New banking package

CRD VI and CRR III

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1. Background

On 19 June 2024, the final texts of two key pieces of legislation for the European banking sector were published in the Official Journal of the European Union (“**EU**”). These are part of the banking package presented by the European Commission in 2021:

a) **Directive 2024/1619 of the European Parliament and of the Council of 31 May 2024,** which amends 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. This is known as the Capital Requirements Directive (“**CRD**”). Directive 2024/1619 deals with supervisory powers, sanctions, third-country branches, and environmental, social and governance risks (“**CRD VI**” or the “**Directive**”); and

b) **Regulation (EU) 2024/1623 of the European Parliament and of the Council of 31 May 2024**, which amends Regulation (EU) 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms. This is known as the Capital Requirements Regulation (“**CRR**”). Regulation (EU) 2024/1623 deals with requirements for credit risk, credit valuation adjustment risk, operational risk, market risk and the output floor (“**CRR III**” or the “**Regulation**”).

Underlying this banking package were three main guidelines aimed at making institutions more resilient to possible systemic shocks: (i) completing the implementation of the Basel III reforms agreed by the Basel Committee on Banking Supervision (“BCBS”) in 2017, (ii) sustainability and contributing to a green transition, and (iii) strengthening the supervisory powers of competent authorities.

2. The key changes in CRD VI

2.1. ESTABLISHMENT OF BRANCHES FOR THE PROVISION OF BANKING SERVICES BY THIRD-COUNTRY ENTITIES

As noted by the European Commission in its proposal[1], since Brexit, there has been no consistent approach in the EU to third-country banking groups operating in the EU. Third-country branches are subject to separate prudential requirements and this situation has potential to jeopardise the financial stability of the EU. In this respect, the European Commission underlines that, according to the European Banking Authority (“**EBA**”), the 15 largest third-country banking groups have a significant presence in EU banking markets and more than three quarters of their assets in the EU are held through third-country branches.

In addition, there are no integrated supervisory mechanisms that allow for the exchange of information between competent authorities supervising branches and subsidiaries of the same group. This creates inherent risks for market integrity in the EU.

New regulatory framework: Third-country banks must now have a physical presence in a Member State in order to start or continue providing banking services.

1 Available here

To address this, a **new regulatory framework has been introduced in Title VI of the CRD**. This covers everything from authorisation requirements to minimum prudential requirements for capital adequacy, liquidity, internal governance and risk management. It also sets out reporting requirements and the supervisory powers of Member States.

Most importantly, **third-country banks must now have a physical presence in a Member State** in order to start or continue providing the services listed in points 1, 2 and 6 of Annex I to the CRD (i.e. taking deposits, granting loans or providing guarantees) in that Member State, under the conditions set out in the new Article 47(1) of CRD VI. In addition, an authorisation is required in order to be regulated and supervised in the EU (Article 21c of CRD VI).

However, this requirement is subject to the following exceptions:

