

INVESTMENT SERVICES RULES FOR INVESTMENT SERVICE PROVIDERS

PART B - STANDARD LICENCE CONDITIONS

Appendix 1C

Capital Buffers Requirement Applicable to Category 3 Investment Services Licence Holders

This Appendix:

- a. details the capital buffers requirement;
- b. explains the various kinds of capital buffers to be maintained by Category 3 Investment Firms; and
- c. explains the manner in which the capital buffers are calculated.

1. Introduction

- 1.1 In terms of Article 6 (2) (b) of the Investment Services Act 1994 (Cap. 370) (hereinafter referred to as ‘the Act’) the competent authority (‘the authority’) as defined in Article 2(1) of the Act is empowered to make Investment Services Rules as may be required for carrying into effect any of the provisions of the Act. The authority may also amend or revoke such Investment Services Rules and any amendment or revocation thereof shall be officially communicated to Investment Services Licence Holders and the authority shall make copies thereof available to the public.

2. Scope and Application

- 2.1 These Rules apply to Category 3 Investment Services Licence Holders licensed under the Act.
- 2.2 These Rules transpose paragraph 30 of Article 3(1), Articles 128(1) – (8), 129, 130, 131, 140, 141, 142, 160(2)(b), (3)(b) (4)(b), (5), (6) and (7), 162(5) of the CRD:

Provided that Article 131 of the CRD is hereby being transposed by the authority in conjunction with Central Bank of Malta.

3. Definitions

- 3.1 For the purposes of the Rule, the following definitions shall apply:
- (i) The ‘Act’ means the Investment Services Act, 1994;
 - (ii) ‘capital conservation buffer’ means the own funds that an investment firm is required to maintain in accordance with Rule 4.1 to 4.3 of this Appendix [Article 129 of the CRD];
 - (iii) ‘Capital Requirements Directive’, hereinafter referred to as the CRD, refers to 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;
 - (iv) ‘Capital Requirements Regulation’, hereinafter referred to as the CRR, refers to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential

requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012;

- (v) 'CBM Directive' means the Central Bank of Malta Directive No. 11 on Macro-prudential policy;
- (vi) 'Central Bank of Malta' means:
 - (a) the 'designate authority' in conjunction with the authority, in charge of identifying on a consolidated basis, global systemically important investment firms (G-SIIs) and, on an individual, sub-consolidated or consolidated basis, as applicable, other systemically important institutions (O-SIIs) which have been authorised in Malta in terms of Article 131 of the CRD as appointed by the Central Bank of Malta Act (Appointment of Designate Authority to implement Macro-Prudential Instruments) Regulations, 2014; and
 - (b) the 'designate authority' responsible for setting the countercyclical buffer rate in accordance with Article 136 of the CRD as appointed by the Central Bank of Malta Act (Appointment of Designate Authority to implement Macro-Prudential Instruments) Regulations, 2014;
- (vii) 'combined buffer requirement' means the total Common Equity Tier 1 capital required to meet the requirement for the capital conservation buffer extended by the following as applicable:
 - (a) an institution-specific countercyclical capital buffer;
 - (b) a G-SII buffer;
 - (c) an O-SII buffer;
 - (d) a systemic risk buffer;
- (viii) 'Common Equity Tier 1 capital' shall have the same meaning as that assigned to it in Article 50 of the CRR;
- (ix) 'countercyclical buffer rate' means the rate that investment firms must apply in order to calculate their institution-specific countercyclical capital buffer, and that is set in accordance with Articles 136 and 137 of the CRD or by a relevant third-country authority, as the case may be;

- (x) 'G-SII buffer' means the own funds that are required to be maintained in accordance with Rule 7.4 of the Appendix [Article 131(4) of the CRD];
- (xi) 'institution-specific countercyclical capital buffer' means the own funds that an investment firm is required to maintain in accordance with Rules 5.1 to 5.3 of this Appendix [Article 130 of the CRD];
- (xii) 'investment firm' means investment firm as defined in point (2) of Article 4 (1) of Regulation (EU) No 575/2013;
- (xiii) 'O-SII buffer' means the own funds that may be required to be maintained in accordance with Rule 7.6 of this Appendix [Article 131(5) of the CRD];
- (xiv) 'Small and medium-sized investment firms' means an investment firm which employs fewer than two hundred and fifty (250) persons and which has an annual turnover not exceeding EUR 50 million, and / or an annual balance sheet total not exceeding EUR 43 million, as defined in Article 2 of Title 1 of the Annex to the Commission Recommendation 2003/361/EC of the 6th May 2003;
- (xv) 'systemic risk buffer' means the own funds that an investment firm is or may be required to maintain in accordance with paragraphs 14 to 32 of the CBM Directive [Article 133 of the CRD];
- (xvi) 'systemically important institution' means an EU parent institution, an EU parent financial holding company, an EU parent mixed financial holding company or an institution the failure or malfunction of which could lead to systemic risk as defined in point (30) of Article 3 (1) of the CRD.

