid because of higher RSF factors. This could have repercussions for several asset classes due to the crucial nature of SFTs markets in funding many types of collateral purchases and in transmitting monetary policy to the real economy.

The impact assessment accompanying the draft CRR2 already stated that 'the vast majority of respondents to the call for evidence and the NSFR targeted consultation expressed concerns on this asymmetry that could be very detrimental to market making activities and, as a consequence, to the liquidity of repo market and of the underlying collateral. Repo markets are presented as essential for the smooth functioning of both banks' liquidity management and market makers' inventory management. This treatment also raises some concerns regarding the impact on the interbank markets, in particular for liquidity management purposes. It may then affect the liquidity of interbank markets, of the securities (including sovereign bonds) and undermine market-making activities.' These arguments remain valid.

3.2. Specific objectives

The two general objectives pursued by this initiative can be broken down into the **four specific objectives** described below.

1. Prevent regulatory arbitrage risk in a very competitive market

To maintain consistency and prevent regulatory arbitrage risk in the very competitive and cross-border SFTs market, the Commission proposes to maintain the current prudential treatment applicable in the EU. This approach is in line with the one retained and applied in other major jurisdictions.

This alignment with how the Basel standard requirements are implemented in major third countries does not prevent raising the point in international fora on the differences between the calibration internationally agreed in the Basel standard and its actual implementation, in particular when applicable to cross-border competitive transactions.

2. Make the NSFR treatment for SFTs consistent with other prudential requirements for banks

SFTs support the swift and orderly transformation of collateral into cash. A damaged SFTs market could negatively affect the effectiveness of the LCR, another prudential liquidity requirement for banks. The LCR aims to make sure banks have a buffer of

liquid assets that can be easily transformed into cash through SFTs or by monetising liquid assets in a 30-day liquidity stress scenario.

3. Avoid increasing the bid-ask spreads for EU sovereign bonds

Increasing the NSFR funding charge applicable to short term SFTs when collateralised by Level 1 HQLA, such as sovereign bonds, could impact the price banks offer for short-term SFTs with such collateral and reduce the liquidity of sovereign bond markets.

4. Make banks operate on liquid markets with a diversity of collateral assets

Maintaining the transitional RSF treatment for short-term SFTs collateralised by assets other than sovereign bonds supports diversification in banks' liquidity buffers, contributes not to increase the pressure on scarce very high-quality collateral such as government bonds, and helps mitigate the sovereign-bank nexus.

Maintaining the current RSF prudential charge for short-term unsecured transactions with financial counterparts supports the use of unsecured funding transactions as a necessary complement to secured funding transactions such as SFTs, to support overall market liquidity and monetary policy transmission, in particular during periods of monetary policy tightening when central banks are expected to reduce their market presence and private market players are expected to take over.

4. WHAT ARE THE AVAILABLE POLICY OPTIONS?

4.1. What is the baseline on which options are assessed?

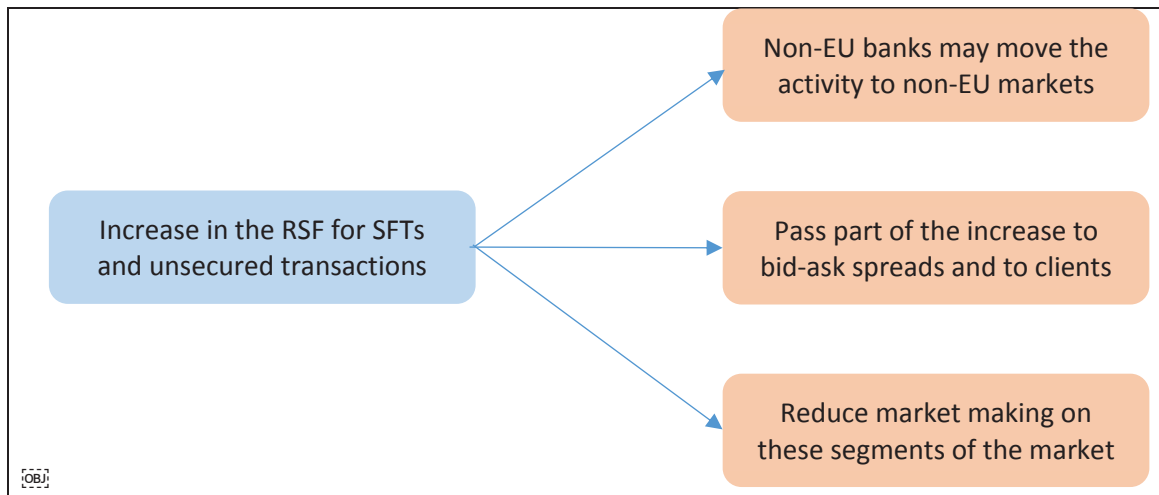
The baseline option assumes no legislative change to the prudential framework applicable at EU level.