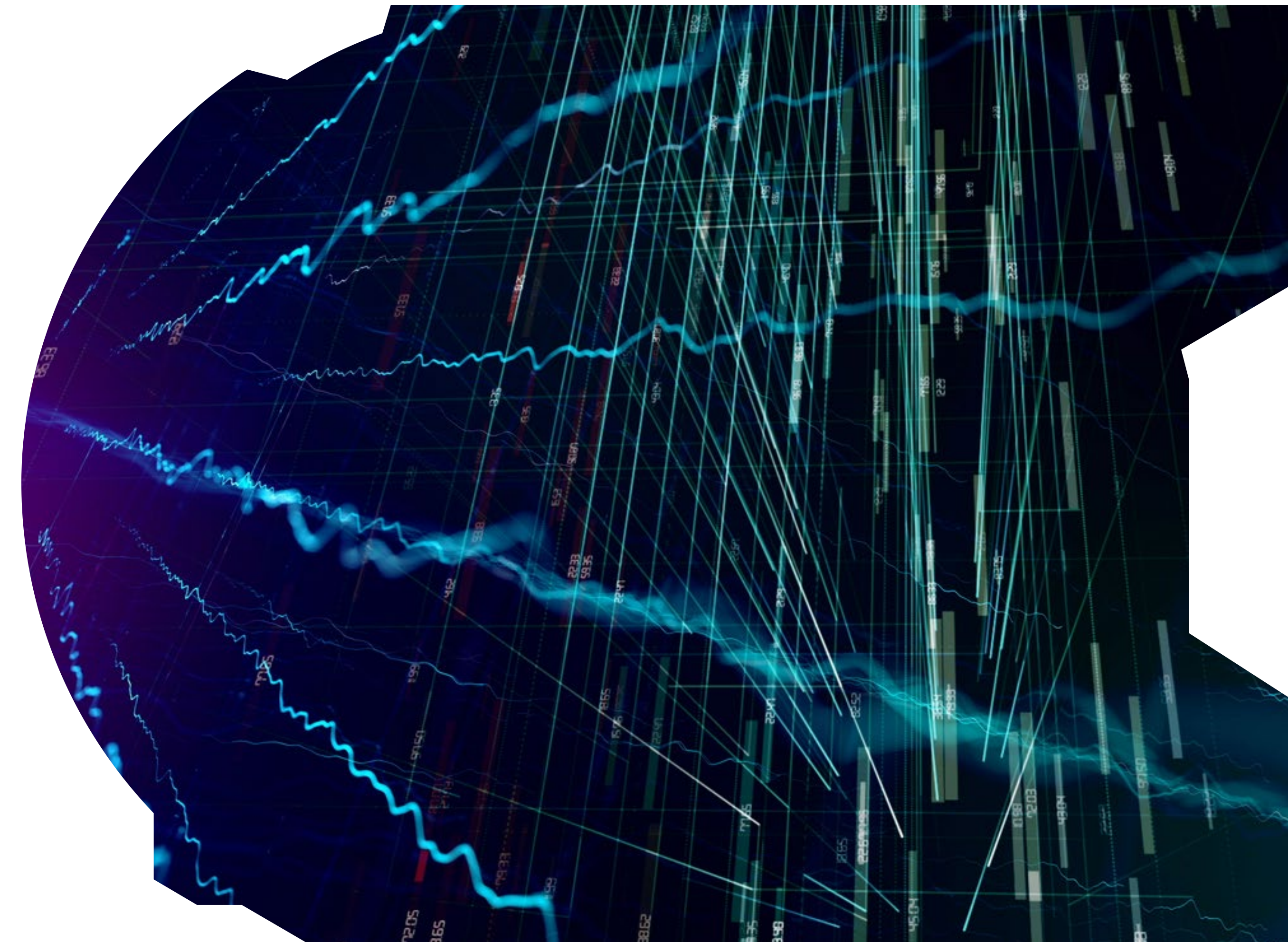
a) It does not apply to cases of **provision of services on the sole initiative of the client** ("reverse solicitation"), which are covered by Articles 21c(2) and 47(1) of CRD VI. In other words, a firm established in a third country may provide a service or activity covered by points 1, 2 and 6 of Annex I to the CRD (i.e. taking deposits, granting loans or providing guarantees) on the sole initiative of a retail client, an eligible counterparty or a professional client within the meaning of Annex II, Sections I and II of Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments ("**MIFID**"), established or resident in the EU. In this case, there is no need to establish a branch in that country;

b) It does not apply when the firm established in a third country provides a service or activity to a client or counterparty established or located in the EU which is a credit institution or **an entity belonging to the same group as the firm established in a third country**;

c) It does not apply to the services or activities listed in Annex I, Section A of the MiFID, including any ancillary services.

Furthermore, this new framework should be applied without prejudice to the discretion currently enjoyed by Member States to require, as a general rule, that companies from certain third countries carry out banking activities in their territory only through subsidiaries authorised under Title III, Chapter 1 of the CRD. This applies, for example, to cases where third countries apply banking supervision and prudential standards that are not equivalent to those laid down in the Member State's national legislation. It also applies to third countries that have strategic deficiencies in their AML/CFT legislation (Article 48i of CRD VI). Article 48i of CRD VI).

