

EBA/RTS/2022/12

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20 December 2022

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## Final report

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Draft Regulatory Technical Standards on the identification of a group of connected clients under Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013

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# 1. Executive Summary

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Article 4(4) of Regulation (EU) No 575/2013 (Capital Requirements Regulation – CRR) requires the EBA to submit to the Commission, by June 2020, draft regulatory technical standards (RTS) specifying in which circumstances the conditions set out in point (39) of Article 4 paragraph 1 to form a group of connected clients are met.

The EBA has already adopted in November 2017 own-initiative Guidelines on connected clients under Article 4(1)(39) of the CRR ([EBA/GL/2017/15](#)) (GL). These GL have applied since 1 January 2019 to competent authorities and institutions. They elaborate on the concepts of control and economic dependency, which are the backbone of the definition of a group of connected clients. Both concepts remain unaltered in the amended CRR.

These draft RTS partially repeal and replace the GL. Sections of the GL related to the circumstances of control, economic dependencies and their interaction, will be repealed and transferred without substantial changes to the RTS. All explanatory examples, as well as further guidance on the alternative approach for exposures to central governments and supervisory expectations with regard to control and management procedures for identifying connected clients, will stay in the GL. While the draft RTS concentrate on a clear and harmonised specification of the circumstances in which the conditions set out in point (39) of Article 4 paragraph 1 of the CRR to form a group of connected clients are met, the GL contain practical examples and provide procedural guidance (i.e., when to increase efforts to identify groups of connected clients). The draft RTS in conjunction with the GL provide the complete framework for the identification of group of connected clients.

The definition of group of connected clients in the CRR allows identifying two or more natural or legal persons who are so closely linked by idiosyncratic risk factors, that it is prudent to treat them as a single risk. Idiosyncratic risk arises where, because of specific circumstances of bilateral interrelationships, financial problems of one person are transferred to another person or persons that otherwise would not be concerned directly. Consequently, the purpose of these draft RTS is to set out clear circumstances where interconnections by means of a control and/or an economic dependency relationship lead to a single risk and thus a grouping requirement.

The draft RTS also set out legal provisions for the assessment of situations where control and economic dependencies coexist and thus one overall group of connected clients, as opposed to two or more separate groups of connected clients, needs to be formed.

Nevertheless, the draft RTS make clear that there might be exceptional situations where the institution can demonstrate to its competent authority that circumstances prevail that refute the existence of a single risk.

## Next steps

The final draft RTS will be submitted to the Commission for adoption. Following the submission, the RTS will be subject to scrutiny by the European Parliament and the Council before being published in the Official Journal of the European Union.

## 2. Background and rationale

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1. These draft RTS partially repeal and replace the EBA Guidelines ([EBA/GL/2017/15](#)) on connected clients under Article 4 paragraph 1 number 39 of the amended Capital Requirements Regulation (Regulation (EU) No 575/2013) (GL) published on 14 November 2017. These GL have been applicable to competent authorities and financial institutions since 1 January 2019.<sup>1</sup> Their objective was to provide clarity on the definition of connected clients as applicable from 2014 onwards. As of 18 March 2021, all EU competent authorities have declared compliance with these GL (see [guidelines compliance table](#)). The draft RTS take into account the experience gained by institutions as well as competent authorities through the application of the GL.
2. These draft RTS focus exclusively on the circumstances in which the conditions set out in Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013 to form a group of connected clients (GCC) are met. The draft RTS apply to all areas of that Regulation where the concept of a GCC is used – i.e., the large exposures regime (Part Four of that Regulation), the categorisation of clients in the retail exposure class for the purposes of credit risk (Article 123(c) and Article 147(5)(a)(ii)), the development and application of rating systems (Article 172(1)(d)), the criteria for STS securitisations qualifying for differentiated capital treatment (Article 243) and the SME supporting factor (Article 501(1)). The draft RTS also apply to EBA technical standards and EBA guidelines that refer to GCCs as defined in Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013, namely in the area of liquidity reporting, where this concept is used in the specification of items requiring stable funding that must be reported to the competent authorities (Article 428 paragraph 1 point (g)(ii) of that Regulation), and in the reporting of concentration of funding by counterparty and concentration of counterbalancing capacity by issuer/counterpart.
3. The objective of the definition of a GCC in Regulation (EU) No 575/2013 is to identify two or more natural or legal persons who are so closely linked by idiosyncratic risk factors that it is prudent to treat them as a single risk. Idiosyncratic risk represents the effect of risks that are specific to individual clients. Idiosyncratic risk arises where, in a bilateral interrelationship, financial problems of one person are transferred via this interrelationship to another person or persons that otherwise would not be concerned directly. Consequently, the purpose of the current GL (and thus also the draft RTS) is to clarify and operationalise the concept of interconnection – i.e., when a control and/or an economic dependency relationship should lead to the grouping of clients because they constitute a single risk in accordance with Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013.