Under this option, the RSF funding charge would increase after 28 June 2025, as specified under Article 510(8) of the CRR2. The RSF for SFTs collateralised by Level 1 HQLA, by other assets, and for unsecured transactions with a residual maturity of less than six months, with financial customers, will increase from 0%, 5% and 10% to 10%, 15% and 15%, respectively.

Figure 1 presents, under the baseline option, the potential adjustments in bank behaviour³⁰ to an increase of the prudential charge for SFTs and unsecured transactions, with a residual maturity of less than six months, with financial counterparts. These stylised actions are not mutually exclusive, and the aggregated outcome will likely encompass a combination of the potential adjustments.

Figure 1 – Stylised bank reaction to an increase in RSF requirement

³⁰ A reduced NSFR level is the mechanic implication of an increase in the RSF for the transactions concerned. Allowing a reduced NSFR level would be another option for banks, but banks argue that they will have to defend and uphold their NSFR levels due to investor and supervisory expectations.



The extent to which a bank will maintain its NSFR buffer level or will be able to pass on the cost of doing so in its internal cost-transfer pricing model, will depend on an individual bank's NSFR level, its internal target for the NSFR, its business model and its associated market positioning, as well as on potential dynamic behavioural effects from other banks. Some banks underline that they have to defend their existing NSFR levels due to supervisory or investor expectations.

The Common Reporting (CoRep) templates to monitor banks exposures may need to be amended to capture the new RSF requirements that will apply beyond 28 June 2025.

4.1.1. Volume impacted

In terms of impact on additional long term funding needs, there is a variety of estimates from market participants, ranging from EUR 80 billion ³¹ to EUR 246 billion ³². These figures correspond to 0.24% and 0.74% of total EU banking assets.

Based on the ECB's Money Market Statistical Reporting, which records the euro denominated SFTs activity of the largest euro area banks, the euro denominated SFTs market is approaching EUR 600 billion ³³ of SFTs to financial counterparties, with government bonds and a maturity of less than six months, as of Q2-2024. Applying to these transactions the changes specified in Article 510(8) of the CRR2 (i.e. increase of the RSF factor from 0% to 10%) would result in an additional requirement of EUR 60 billion in long term stable funding. In addition, 3% to 6% ³⁴ of the outstanding volume reported in MMSR would be categorised as short-term SFTs with financial counterparties backed by non-Level 1 HQLA. For these transactions the RSF factor

³¹ Association for Financial Markets in Europe, „CRD 5: The Net Stable Funding Ratio“, March 2017 (<https://www.afme.eu/portals/0/globalassets/downloads/briefing-notes/2017/afme-prd-nsfr-non-technical-paper.pdf>)

³² International Capital Market Association (ICMA), „NSFR and Reverse Repo“, May 2024 (https://www.icmagroup.org/assets/ICMA-ERCC_BN_NSFR-and-reverse-repo_May-2024_Final.pdf)

³³ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

³⁴ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

would increase from 5% to 15%, prompting an additional EUR 25 billion ³⁵ in stable funding.

According to regulatory common reporting (CoRep) data ³⁶, for all banks supervised in the EU at Q2-2024, the end of the transitional treatment on 28 June 2025 would, all else equal, result in a cumulative funding need of approximately EUR 300 billion ³⁷, to fully offset the impact.