4. Capital Conservation Buffer

- 4.1 In addition to the Common Equity Tier 1 capital maintained to meet the own funds requirement imposed by Article 92 of the CRR, investment firms shall maintain a capital conservation buffer of Common Equity Tier 1 capital equal to 2.5% of their total risk exposure amount calculated in accordance with Article 92(3) of the CRR on an individual and consolidated basis, as applicable in accordance with Part One, Title II of the CRR.
- 4.2 Investment firms shall not use Common Equity Tier 1 capital that is maintained to meet the requirement prescribed in terms of Rule 4.1 of this Appendix to meet any requirements prescribed in terms of Schedule III of the Investment Services Act (Supervisory Review) Regulations, 2013 [L.N. 30 of 2014] [Article 104 of the CRD].

- 4.3 Where an investment firm fails to meet fully the requirement prescribed in terms of Rule 4.1 of this Appendix, it shall be subject to the restrictions on distributions set out in Rules 9.1 to 9.10 of this Appendix. [Article 141(2) and (3) of the CRD].
- 4.4 By way of derogation from Rule 4.1 of this Appendix, small and medium-sized investment firms shall be exempted from the requirements set out in that paragraph if such an exemption does not threaten the stability of Malta's financial system:

Provided that for the purposes of this Rule, small and medium-sized investment firms shall be defined in accordance with the European Commission Recommendation 2003/361/EC concerning the definition of micro, small and medium-sized enterprises.

5. Institution Specific Countercyclical Buffer

- 5.1 Investment firms shall maintain an institution-specific countercyclical capital buffer equivalent to their total risk exposure amount calculated in accordance with Article 92(3) of the CRR multiplied by the weighted average of the countercyclical buffer rates calculated in accordance with Rules 6.1 to 6.8 of this Appendix [Article 140 of the CRD] on an individual and consolidated basis, as applicable in accordance with Part One, Title II of the CRR.
- 5.2 Investment firms shall meet the requirement imposed by Rule 5.1 of this Appendix with Common Equity Tier 1 capital, which shall be additional to:
- i. any Common Equity Tier 1 capital maintained to meet the own funds requirement imposed by Article 92 of the CRR;
 - ii. the requirement to maintain a capital conservation buffer in terms of Rules 4.1 to 4.3 of this Appendix [Article 129 of the CRD]; and
 - iii. any requirement imposed in terms of Schedule III of the Investment Services Act (Supervisory Review) Regulations, 2013 [L.N. 30 of 2014] [Article 104 of the CRD].
- 5.3 Where an investment firm fails to meet fully the requirement prescribed in terms of Rule 5.1 of this Appendix, it shall be subject to the restrictions on distributions set out in Rules 9.1 to 9.10 of this Appendix [Article 141(2) and (3) of the CRD].
- 5.4 By way of derogation from Rule 5.1 of this Appendix, small and medium-sized investment firms shall be exempted from the requirements set out in that paragraph if such an exemption does not threaten the stability of Malta's financial system:

- 5.5 Provided that for the purposes of this Rule, small and medium-sized investment firms shall be defined in accordance with the European Commission Recommendation 2003/361/EC concerning the definition of micro, small and medium-sized enterprises.