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<sup>1</sup> The GL revised and replaced the 'Guidelines on the implementation of the revised large exposures regime' issued by CEBS on 11 December 2009.

4. Geographical and sectorial concentration risks fall outside the scope of these draft RTS and are addressed by other means, such as the risk management rules on concentration risk under Pillar 2. Geographical or sectorial risk can be defined as a dependency linked to an external factor (e.g., a certain product market or a specific region) that affects all entities active in the region or sector in the same manner. Institutions that only operate in a well-defined geographical area, or in an area dominated by one specific industry or sector, are not more affected in their conduct of business by the grouping requirement than other institutions.
5. Based on the current GL, the draft RTS shed light on when the criteria for the two types of interconnections – control and economic dependency as defined in Article 4 paragraph 1 number 39 points (a) and (b) respectively – are met. In particular, they provide guidance on how institutions shall identify GCCs following these two types of interconnections separately as well as when both conditions prevail.
6. Furthermore, the GL explain the alternative approach of grouping when the head of the group is the central government, as specified in the second subparagraph of the definition.
7. They also include a section on due diligence/governance expectations (control and management procedures for the identification of GCCs, documentation and review requirements). Clearly defined policies and procedures for determining GCCs and a diligent documentation of compliance with these policies and procedures (including a periodic review) is of crucial importance.
8. The main advantage of the GL is the possibility to have descriptive examples and illustrations of different grouping situations. Given the legal nature and formal requirements of RTS, such examples cannot be part of the legal text. However, for consultation purposes, all examples of the GL (and additional ones) were included in the background of this draft.

## 2.1 Legal mandate and approach retained

9. The Commission's Risk Reduction Measures Package, amending, inter alia, Regulation (EU) No 575/2013, includes new mandates for the EBA. Paragraph 4 of Article 4 mandates the EBA to:

*"[...] develop draft regulatory technical standards specifying in which circumstances the conditions set out in point (39) of paragraph 1 are met.*

*EBA shall submit those draft regulatory technical standards to the Commission by 28 June 2020."*

10. Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013 defines a GCC for the purposes of Regulation (EU) No 575/2013. The conditions set out therein refer to cases in which two or more natural or legal persons:
  - a. are directly or indirectly interconnected by a control relationship as defined in Article 4 paragraph 1 number 37 of that Regulation;