There are limits to the reliability of the above estimates as estimates typically do not account for the netting of repos and reverse repos to the same counterparty and matching maturities.

4.1.2. Additional cost

Focusing on SFTs collateralised by Level 1 HQLA, the likely pass-through of the costs related to the introduction of non-neutral RSF factor may result in a higher bid-ask spread. Based on ECB estimations, assuming a full pass-through of the 10% increase in the RSF factor for the SFTs affected indicate a range of price increases between 2 and 10 basis points (bps) ³⁸. Estimates lie between a lower-bound of 3 bps to an upper bound of 9 bps, which represents a material increase considering the high-volume, low-margin nature of the business activity with currently persisting bid-ask spreads of 1 to 3 bps ³⁹. This increase in the prudential charge could hence have repercussions on transactions collateralised by sovereign bonds, but also more generally on primary and secondary markets for government bonds. Other asset classes and activities may also be impacted due to the interconnected nature of SFTs markets with sovereign bonds and other collateral markets (bond trading, bond futures, short selling of bonds).

Similarly, after end-June 2025, the RSF for SFTs backed by assets other than Level 1 HQLA will go up from 5% to 15%. This may lead to a further increase of the cost for transactions, ranging between 4 bps to 8 bps ⁴⁰ depending on the degree of compensation by banks (i.e. the extent to which it would be passed-through). This cost increase may affect all market participants on collateral markets considering the diversity of assets used in these transactions.

That being said, the degree to which regulatory costs are passed on is very hard to estimate, especially as most market maker banks still operate well above the NSFR minimum requirement and above their internal target levels. If banks chose to operate

³⁵ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

³⁶ EBA data based on Common Reporting (CoRep) - European Union area perimeter

³⁷ EUR 179.4 billion, in case of an increase of the RSF from 0% to 10% for monies due from SFTs collateralised by Level 1 HQLA. EUR 84.2 billion, in case of an increase of the RSF from 5% to 15% for monies due from SFTs collateralised by other assets (i.e. non-Level 1 HQLA). EUR 36.2 billion, in case of an increase of the RSF from 10% to 15% for unsecured financing transactions with financial counterparties.

³⁸ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

³⁹ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

⁴⁰ Commission evaluation based on ECB data.

with a lower buffer above the NSFR requirement (and their internal target levels), the estimated pricing impact on affected reverse repo transactions could be limited.

These additional costs would come with no significant benefit in terms of financial stability enhancement. Under the transitional treatment there were no significant prudential concerns, despite significant shocks (Covid-19, 2023 banking turmoil).

In light of the above, allowing the transitional measure to elapse is not considered as a preferred policy option, while acknowledging the potential trade-offs for financial stability and the EU's Basel compliance. Two alternative options are therefore considered and compared below for maintaining the current NSFR treatment for short-term SFTs and unsecured transactions with financial customers. A distinction between both options is introduced as to the nature of transactions concerned.

4.2. Description and assessment of policy options

Option 1 - Maintain the transitional treatment for SFTs collateralised by Level 1 HQLA

This option would maintain the NSFR transitional treatment for SFTs collateralised by Level 1 HQLA such as sovereign bonds, with a residual maturity of less than six months, with financial customers, also beyond end-June 2025. For SFTs collateralised by other assets and for unsecured transactions the transitional treatment would end after 28 June 2025.

This option would make the stable funding requirement for the transactions concerned consistent and comparable with the one applied in other major jurisdictions such as the United States, the United Kingdom, Switzerland and Japan. It would also prevent the sovereign debt market from experiencing a potential increase in the prudential charge applicable to debt issued by EU Member States and to NextGenerationEU bonds.

This option would reduce the risk of regulatory arbitrage in this very competitive and cross-border activity, with a limited impact on the level of the NSFR requirement applicable to banks, in the EU.

Maintaining the transitional treatment without expiry date will give clarity and legal certainty to banks and other market participants. This will also be consistent with the approach retained in other major jurisdictions.