6. Calculation of Institution-Specific Countercyclical Capital Buffer Rates

- 6.1 The institution-specific countercyclical capital buffer rate shall consist of the weighted average of the countercyclical buffer rates that apply in the jurisdictions where the relevant credit exposures of the investment firm are located or are applied for the purposes of Rules 6.1 to 6.8 of this Appendix by virtue of paragraphs 62 and 63 of the CBM Directive [Article 139(2) or (3) of the CRD].
- 6.2 In order to calculate the weighted average referred to in Rule 6.1 of this Appendix, investment firms shall apply to each applicable countercyclical buffer rate its total own funds requirements for credit risk, determined in accordance with Part Three, Titles II and IV of the CRR, that relates to the relevant credit exposures in the territory in question, divided by its total own funds requirements for credit risk that relates to all of its relevant credit exposures.
- 6.3 If, in accordance with paragraph 55 of the CBM Directive, the Central Bank of Malta sets a countercyclical buffer rate in excess of 2.5% of total risk exposure amount calculated in accordance with Article 92(3) of the CRR, investment firms shall apply that buffer rate in excess of 2.5% of total risk exposure amount to relevant credit exposures located in Malta for the purposes of the calculation prescribed in terms of Rules 6.1 and 6.2 of this Appendix including, where relevant, for the purposes of the calculation of the element of consolidated capital that relates to the investment firm in question.
- 6.4 If, in accordance with Article 136(4) of the CRD, a designated authority in another Member State sets a countercyclical buffer rate in excess of 2.5% of total risk exposure amount calculated in accordance with Article 92(3) of the CRR, the following buffer rates shall apply to relevant credit exposures located in the Member State of that designated authority for the purposes of the calculation prescribed in terms of Rules 6.1 and 6.2 of this Appendix including, where relevant, for the purposes of the calculation of the element of consolidated capital that relates to the investment firm in question:
- (a) investment firms shall apply a countercyclical buffer rate of 2.5% of total risk exposure amount if the Central Bank of Malta has not recognised the buffer rate in excess of 2.5 % in accordance with paragraph 59 of the CBM Directive [Article 137(1) of the CRD];

- (b) investment firms shall apply the countercyclical buffer rate set by the designated authority of another Member State appointed for the purposes of Article 136(1) of the CRD if the Central Bank of Malta has recognised the buffer rate in accordance with paragraph 59 and 60 of the CBM Directive [Article 137 of the CRD].

- 6.5 If the countercyclical buffer rate set by the relevant third-country authority for a third country exceeds 2.5% of total risk exposure amount calculated in accordance with Article 92(3) of the CRR, the following buffer rates shall apply to relevant credit exposures located in that third country for the purposes of the calculation prescribed in terms of Rules 6.1 and 6.2 of this Appendix including, where relevant, for the purposes of the calculation of the element of consolidated capital that relates to the investment firm in question:
 - (a) investment firms shall apply a countercyclical buffer rate of 2.5% of total risk exposure amount if the Central Bank of Malta has not recognised the buffer rate in excess of 2.5% in accordance with paragraph 59 of the CBM Directive [Article 137(1) of the CRD];
 - (b) investment firms shall apply the countercyclical buffer rate set by the relevant third-country authority if the Central Bank of Malta has recognised the buffer rate in accordance with paragraphs 59 and 60 of the CBM Directive [Article 137 of the CRD].

- 6.6 Relevant credit exposures shall include all those exposure classes, other than those referred to in points (a) to (f) of Article 112 of the CRR, that are subject to:
 - (a) the own funds requirements for credit risk under Part Three, Title II of the CRR;
 - (b) where the exposure is held in the trading book:
 - i. own funds requirements for specific risk under Part Three, Title IV, Chapter 2 of the CRR; or
 - ii. incremental default and migration risk under Part Three, Title IV, Chapter 5 of the CRR;
 - (c) where the exposure is a securitisation, the own funds requirements under Part Three, Title II, Chapter 5 of the CRR.

- 6.7 Investment firms shall identify the geographical location of a relevant credit exposure in accordance with [Commission Delegated Regulation \(EU\) No 1152/2014 of 4 June 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to regulatory technical standards on the identification of](#)

[the geographical location of the relevant credit exposures for calculating institution-specific countercyclical capital buffer rates](#). Moreover, pursuant to Article 440 of the CRR, investment firms shall disclose key elements of the calculation of their countercyclical capital buffer in accordance with the [Commission Delegated Regulation \(EU\) 2015/1555 of 28 May 2015 supplementing Regulation \(EU\) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for the disclosure of information in relation to the compliance of institutions with the requirement for a countercyclical capital buffer](#).

- 6.8 For the purposes of the calculation prescribed in terms of Rules 6.1 and 6.2 of this Appendix:
- (a) a countercyclical buffer rate for Malta shall apply from the date specified in the information published in accordance with paragraphs 58(e) or 60(c) of the CBM Directive if the effect of that decision is to increase the buffer rate;
 - (b) a countercyclical buffer rate for another Member State shall apply from the date specified in the information published in accordance with Article 136(7)(e) or Article 137(2)(c) of the CRD if the effect of that decision is to increase the buffer rate;
 - (c) subject to point (d), a countercyclical buffer rate for a third country shall apply 12 months after the date on which a change in the buffer rate was announced by the relevant third-country authority, irrespective of whether that authority requires institutions incorporated in that third country to apply the change within a shorter period, if the effect of that decision is to increase the buffer rate;
 - (d) where the Central Bank of Malta sets the countercyclical buffer rate for a third country pursuant to paragraphs 62 and 63 of the CBM Directive [Article 139(2) or (3) of the CRD], or recognises the countercyclical buffer rate for a third country pursuant to paragraphs 59 and 60 of the CBM Directive [Article 137 of the CRD], that buffer rate shall apply from the date specified in the information published in accordance with paragraphs 65(c) or 60(c) of the CBM Directive [Article 139(5)(c) or Article 137(2)(c) of the CRD], if the effect of that decision is to increase the buffer rate;
 - (e) a countercyclical buffer rate shall apply immediately if the effect of that decision is to reduce the buffer rate.