The minimum conditions for the authorisation of branches in third countries are described in the new Article 48c. It provides that the competent authorities may decide that authorisations granted until 10 January 2027 will remain valid, provided the third-country branches to which these authorisations were granted comply with the minimum requirements laid down.



Finally, CRD VI (Article 48a of CRD VI) introduces proportionality in the minimum requirements imposed on branches in third countries in relation to the risk they pose to the financial stability and integrity of the EU market by creating different classes of branches. They should be in class 1 if they are considered to pose a higher risk, or otherwise in class 2 if they are considered to be small and non-complex and do not pose a significant risk to financial stability. This is defined in Article 4(145)(1) of the CRR. For example, branches in third countries with assets of EUR 5 billion or more in a Member State are considered higher risk, as are those authorised to take deposits, irrespective of their size, if the amount of such deposits exceeds a certain threshold.

Although branches of third-country institutions do not have a significant presence in Portugal, it has become apparent that there is a need to establish a specific regulatory framework for these branches, which is not the result of purely prescriptive rules. In addition to ensuring consistency within the EU, the existence of a solid specific regulatory framework will undoubtedly help the competent authorities to exercise greater control over these entities, thus contributing to greater legal certainty and stability.

Of particular note is the explicit provision, for the first time in the European banking regulatory framework, of the possibility of providing banking services on the sole initiative of the client. In Portugal, this possibility is expressly provided for only in relation to the provision of investment services by investment firms (Article 38 of Decree-Law 109-H/2021 of 10 December).

These rules on the establishment and supervision of branches of third-country entities **will apply from 11 January 2027** (except for existing contracts signed before 11 July 2026, which will apply from that date).

The Directive aims to give the competent authorities the supervisory powers they need to monitor all operations that may have a significant impact on the institutions they supervise.

2.2. REINFORCEMENT OF SUPERVISORY POWERS - IN PARTICULAR THE REQUIREMENT FOR PRIOR NOTIFICATION OF “SIGNIFICANT OPERATIONS”

The Directive also aims to give the competent authorities the supervisory powers they need to monitor all operations that may have a significant impact on the institutions they supervise. Thus, three chapters are added to Title III (Articles 27a to 27l) of the Directive and a **new concept of “material operation”** is introduced-. This concept covers the acquisition of significant holdings by supervised entities, significant transfers of assets and liabilities to or from supervised entities, and mergers and divisions involving supervised entities. Essentially, these are operations that may raise concerns about their prudential profile or possible money laundering or terrorist financing activities.

The Directive also introduces the concept of “**material holding**”. This concept covers the acquisition by supervised entities of holdings of 15% or more of the eligible capital of the proposed acquirer in any entity, whether or not in the financial sector, with the exception of intra-group acquisitions. These operations will now be assessed by the competent authority on the basis of a procedure requiring prior notification and tacit approval, which these authorities have 60 working days to provide. If the proposed acquisition concerns a qualifying holding in a credit institution under the conditions and for the purposes of Article 22 of the CRD, the proposed acquirer is also subject to the notification and assessment requirements set out in that Article (Articles 27a to 27e of CRD VI).

In the case of a **transfer of assets and liabilities**, the proposed operation is considered to be material to an entity if it represents at least 10% of its total assets or total liabilities, unless it is between entities within the same group, in which case the proposed operation is considered to be material to an entity if it represents at least 15% of its total assets or total liabilities. (Articles 27f and 27g CRD VI).

With respect to **mergers and divisions**, the established assessment procedure is intended to complement the procedure laid down in Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017 on certain aspects of company law and Council Regulation (EC) 139/2004 of 20 January 2004 on the control of concentrations between undertakings. The concepts of merger and division for the purposes of this procedure are defined in Article 27h of CRD VI and require a favourable prior opinion from the competent authorities (Articles 27h to 27l of CRD VI).

The aim of these new amendments is to ensure that the competent authorities are informed in a timely manner and that they have all the information they need to prudentially assess these operations. Ultimately, the competent authorities will have to object to operations that could jeopardise the prudential profile of supervised entities or raise money laundering or terrorist financing concerns.