- b. are interconnected by some form of economic dependency as set out in Article 4 paragraph 1 number 39 point (b), so that, if one of them were to experience financial problems, in particular funding or repayment difficulties, the other or all of the others would also be likely to encounter funding or repayment difficulties.<sup>2</sup>
11. Those two conditions, which were already further elaborated on in the GL, allow identifying natural and/or legal persons so closely linked by idiosyncratic risk factors that it is prudent to treat them as a single risk. It has to be noted that the term “legal person” used in the RTS should be understood and applied to any entity other than a natural person irrespective of its national legal structure (also encompassing e.g. civil law associations). It applies also to cases where one or more natural or legal persons fall under the definition of shadow banking entities. If the reporting institution has exposures to two or more shadow banking entities that are not connected by idiosyncratic risk (i.e., neither by control nor economic dependency) then according to the EBA guidelines on limits on exposures to shadow banking entities ([EBA/GL/2015/15](#)) the institution has still to set an adequate aggregate limit to these exposures.<sup>3</sup>
12. Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013 provides two deviations from the grouping requirement: i) cases where the central government is the head of the group of connected clients and ii) cases of direct exposures to a central counterparty (CCP) for clearing activities purposes (the latter introduced by Regulation 2019/876 amending Regulation (EU) No 575/2013). As these are exemptions from the grouping requirement conclusively specified in level 1, they are not covered by the draft RTS (their inclusion would only result in a repetition of level 1 text).
13. The deadline included in Regulation (EU) No 575/2013 for the EBA to submit these draft RTS to the Commission was 28 June 2020. As reported in the [EBA Risk Reduction Package Roadmaps](#), published in November 2019, the EBA deemed it beneficial to allow institutions to gain sufficient experience with the application of the GL before their partial integration into the draft RTS. For this reason, the EBA is committed to submit these draft RTS to the Commission by December 2022.
14. The approach taken by the EBA in developing these draft RTS has been to leverage on the existing GL for the parts that fall under the mandate of the RTS, given that it is EBA’s understanding that the approach of the existing GL has not been challenged by the industry. In this vein, sections 4, 6 and 7 of the GL will be repealed as soon as the RTS will enter into force. The GL will be amended and stay in force, with its remaining content giving guidance on the alternative approach for exposures to central governments (Section 5) and control and management procedures for identifying connected clients (Section 8). In addition, the EBA deems it useful to maintain the illustrative examples that were provided in the GL also

<sup>2</sup> Instances where economic dependency can be assumed: i) direct economic dependencies such as supply chain links or dependence on large customers; or ii) a common main source of funding in the form of credit support, potential funding or direct, indirect or reciprocal financial assistance.

<sup>3</sup> According to the EBA guidelines on limits on exposures to shadow banking entities which carry out banking activities outside a regulated framework under Article 395(2) of Regulation (EU) No 575/2013 ([EBA/GL/2015/20](#)), institutions set limits, as part of their internal processes, on their individual exposures to shadow banking entities and on their aggregate exposure to shadow banking entities.

for the parts that are now transferred to the draft RTS, as they are deemed crucial for the understanding of the requirements but cannot be part of the legal text (see Section 2.4).

## 2.2 Identification of a group of connected clients

### 2.2.1 Control relationship

15. Section 4 of the GL provides guidance when the circumstances set out in Article 4 paragraph 1 number 39 point (a) of Regulation (EU) No 575/2013 are met. This section of the GL has been transposed into Article 1 of the draft RTS.
16. Where a control relationship as defined in Article 4 paragraph 1 number 37 of Regulation (EU) No 575/2013 exists, the controlling person/entity has legally enforceable rights that establish a strong form of financial dependency on the controlled person/entity by the controlling entity. In case of financial problems of the controlling entity, it can be assumed that it will make use of its rights to extract capital and/or liquidity from the controlled entity, thereby weakening the financial position of the latter. Thus, financial problems can be transferred to the controlled person/entity, with the result that both the controlling person/entity and the controlled one would experience financial problems ("domino effect"). From the perspective of prudential risk stemming from exposures to clients, it is therefore appropriate to attach the strong assumption of a single risk to a relationship of control between different natural and/or legal persons.
17. The definition of control in Article 4 paragraph 1 number 37 of Regulation (EU) No 575/2013 points to the definition of the relationship between a parent undertaking and a subsidiary, as defined in the Accounting Directive 2013/34/EU,<sup>4</sup> or to the accounting standards to which an institution is subject under Regulation (EC) No 1606/2002,<sup>5</sup> or to a similar relationship between any natural or legal person and an undertaking.
18. Where the Accounting Directive 2013/34/EU is applicable, it has an impact on the way institutions assess control relationships for the purposes of grouping connected clients. Taking into account that Article 22 paragraphs 1 and 2 of Directive 2013/34/EU establish several options and national discretions for Member States, the notion of a control relationship depends on the national transposition of the Directive.
19. For clients to which the EU accounting rules do not apply (e.g., natural persons, central governments and/or clients that prepare consolidated financial statements in accordance with the accounting rules of a third country), the draft RTS list circumstances that always

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<sup>4</sup> Directive 2013/34/EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEC and 83/349/EEC.