For the purposes of point (c), a change in the countercyclical buffer rate for a third country shall be considered to be announced on the date that it is published by the relevant third-country authority in accordance with the applicable national rules.

7. Global and Other Systemically Important Institutions

7.1 The Authority shall, in accordance with article 12(1)(k) and (l) of the Act, together with the Central Bank of Malta, appointed as the designate authority for the purposes of Article 131(1) of the CRD in terms of the Central Bank of Malta Act (Appointment of Designate Authority to implement Macro-Prudential Instruments) Regulations, 2014 [L.N. 29 of 2014], be responsible for identifying, on a consolidated basis, global systemically important institutions (G-SIIs), and, on an individual, sub-consolidated or consolidated basis, as applicable, other systemically important institutions (O-SIIs), which have been licensed in terms of the Act.

G-SIIs shall be an EU parent institution, an EU parent financial holding company, an EU parent mixed financial holding company or an institution as defined in the CRR. G-SIIs shall not be an institution that is a subsidiary of an EU parent institution, of an EU parent financial holding company or of an EU parent mixed financial holding company.

O-SIIs can either be an EU parent institution, an EU parent financial holding company, an EU parent mixed financial holding company or an institution as defined in the CRR.

7.2 The identification methodology for G-SIIs shall be based on the following categories:

- (a) size of the group;
- (b) interconnectedness of the group with the financial system;
- (c) substitutability of the services or of the financial infrastructure provided by the group;
- (d) complexity of the group;
- (e) cross-border activity of the group, including cross border activity between Member States and between a Member State and a third country.

Each category shall receive an equal weighting and shall consist of quantifiable indicators.

The methodology shall produce an overall score for each entity assessed as referred to in Rule 7.1 of this Appendix, which allows G-SIIs to be identified and allocated into a sub-category as described in Rule 7.10 of this Appendix.

- 7.3 O-SIIs shall be identified in accordance with Rule 7.1 of this Appendix. Systemic importance shall be assessed on the basis of at least any of the following criteria:
- (a) size;
 - (b) importance for the economy of the Union or of Malta;
 - (c) significance of cross-border activities;
 - (d) interconnectedness of the investment firm or group with the financial system.

In determining the conditions of application of Rule 7.3 of this Appendix in relation to the assessment of O-SIIs, the authority may be guided, *inter alia*, by any guideline/s published by the EBA in accordance with Article 131(3) of the CRD.

- 7.4 Each G-SII shall, on a consolidated basis, maintain a G-SII buffer which shall correspond to the sub-category to which the G-SII is allocated. That buffer shall consist of and shall be supplementary to Common Equity Tier 1 capital.
- 7.5 The authority, acting jointly with the Central Bank of Malta, may require each O-SII, on a consolidated or sub-consolidated or individual basis, as applicable, to maintain an O-SII buffer of up to 2% of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR, taking into account the criteria for the identification of the O-SII:

Provided that such buffer shall consist of and shall be supplementary to Common Equity Tier 1 capital.

- 7.6 When requiring an O-SII buffer to be maintained the authority, acting jointly with the Central Bank of Malta, shall comply with the following:
- (a) the O-SII buffer must not entail disproportionate adverse effects on the whole or parts of the financial system of other Member States or of the Union as a whole forming or creating an obstacle to the functioning of the internal market;
 - (b) the authority, acting jointly with the Central Bank of Malta, shall review the O-SII buffer at least annually.

7.7 Before setting or resetting an O-SII buffer, the authority, acting jointly with the Central Bank of Malta, shall notify the European Commission, the ESRB, the EBA, and the competent and designated authorities of the Member States concerned one month before the publication of the decision referred to in Rule 7.6 of this Appendix.

The said notification shall describe in detail:

- (a) the justification for why the O-SII buffer is considered likely to be effective and proportionate to mitigate the risk;
- (b) an assessment of the likely positive or negative impact of the O-SII buffer on the internal market, based on information which is available to the authority and the Central Bank of Malta;
- (c) the O-SII buffer rate that the authority, acting jointly with the Central Bank of Malta, wishes to set.