Under this option, banks may not have to further increase their liquidity buffer under the NSFR and might be more vulnerable to liquidity shocks. At the same time, EU banks are already characterised by significant NSFR buffers, above the minimum threshold of a 100% NSFR. The costs in terms of financial stability risks do not appear significant.

In terms of benefits, banks could rely on more short-term funding (between EUR 60 billion ⁴¹ and EUR 246 billion ⁴², corresponding to 0.24% and 0.74% of total EU banking

⁴¹ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

⁴² International Capital Market Association (ICMA), „NSFR and Reverse Repo“, May 2024 (https://www.icmagroup.org/assets/ICMA-ERCC_BN_NSFR-and-reverse-repo_May-2024_Final.pdf)

assets) lowering their funding costs and supporting SFT market liquidity instead of having to rely on more stable funding sources. Banks, market participants on sovereign debt markets and Member States will be preserved from an increase of the bid-ask spread on short-term SFTs backed by Level 1 HQLA such as sovereign bonds.

Under this option, the EBA will be mandated to assess and report regularly on the implications of maintaining the transitional treatment. This report that could be part of the proposal would enable the Commission to draw up a legislative proposal to amend the prudential treatment, if deemed useful. This will come in addition to the monitoring of capital market developments by central banks and to the ongoing supervision by competent authorities.

However, under this option, an increase in stable funding would still be introduced for short term SFTs with non-Level 1 HQLA collateral and for short term unsecured transactions. The additional funding need may span from EUR 25 billion ⁴³ to EUR 84 billion ⁴⁴ (0.08% to 0.25% of total EU banking assets) in case of an increase of the RSF from 5% to 15% for monies due from SFTs collateralised by assets other Level 1 HQLA. It may reach EUR 36.2 billion ⁴⁵, in case of an increase of the RSF from 10% to 15% for short-term unsecured transactions with financial counterparties.

This increase would likely affect the liquidity of the underlying collateral markets and reinforce the incentives towards sovereign bonds holdings, thereby undermining the diversification of liquidity buffer held by banks.

Option 2 - Maintain the transitional treatment for all SFTs and unsecured transactions with a residual maturity of less than six months with financial customers

This option will not only prolong the NSFR transitional treatment proposed under option 1 for SFTs collateralised by Level 1 HQLA, but also maintain the current RSF prudential charge for SFTs collateralised by other assets (5%) and for unsecured transactions (10%) with no material impact on the level of the NSFR buffer for EU banks.

Under this option, the cost would be the absence of higher NSFR prudential buffers due to more comprehensive RSF factors not only for SFTs collateralised by Level 1 HQLA, but also for SFTs collateralised by other assets and unsecured transactions, and a gap between the standard internationally agreed and the one applied in the EU. In other words, banks could rely on additional EUR 300 billion ⁴⁶

(0.9% of EU banking assets) of short-term funding compared to the baseline scenario, lowering their funding costs and supporting market liquidity. Beyond the benefits mentioned for option 1, market participants in all capital markets, and not only those on sovereign bond markets, will be preserved from an increase of the bid-ask spread on short term SFTs and unsecured transactions. Option 2 will maintain consistency in the steps (i.e. difference in the prudential charge) between the RSF factors that apply to

⁴³ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

⁴⁴ EBA data based on Common Reporting (CoRep) - European Union area perimeter

⁴⁵ EBA data based on Common Reporting (CoRep) - European Union area perimeter

⁴⁶ EBA data based on Common Reporting (CoRep) - European Union area perimeter

monies due from SFTs collateralised by sovereign bonds and monies due from SFTs collateralised by other assets. It will permit to mitigate the pressure on (scarce) high quality collateral. These would represent higher benefits than under option 1.

Extending the perimeter to SFTs collateralised by assets other than Level 1 HQLA will support the liquidity and diversity of assets that are also eligible to the liquidity buffer of banks under the LCR. It seems appropriate not to disconnect the two dimensions of the liquidity requirements that pursue complementary objectives.