<sup>5</sup> Regulation (EC) No 1606/2002 of the European Parliament and of the Council of 19 July 2002 on the application of international accounting standards.

constitute a control relationship, and additionally provides a non-exhaustive list of indicators that institutions should use when assessing the control relationship.

20. A GCC shall be identified according to Article 4 paragraph 1 number 39 point (a) of Regulation (EU) No 575/2013 when it can be concluded that there is a control relationship among natural and/or legal persons (“control group”). As the definition of control presupposes a parent-subsidiary relationship, two legal persons that are subsidiaries of the same parent entity do not themselves control each other. However, when these legal persons are part of the same consolidated financial statements – i.e., controlled by the same natural and/or legal person; the condition in Article 4 paragraph 1 number 39 point (a) of Regulation (EU) No 575/2013 is still deemed to be met, even in the absence of exposures towards the natural or legal person that controls the group.
21. For cases where no consolidated financial statements have to be prepared, the draft RTS provide a non-exhaustive list of circumstances of control criteria and control indicators for the assessment if there is a parent-subsidiary-similar relationship among natural and/or legal persons. The two-segment-list contains circumstances that always constitute a control relationship among natural and/or legal persons and indicators that should be considered by institutions in their assessment, as any of these circumstances might constitute a control relationship among natural and/or legal persons.
22. The draft RTS also address the case of intragroup exposures – i.e., when the reporting institution is itself part of a control group (in other words: an institution that is owned/controlled by another institution and they are all part of a banking group that holds participations in both financial and non-financial entities). In these cases, the institution shall consider the existence of a single risk because the entities within its own group are again being part of the same consolidated financial statement.<sup>6</sup>
23. It is to be noted that Article 4 paragraph 1 number 39 point (a) of Regulation (EU) No 575/2013 foresees an exception that enables the institution to abstain from forming a group of connected clients when it can demonstrate that, despite the existence of a control relationship, those natural and/or legal persons do not constitute a single risk (see [Scenario C 1](#) in Section 2.4 below).
24. In any case, the assessment of a control relationship is only the first step in the assessment of the connections among natural and/or legal persons, which is done before assessing any potential economic dependency and possible interlinkages between control and economic dependency relationships.

### **2.2.2 Economic dependency**

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<sup>6</sup> Even though such types of exposures are likely to be fully or partially exempted – either via Article 400(1)(f), Article 400(2)(c), or Article 493(3)(c) of Regulation (EU) No 575/2013, and provided the counterparty concerned is covered by the supervision on a consolidated basis to which the institution itself is subject, it is necessary to assess the existence of a GCC in order to calculate the large exposure amount.



25. Section 6 of the GL provides guidance when the circumstances set out in Article 4 paragraph 1 number 39 point (b) of Regulation (EU) No 575/2013 are met. This section of the GL has been transposed in Article 2 of the draft RTS.
26. Even if the issue of control of one natural or legal person over another does not apply, institutions are obliged to assess whether there exists a relationship of economic dependency. If it is likely that the financial difficulties of one natural or legal person would spread to other(s) impacting full and timely repayment of liabilities, there exists an idiosyncratic risk that needs to be addressed by considering the natural and/or legal persons to be connected. An economic dependency among natural and/or legal persons thereby may be mutual or only one way (see Scenarios [E 1](#), [E 2](#), [E 3](#), [E 4](#), [E 6](#), [E 7](#) and [E 8](#) in Section 2.4 below).<sup>7</sup>
27. Dependency might arise in the context of business interconnections (e.g., supply chain links, dependence on large customers or counterparty exposures, financial dependency) that are not linked to sectorial or geographical risks, exposing the natural and/or legal persons involved to the same idiosyncratic risk factor. If this idiosyncratic risk materialises, one or both obligors are likely to experience repayment difficulties. Consequently, interconnections among entities (or persons) due to bilateral business relationships may lead to contagion risk that is independent of sectorial or geographical risks. The fact that the existence of common idiosyncratic risk factors may lead to contagion risk for otherwise unrelated natural and/or legal persons is at the core of the concept of economic interconnection.
28. In analysing economic dependencies, institutions should also consider the non-exhaustive list of situations in Article 2(1) of these draft RTS when assessing connections among shadow banking entities. Institutions should give due consideration to the fact that relationships between legal persons falling under the definition of shadow banking entities will most likely consist not of equity ties but rather of a different type of relationship – i.e., situations of de facto control or relationships characterised by contractual obligations, implicit support or potential reputational risk (e.g., sponsorship or even branding).
29. The rationale for the definition of economic interconnection is to identify channels of contagion stemming from economic dependencies that a natural or legal person cannot overcome without experiencing repayment difficulties. However, even if a natural or legal person is currently economically dependent on another person, it could still be possible for the entity to easily (i.e., in a timely manner without excessively increased costs) find a replacement or to compensate for any losses (or foregone profits) inflicted by the person in financial difficulties without experiencing own repayment difficulties. Coming to this conclusion, the institution does not need to consider these persons as a single risk.