7.8 Without prejudice to paragraphs 14 to 32 of the CBM Directive [Article 133 of the CRD] and Rule 7.5 of this Appendix, where an O-SII is a subsidiary of either a G-SII or an O-SII which is an EU parent institution and subject to an O-SII buffer on a consolidated basis, the buffer that applies at individual or sub-consolidated level for the O-SII shall not exceed the higher of:

- (a) 1 % of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR; and
- (b) the G-SII or O-SII buffer rate applicable to the group at consolidated level.

7.9 The authority, acting jointly with the Central Bank of Malta, shall establish at least five subcategories of G-SIIs.

The lowest boundary and the boundaries between each sub-category shall be determined by the scores under the identification methodology.

The cut-off scores between adjacent sub-categories shall be defined clearly and shall adhere to the principle that there is a constant linear increase of systemic significance, between each sub-category resulting in a linear increase in the requirement of additional Common Equity Tier 1 capital, with the exception of the highest sub-category.

The lowest sub-category shall be assigned a G-SII buffer of 1 % of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR and the

buffer assigned to each sub-category shall increase in gradients of 0.5% of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR up to and including the fourth sub-category.

The highest sub-category of the G-SII buffer shall be subject to a buffer of 3.5% of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR.

For the purposes of this paragraph, “systemic significance” is the expected impact exerted by the G-SII's distress on the global financial market.

7.10 Without prejudice to Rule 7.1 and 7.9 of this Appendix, the authority, acting jointly with the Central Bank of Malta, may, in the exercise of sound supervisory judgment:

- (a) re-allocate a G-SII from a lower sub-category to a higher sub-category;
- (b) allocate an entity as referred to in Rule 7.1 of this Appendix, which has an overall score that is lower than the cut-off score of the lowest sub-category, to that sub-category or to a higher sub-category, thereby designating it as a G-SII.

7.11 Where the authority, acting jointly with the Central Bank of Malta, takes a decision in accordance with Rule 7.10(b) of this Appendix, it shall notify the EBA accordingly, providing reasons.

7.12 The authority, acting jointly with the Central Bank of Malta, shall notify the names of the G-SIIs and O-SIIs and the respective sub-category to which each G-SII is allocated, to the European Commission, the ESRB and the EBA, and shall disclose their names to the public. The authority, acting jointly with the Central Bank of Malta, shall disclose to the public the sub-category to which each G-SII is allocated.

The authority, acting jointly with the Central Bank of Malta, shall review annually the identification of G-SIIs and O-SIIs and the G-SII allocation into the respective sub-categories and report the result to the systemically important institution concerned, to the European Commission, the ESRB and the EBA and disclose the updated list of identified systemically important institutions to the public.

The authority, acting jointly with the Central Bank of Malta, shall disclose to the public the sub-category into which each identified G-SII is allocated.

7.13 Systemically important institutions shall not use the Common Equity Tier 1 capital which is maintained in terms of Rule 7.5 and 7.6 of this Appendix, to meet any of the following requirements:

- (i) requirements imposed under Article 92 of the CRR;
 - (ii) requirements to maintain a capital conservation buffer as prescribed in Rules 4.1 to 4.3 of this Appendix;
 - (iii) requirements to maintain an institution-specific countercyclical capital buffer as prescribed in Rules 5.1 to 5.3 of this Appendix; and
 - (iv) any requirements imposed in terms of Article 16 of the Investment Services Act (Supervisory Review) Regulations, 2013 [L.N. 30 of 2014] [Article 102 of the CRD].
 - (v) any requirements imposed in terms of Schedule III of the Investment Services Act (Supervisory Review) Regulations, 2013 [L.N. 30 of 2014] [Article 104 of the CRD].
- 7.14 Where a group, on a consolidated basis, is subject to the following, the higher buffer shall apply in each case:
- (a) a G-SII buffer and an O-SII buffer;
 - (b) a G-SII buffer, an O-SII buffer and a systemic risk buffer in accordance with Article 133 of the CRD.

Where an investment firm, on an individual or sub-consolidated basis is subject to an O-SII buffer and a systemic risk buffer in accordance with Article 133 of the CRD, the higher of the two shall apply.