Option 2 will permit to maintain the (10%) RSF for unsecured transactions that may prove helpful for market transactions as a complement to secured transactions such as SFTs, in a period of change in the monetary policy when private market players are expected to increase their market presence.

5. HOW DO THE DIFFERENT POLICY OPTIONS COMPARE?

Option 1 would address the primary concern surrounding the end of the transitional treatment applicable to SFTs of less than six months when collateralised by Level 1 HQLA. It would target low-margin high-volume transactions for banks and prevent an increase in the funding charge for EU sovereign debt. This will ensure that the EU's treatment is consistent and comparable with that of other major jurisdictions. This will preserve the EU from the risk of regulatory arbitrage on the sovereign debt collateral market. The steady state nature of this option will also give clarity to market participants on the prudential requirement that will apply to this activity. The continuation of the transitional treatment from 29 June 2025 onwards will ensure continuity and no erratic changes will be enacted to the prudential charge, which would otherwise adversely affect the liquidity of the market.

Under this option, the increase of the prudential charge for SFTs collateralised by other assets may impair the effective liquidity of assets other than sovereign bonds in the EU capital markets and the diversity of collateral eligible for the liquidity buffer of banks. The increase in the prudential charge for SFTs collateralised by other assets and unsecured transactions may also impair the attractiveness of these transactions for market participants and the effective transmission of the monetary policy to the real economy through short-term markets. The market monitoring by central banks and the ongoing banking supervision by competent authorities will contribute to the constant screening of stakeholders' practices and as safety layer against potential future financial stability concerns due to the absence of further increase of the NSFR prudential charge for the concerned transactions.

Option 2 proposes maintaining the transitional treatment for monies due from SFTs collateralised by Level 1 HQLA (as for option 1), but also for SFTs collateralised by other assets and for unsecured transactions with a residual maturity of less than six months, with financial counterparties.

This option will prevent the EU from the risk of regulatory arbitrage on transactions collateralised by sovereign debt, that represent the bulk of SFTs. Considering that option 2 covers a broader range of transactions and collateral than option 1, this option will further prevent the EU capital markets and market participants from an increase in the prudential cost for all the transactions concerned.

Similarly to option 1, this option will contribute to avoid an increase in the prudential charge for transactions with sovereign bonds collateral.

This option would further contribute to supporting an orderly transformation of collateral into cash, which is in line with the prudential requirements of the LCR.

Option 2 will also further support the development and sustainability of capital markets and liquidity for collateral assets in the EU, as it will not only cover Level 1 HQLA such as sovereign bonds, but also other collateral assets. As such, option 2 will further support the liquidity of a diversity of collateral assets in the EU capital markets.

In terms of efficiency, the cost of option 2 and option 1 in terms absence of higher NSFR prudential charge for the concerned transactions and gap between the standard internationally agreed and the one effectively applied in the EU are comparable.

In terms of effectiveness, option 2 will permit to provide further long-term funding to the real economy (EUR 300 billion ⁴⁷) than option 1 (between EUR 60 billion ⁴⁸ and EUR 246 billion ⁴⁹). It will also make the liquidity of the LCR ratio more efficient, with lower bid-ask spreads.

Moreover, compared to option 1, option 2 would help to better achieve diversification of banks' liquidity buffers and risk profile, but also contribute to mitigate the sovereign-bank nexus.

Comparative presentation of the effectiveness of Option 1 and Option 2.

	Option 1	Option 2
Prevent regulatory arbitrage risk in a very competitive market	Summary: + + (Preserve from a unilateral increase of the prudential charge for SFTs collateralised by sovereign bonds)	Summary: ++ + (Preserve from a unilateral increase of the prudential charge for SFTs collateralised by sovereign bonds) + (further support the development and sustainability of capital

⁴⁷ EBA data based on Common Reporting (CoRep) - European Union area perimeter

⁴⁸ ECB data based on Money Market Statistical Reporting - Banking Union area perimeter