There is also a framework of penalties for non-compliance with these provisions, which must include administrative fines, periodic penalty payments and other administrative measures. In particular, in the case of legal persons, fines may amount to up to 10% of the total annual net turnover of the entity, or up to twice the amount of profits made or losses avoided as a result of the offence if such profits or losses can be determined. In addition, periodic fines may be imposed up to a maximum of 5% of the average daily net turnover.

2.3. ESG (ENVIRONMENTAL, SOCIAL AND GOVERNANCE) RISKS

This Directive also reflects the concern to ensure that the financial sector, and credit institutions in particular, adapt appropriately to the objective of making the EU economy climate neutral by 2050.

Institutions are therefore required to have **sound governance systems and internal processes** for managing environmental, social and governance ("**ESG**") risks and to have strategies approved by their management bodies that take into account not only the current but also the future impact of these risks.

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To this end, the wording of Articles 73 and 74 of the CRD is amended to include an obligation for institutions to take ESG risks into account when assessing the **adequacy of their internal capital and when establishing effective processes for their proper identification, monitoring and management**. A new paragraph is also added to Article 76(2), requiring the board to oversee the institution's implementation of specific plans that include quantifiable targets and processes for monitoring and responding to financial risks arising from these ESG risks in the short, medium and long term, including those arising from the objective of achieving climate neutrality.

Proportionality will be ensured for small and non-complex institutions by means of a waiver or a simplified procedure.

In turn, the independence and resource requirements of internal control functions are strengthened to ensure proper identification and assessment of all types of risks to which the institution is exposed, not just ESG risks.

These new obligations for credit institutions are accompanied by enhanced supervision, as provided for in Article 87a of CRD VI. This requires competent authorities to ensure that institutions comply with the Directive's ESG obligations. In particular, they must ensure that they have effective and proportionate strategies, policies, procedures and systems in place to identify, assess, manage and monitor ESG risks in the short, medium and long term. To this end, the EBA is expected to issue guidance by 10 January 2026.

Finally, the amendment of Article 133 on the framework for the systemic risk reserve to cover risks related to climate change is noteworthy.

2.4. SUITABILITY OF MEMBERS OF THE BOARD OF DIRECTORS AND KEY FUNCTION HOLDERS

The Directive also aims to harmonise the rules on assessing the suitability of board members and key function holders in all EU countries.

With regard to the **assessment of the suitability of board members**, new paragraphs have been added to Article 91 of the CRD to specify the need for a prior assessment before the new member takes office. Exceptions are made in cases where it is intended to replace at the same time the majority of the members of the management body by newly appointed members and the prior assessment would result in the assessment of the suitability of the new members being carried out by the outgoing members. In such cases, Member States may allow the assessment to take place after the newly appointed members have taken office. A continuous assessment of the suitability criteria and requirements is also required. The possibility for the competent authorities to conduct interviews or hearings with candidates is made explicit.

It is also intended to ensure that competent authorities have the necessary powers to: (i) in the case of an assessment made before a potential member takes up a position, to prevent that member from being part of the management body or to remove him or her from the management body; (ii) in the case of an assessment after a person has become a member, to remove that member from the management body; or (iii) to require the entities concerned to take the additional measures necessary to ensure that such members are or become suitable for the position in question.

A new Article 91a is also introduced, which sets out a framework for assessing the suitability of key function holders.

Of particular note is the introduction of an obligation for institutions to draw up individual statements setting out the roles and duties of each member of the management body in its management function, senior management and key function holders. They must also draw up a mapping of duties, including details of the lines of communication, reporting lines and persons who are part of the governance arrangements of the institution, and of their duties. However, this does not affect the overall responsibility of the management body (Article 88(3) of CRD VI).

2.5. CRYPTOASSETS

In line with existing European legislation on cryptoassets, this Directive also ensures that institutions with direct or indirect exposures to cryptoassets, or institutions providing related services for any type of cryptoasset, have risk management policies, processes and practices in place to adequately manage the risks arising from their exposures to cryptoassets (see Articles 81, 85 and 98 of CRD VI).