- 7.15 Notwithstanding the provisions of Rules 7.14 of this Appendix, where the systemic risk buffer applies to all exposures located in Malta, but does not apply to exposures outside Malta, that systemic risk buffer shall be cumulative with the O-SII or G-SII buffer that is applied in accordance with Rules 7.1 to 7.19 of this Appendix.
- 7.16 Where Rule 7.15 of this Appendix applies and an investment firm is part of a group or a sub-group to which a G-SII or an O-SII belongs, this shall never imply that such investment firm is, on an individual basis, subject to a combined buffer requirement that is lower than the sum of the capital conservation buffer, the countercyclical capital buffer, and the sum of the O-SII buffer and systemic risk buffer applicable to it on an individual basis.
- 7.17 Where Rule 7.16 of this Appendix applies and an investment firm is part of a group or a sub-group to which a G-SII or an O-SII belongs, this shall never imply that such investment firm is, on an individual basis, subject to a combined buffer requirement that is lower than the sum of the capital conservation buffer, the countercyclical

capital buffer, and the sum of the O-SII buffer and systemic risk buffer applicable to it on an individual basis.

- 7.18 The authority, acting jointly with the Central Bank of Malta, shall identify an EU parent institution or EU parent financial holding company or EU parent mixed financial holding company as a G-SII and shall define the sub-categories and the allocation of G-SIIs in sub-categories based on their systemic significance in accordance with the methodology specified in the [Commission Delegated Regulation \(EU\) No 1222/2014 of 8 October 2014 supplementing Directive 2013/36/EU of the European Parliament and of the Council with regard to Regulatory Technical Standards for the specification of the methodology for the identification of global systemically important institutions and for the definition of subcategories of global systemically important institutions](#):

Provided that, pursuant to Article 441 of the CRR, investment firms identified as G-SIIs shall disclose indicator values used in the identification process in accordance with the [Commission Implementing Regulation \(EU\) No 1030/2014 of 29 September 2014 laying down Implementing Technical Standards with regard to the uniform formats and date for the disclosure of the values used to identify globally systemic important institutions according to Regulation \(EU\) No 575/2013 of the European Parliament and Council](#) and the [Guidelines on Disclosure of Indicators of Global Systemic Importance](#), which were published by the EBA on the 5 June 2014.

8. Systemic Risk Buffer

Investment firms are to refer to the Central Bank of Malta Act (Appointment of Designate Authority to implement Macro-Prudential Instruments) Regulations, 2014 [L.N. 29 of 2014] and to the CBM Directive with regards to the maintenance of a systemic risk buffer under Article 133 of the CRD.

9. Restrictions on Distributions

- 9.1 An investment firm that meets the combined buffer requirement shall be prohibited from making a distribution in connection with Common Equity Tier 1 capital to an extent that would decrease its Common Equity Tier 1 capital to a level where the combined buffer requirement is no longer met.
- 9.2 An investment firm that fails to meet the combined buffer requirement shall be required to calculate the Maximum Distributable Amount ('MDA') in accordance with Rule 9.4 of this Appendix. Such investment firms shall be required to notify the authority of that MDA.

In such circumstances the investment firm shall be prohibited from undertaking any of the following actions before it has calculated the MDA:

- (a) make a distribution in connection with Common Equity Tier 1 capital;
- (b) create an obligation to pay variable remuneration or discretionary pension benefits or pay variable remuneration if the obligation to pay was created at a time when the investment firm failed to meet the combined buffer requirements;
- (c) make payments on Additional Tier 1 instruments.

9.3 An investment firm that fails to meet or exceed its combined buffer requirement shall be prohibited from distributing more than the MDA calculated in accordance with Rule 9.4 of this Appendix through any action referred to in sub-paragraphs (a), (b) and (c) of Rule 9.2 of this Appendix.

9.4 An investment firm shall calculate the MDA by multiplying the sum calculated in accordance with Rule 9.5 of this Appendix by the factor determined in accordance with Rule 9.6 of this Appendix.

The MDA shall be reduced by any of the actions referred to in sub-paragraphs (a), (b) or (c) of Rule 9.2 of this Appendix.

9.5 The sum to be multiplied in accordance with Rule 9.4 of this Appendix shall consist of:

- (a) interim profits not included in Common Equity Tier 1 capital pursuant to Article 26(2) of the CRR that have been generated since the most recent decision on the distribution of profits or any of the actions referred to in sub-paragraphs (a), (b) or (c) of Rule 9.2 of this Appendix;

plus

- (b) year-end profits not included in Common Equity Tier 1 capital pursuant to Article 26(2) of the CRR that have been generated since the most recent decision on the distribution of profits or any of the actions referred to in sub-paragraphs (a), (b) or (c) of Rule 9.2 of this Appendix;

minus

- (c) amounts which would be payable by tax if the items specified in points (a) and (b) of this paragraph were to be retained.