⁴⁹ International Capital Market Association (ICMA), „NSFR and Reverse Repo“, May 2024 (https://www.icmagroup.org/assets/ICMA-ERCC_BN_NSFR-and-reverse-repo_May-2024_Final.pdf)

		markets and liquidity for collateral assets in the EU)
Make the NSFR treatment for SFTs consistent with other prudential requirements for banks	Summary: + + (Support the transformation of collateral into cash, by banks)	Summary: ++ + (Support the transformation of collateral into cash, by banks) + (Support diversification of banks' liquidity risk profile)
Avoid increasing the bid-ask spreads for EU sovereign bonds	Summary: + + (Preserve from an increase of the prudential charge for SFTs collateralised by sovereign bonds that are low-margin high-volume transactions)	Summary: + + (Preserve from an increase of the prudential charge for SFTs collateralised by sovereign bonds that are low-margin high-volume transactions)
Make banks operate on liquid markets with a diversity of collateral assets	Summary: - - (Targets transactions on sovereign bonds)	Summary: + + (Support transactions secured by a diversity of collateral assets and unsecured transactions)

Legend: ++ = Positive + = Slightly positive effect 0 = no effect - = Slightly negative

6. PREFERRED POLICY OPTION

In terms of effectiveness, the preferred policy option (**option 2**) would ensure a consistent RSF funding charge to SFTs with a residual maturity of less than six months in the EU and in other major jurisdictions, supporting the contribution of banks to a smooth functioning of the EU SFTs and sovereign bond markets. It would support the international attractiveness of EU capital markets, which is consistent with other Commission initiatives.

This option will also support an orderly transformation of securities into cash for the purpose of the LCR prudential ratio and a diversification in banks' liquidity buffer and securities inventories.

Moreover, the preferred policy option will reduce to a greater extent than option 1 the additional long-term funding needs for banks, estimated between EUR 60 billion ⁵⁰ and EUR 300 billion ⁵¹ (see section “4.1.1. Volume impacted” for further details), with a subsequent impact on the bid-ask spread for market transactions that may adversely affect all market participants (see section “4.1.2. Additional cost” for further details). The calibration of the NSFR and the LCR prudential ratios, making banks resilient to liquidity risk, will remain almost unchanged.

Option 2 will also avoid a potential increase in Member States’ funding charge for issuing sovereign debt. This will mitigate the risk of a potential reduction in the liquidity of sovereign debt markets in a context of tightening monetary policy.

In terms of effectiveness, option 2 will permit to provide further long-term funding to the real economy.

In terms of consistency, it will further support the liquidity of the LCR buffer, with lower bid-ask spreads, on a larger perimeter of transactions.

The preferred policy option will give legal certainty to market players on the prudential treatment for the transactions concerned, which will continue to be reported and disclosed by banks. Meanwhile, the relevant authorities will retain their supervisory power to address any specific prudential concern.

The preferred option will have no impact on capital requirements for banks, compared to the current treatment.

Option 2 presents benefit for the transmission of monetary policy to the real economy, the smooth functioning of EU capital markets and the diversification in banks’ liquidity risk profile.

7. HOW WILL THE IMPACT BE MONITORED AND EVALUATED?

Beyond the regular capital market monitoring, supervisory reviews, stress testing exercises and data collection carried out by central banks and supervisory authorities, including at EU level, the proposal sets out that the EBA will also monitor the effects of the amendments on banks’ NSFR and the liquidity of the underlying collateral markets every five years. This would allow detecting any financial stability concern or unexpected cost of these measures and react as needed.

The development of the periodic monitoring report should not introduce an additional reporting burden on EU banks as it could rely on available market intelligence and existing supervisory reporting requirements (e.g. Common Reporting (CoRep) templates C80.00, C81.00 and C84.00).

⁵⁰ ECB data based on Money Market Statistical Reporting on the perimeter of the Banking Union area

⁵¹ EBA data based on Common Reporting (CoRep) - European Union area perimeter

If the transitional NSFR requirements are maintained beyond 28 June 2025, no amendment to the Common Reporting (CoRep) templates appears necessary.