In its recitals, the Directive highlights the risks of cryptoasset technologies, general information and communication technology (ICT) risks and cyber risks, legal risks, money laundering and terrorist financing risks and valuation risks.

The Directive requires Member States to take the necessary measures to ensure that competent authorities exercise their supervisory powers in a transparent, independent and objective manner.

2.6. STRENGTHENING INDEPENDENCE RULES FOR COMPETENT AUTHORITIES WITH SUPERVISORY POWERS

The Directive requires Member States to take the necessary measures to ensure that competent authorities, including their staff and members of their management bodies, exercise their supervisory powers in a transparent, independent and objective manner.

- **Disclosure of appointment criteria and term limits**
  The published criteria for the appointment of members of the governance body of a competent authority must be objective and transparent from the outset. In addition, they must be subject to removal if they no longer meet these criteria or if they have been convicted of a serious criminal offence. Furthermore, no member of the governing body of a competent authority appointed after 11 January 2026 should remain in office for more than 14 years. In addition, employees and members of the governing bodies of competent authorities will have to submit an annual declaration of interests, including information on holdings in financial instruments.

- **Conflicts of interest**
  The Directive also lays down minimum requirements to prevent conflicts of interest, in particular by providing for cooling-off periods for taking new positions, which may be up to 12 months in certain cases, and the right to appropriate compensation. These cooling-off periods apply (i) to trading in financial instruments issued by, or related to, the institutions supervised by the competent authorities and their direct or indirect parent companies, subsidiaries or affiliates, or, more prominently, (ii) to the provision of professional services to (a) institutions in which the staff member or member of the governing body of the competent authority has been directly involved for supervisory or decision-making purposes; or including direct or indirect parent companies, subsidiaries or branches of such entities, (b) entities providing services to any of the above mentioned entities, and (c) entities carrying out lobbying or advocacy activities directed at the competent authority on matters for which the staff member or member of the governing body of the competent authority was responsible during his or her contract of employment or term of office.

3. Changes to CRR III – Brief notes

The recitals of the CRR state that the overall level of own funds of institutions in the EU is considered satisfactory. However, the aim is to provide legal certainty and to fulfil the commitment made to the international partners of the G20 by incorporating, through this Regulation, the outstanding elements of the Basel III reforms agreed by the BCBS in 2017.

First, this Regulation establishes an output floor (minimum threshold) for the capital requirements that banks must maintain in order to reduce the excessive variability of banks' capital requirements calculated on the basis of internal models, thus allowing for greater comparability between them (Article 92). These provisions should be read in conjunction with the amendments to Article 104a of CRD VI.

Changes are made to the calculation of capital requirements for market risk to reflect the fundamental review of the trading book to be completed by the BCBS in 2019 (Articles 325 and 325a of the Regulation).

New articles are also introduced to specify the methods for calculating capital requirements for credit valuation adjustment ("CVA") risk. This is defined as the risk of loss resulting from changes in the value of the CVA calculated for the portfolio of transactions entered into with a counterparty due to fluctuations in the counterparty credit spread risk factors and other risk factors included in the portfolio of transactions (Articles 381 to 384 of the Regulation).

It also introduces a standardised approach to the calculation of capital requirements for operational risk, replacing the models currently in use and redrafts Title III of Part III (Articles 312 to 324 of the Regulation).

Also noteworthy is the concern for proportionality in order to reduce the regulatory burden on smaller, non-complex institutions by allowing a reduction of the burden by reference to disclosure requirements (Articles 433b and 434c of the Regulation).

4. Entry into force and deadlines for implementation

CRD VI will enter into force on 9 July 2024. For their part, Member States must incorporate CRD VI into national law by 10 January 2026. The only exceptions are some specific provisions, including the new rules on the establishment of branches of entities based in third countries and their supervision. These rules will apply from 11 January 2027. However, existing contracts concluded before 11 July 2026 will apply from that date.

CRR III will also enter into force on 09 July 2024 and will apply from 1 January 2025, except for some specific provisions which will apply immediately, i.e. from 9 July 2024.

CRD VI must be incorporated into national law by 10 January 2026. CRR III will apply from 1 January 2025.

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About the Banking and Finance team

→ What we do

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