9.6 The factor shall be determined as follows:

- (a) where the Common Equity Tier 1 capital maintained by the investment firm which is not used to meet the own funds requirement under Article 92(1)(c) of the CRR, expressed as a percentage of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR, is within the first (that is, the lowest) quartile of the combined buffer requirement, the factor shall be 0;
- (b) where the Common Equity Tier 1 capital maintained by the investment firm which is not used to meet the own funds requirement under Article 92(1)(c) of the CRR, expressed as a percentage of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR, is within the second quartile of the combined buffer requirement, the factor shall be 0.2;
- (c) where the Common Equity Tier 1 capital maintained by the investment firm which is not used to meet the own funds requirement under Article 92(1)(c) of the CRR, expressed as a percentage of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR, is within the third quartile of the combined buffer requirement, the factor shall be 0.4;
- (d) where the Common Equity Tier 1 capital maintained by the investment firm which is not used to meet the own funds requirement under Article 92(1)(c) of the CRR, expressed as a percentage of the total risk exposure amount calculated in accordance with Article 92(3) of the CRR, is within the fourth (that is, the highest) quartile of the combined buffer requirement, the factor shall be 0.6;

The lower and upper bounds of each quartile of the combined buffer requirement shall be calculated as follows:

$$\text{Lower bound of quartile} = \frac{\text{Combined buffer requirement}}{4} \times (Q_n - 1)$$

$$\text{Upper bound of quartile} = \frac{\text{Combined buffer requirement}}{4} \times Q_n$$

"Q_n" indicates the ordinal number of the quartile concerned.

- 9.7 The restrictions imposed by Rules 9.1 to 9.10 of this Appendix shall only apply to payments that result in a reduction of Common Equity Tier 1 capital or in a reduction of profits, and where a suspension of payment or failure to pay does not constitute an event of default or a condition for the commencement of proceedings under the insolvency regime applicable to the investment firm.
- 9.8 Where an investment firm fails to meet the combined buffer requirement and intends to distribute any of its distributable profits or undertake an action referred to in subparagraphs (a), (b) and (c) of Rule 9.2 of this Appendix, it shall notify the authority and provide the following information:
- (a) the amount of capital maintained by the investment firm, subdivided as follows:
 - i. Common Equity Tier 1 capital,
 - ii. Additional Tier 1 capital,
 - iii. Tier 2 capital;
 - (b) the amount of its interim and year-end profits;
 - (c) the MDA calculated in accordance with Rule 9.4 of this Appendix;
 - (d) the amount of distributable profits it intends to allocate between the following:
 - i. dividend payments,
 - ii. share buybacks,
 - iii. payments on Additional Tier 1 instruments,
 - iv. the payment of variable remuneration or discretionary pension benefits, whether by creation of a new obligation to pay, or payment pursuant to an obligation to pay created at a time when the investment firm failed to meet its combined buffer requirements.

- 9.9 Investment firms shall maintain arrangements to ensure that the amount of distributable profits and the MDA are calculated accurately, and shall be able to demonstrate that accuracy to the authority on request.
- 9.10 For the purposes of Rules 9.1 and 9.2 of this Appendix, a distribution in connection with Common Equity Tier 1 capital shall include the following:
- (a) a payment of cash dividends;
 - (b) a distribution of fully or partly paid bonus shares or other capital instruments referred to in Article 26(1)(a) of the CRR;
 - (c) a redemption or purchase by an investment firm of its own shares or other capital instruments referred to in Article 26(1)(a) of the CRR;
 - (d) a repayment of amounts paid up in connection with capital instruments referred to in Article 26(1)(a) of the CRR;
 - (e) a distribution of items referred to in points (b) to (e) of Article 26(1) of the CRR.

10. Capital Conservation Plan

- 10.1 Where an investment firm fails to meet its combined buffer requirement, it shall prepare a capital conservation plan and submit it to the authority no later than five working days after it identified that it was failing to meet that requirement, unless the authority authorises a longer delay up to 10 days.

The authority shall grant such authorisations only on the basis of the individual situation of an investment firm and taking into account the scale and complexity of the investment firm's activities.

- 10.2 The capital conservation plan shall include the following:
- (a) estimates of income and expenditure and a forecast balance sheet;
 - (b) measures to increase the capital ratios of the investment firm;
 - (c) a plan and timeframe for the increase of own funds with the objective of meeting fully the combined buffer requirement;

- (d) any other information that the authority considers to be necessary to carry out the assessment required in terms of Rule 10.3 of this Appendix.
- 10.3 The authority shall assess the capital conservation plan, and shall approve the plan only if it considers that the plan, if implemented, would be reasonably likely to conserve or raise sufficient capital to enable the investment firm to meet its combined buffer requirements within a period which the authority considers appropriate.
- 10.4 If the authority does not approve the capital conservation plan in accordance with Rule 10.3 of this Appendix, it shall impose one or both of the following:
- (a) require the investment firm to increase own funds to specified levels within specified periods;
 - (b) exercise its powers in terms of Article 17 of the Act [Article 102 of the CRD] to impose more stringent restrictions on distributions than those required by Rules 9.1 to 9.10 of this Appendix.

11. Transitional Provisions

- 11.1 The requirement for the capital conservation buffer shall be transitioned between the 1 January 2016 and the 31 December 2018 as follows:
- (a) For the period from the 1 January 2016 until the 31 December 2016 the capital conservation buffer shall consist of Common Equity Tier 1 equal to 0.625% of the total of the risk-weighted exposure amounts of the investment firm calculated in accordance with Article 92(3) of the CRR;
 - (b) For the period from the 1 January 2017 until the 31 December 2017 the capital conservation buffer shall consist of Common Equity Tier 1 equal to 1.25% of the total of the risk-weighted exposure amounts of the investment firm calculated in accordance with Article 92(3) of the CRR;
 - (c) For the period from the 1 January 2018 until the 31 December 2018 the capital conservation buffer shall consist of Common Equity Tier 1 equal to 1.875% of the total of the risk-weighted exposure amounts of the investment firm calculated in accordance with Article 92(3) of the CRR.

11.2 The requirement for an institution-specific countercyclical capital buffer shall be transitioned between the 1 January 2016 and the 31 December 2018 as follows:

- (a) For the period from the 1 January 2016 until the 31 December 2016 the institution-specific countercyclical capital buffer shall be no more than 0.625% of the total of the risk-weighted exposure amounts of the investment firm calculated in accordance with Article 92(3) of the CRR;
- (b) For the period from the 1 January 2017 until the 31 December 2017 the institution-specific countercyclical capital buffer shall be no more than 1.25% of the total of the risk-weighted exposure amounts of the investment firm calculated in accordance with Article 92(3) of the CRR;
- (c) For the period from the 1 January 2018 until the 31 December 2018 the institution-specific countercyclical capital buffer shall be no more than 1.875% of the total of the risk-weighted exposure amounts of the investment firm calculated in accordance with Article 92(3) of the CRR.

11.3 The requirement for a capital conservation plan and the restrictions on distributions referred to in Rules 9.1 to 10.4 of this Appendix [Articles 141 and 142 of the CRD] shall apply during the transitional period between 1 January 2016 and 31 December 2018 where investment firms fail to meet the combined buffer requirement taking into account the requirements set out in Rule 11.1 and 11.2 of this Appendix.

11.4 The G-SII buffer shall be implemented as follows:

- (a) 25% of the G-SII buffer, set in accordance with Rule 7.5 of this Appendix, in 2016;
- (b) 50% of the G-SII buffer, set in accordance with Rule 7.5 of this Appendix, in 2017;
- (c) 75% of the G-SII buffer, set in accordance with Rule 7.5 of this Appendix, in 2018;
- (d) 100% of the G-SII buffer, set in accordance with Rule 7.5 of this Appendix, in 2019.

12. Entry into Force

- 12.1 The capital conservation buffer shall apply for 1 January 2016 subject to the transitional periods prescribed in Rule 11.1 of this Appendix.

Notwithstanding the provisions of this paragraph and the transitional periods prescribed in Rule 11.1 of this Appendix, the authority may, in accordance with Article 106(6) of the CRD, impose a shorter transitional period and thereby implement the capital conservation buffer prior to 1 January 2016. Where the authority imposes such a shorter transitional period, it shall inform the relevant parties, including the European Commission, the ESRB, the EBA and the relevant supervisory colleges, accordingly.

The authority may also recognise shorter transitional periods than those prescribed by Article 160(2)(a), (3)(a) and (4)(a) concerning the introduction of the capital conservation buffer imposed by other Member States. Where the authority recognises such a shorter transitional period, it shall notify the European Commission, the ESRB, the EBA and the relevant supervisory college, accordingly.

- 12.2 The institution-specific countercyclical capital buffer shall apply from the 1st January 2016 subject to the transitional periods prescribed in Rule 11.2 of this Appendix and to any shorter transitional periods which may be imposed in accordance with paragraph 66 of the CBM Directive in respect of the countercyclical capital buffer.
- 12.3 Subject to the transitional periods prescribed in Rule 11.4 of this Appendix, the G-SII buffer shall apply from the 1st January 2016.
- 12.4 The authority, acting jointly with the Central Bank of Malta, may require each O-SII, on a consolidated or sub-consolidated or individual basis, as applicable, to maintain, as from the 1st January 2016, an O-SII buffer as prescribed in Rule 7.5 of this Appendix.