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<sup>7</sup> Dependency might arise in the context of business interconnections (e.g., supply chain links, dependency on large customers or counterparty exposures, financial dependency) that are not linked to sectorial or geographical risks, and it suggests that the natural or legal persons involved are exposed to the same idiosyncratic risk factor.

30. Economic dependency may arise where funding problems of one natural or legal person are likely to spread to another on account of the same main funding source. This does not include cases where natural and/or legal persons get funding from the same market (e.g., the market for commercial paper) or where a common source of funding is due solely to the geographical location. Small and medium-sized corporates will, in many cases, not have the capacity or commercial incentive to have financial relationships with institutions other than their local bank, and, in addition, for most of them the personal relationship with their bank officer is the key to better financial services. This fact does not in itself justify regarding these natural and/or legal persons as interconnected, even though they have a common source of funding (potentially even the reporting institution itself). Such funding dependencies can normally be replaced (see Scenario E 5 in Section 2.4 below). In the same vein, natural and/or legal persons that depend on their existing source of funding because of their poor creditworthiness also do not belong to this category.
31. Institutions should also consider cases where the common source of funding is provided by the institution itself, its financial group or its connected parties<sup>8</sup> (see Scenarios [E 5](#) and [E 6](#) in Section 2.4 below) and cannot be replaced in a timely manner without excessively increased costs. Institutions should also assess any contagion or idiosyncratic risk that could emerge from the following situations:
- a. use of one funding entity (e.g., the same entity or conduit that cannot be easily replaced);
  - b. use of similar structures (e.g., where the entity has some liquidity support mechanisms provided by a sponsor and is allowed to draw on these when experiencing financial difficulties);
  - c. reliance on commitments from one source (e.g., guarantees or other potential fundings; credit support in structured transactions or non-committed liquidity facilities, including direct, indirect, or reciprocal financial assistance), taking into account its solvency, especially where there are maturity mismatches between the maturity of the underlying assets and the frequency of the refinancing needs.
32. Institutions are not required to actively collect information about whether their clients share an external common source of funding. However, institutions do need to take into account available information in this regard.
33. It shall be underlined that according to the GL, institutions are expected to strengthen their investigation of economic dependencies among their clients in all cases where the sum of all exposures to one individual client exceeds 5% of Tier 1 capital. Therefore, institutions should perform an extensive research of any type of “soft information” (e.g. other public

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<sup>8</sup> Recital 54 to Regulation (EU) No 575/2013 sets out that “In determining the existence of a group of connected clients and thus exposures constituting a single risk, it is also important to take into account risks arising from a common source of significant funding provided by the institution itself, its financial group or its connected parties.”

or private information available) that typically exists at the level of individual loan officers and relationship managers, even though such information goes beyond the institutions' clients.

### **2.2.3 Interrelation between control relationship and economic dependency**

34. Article 3 of the draft RTS incorporates section 7 of the GL and specifies the grouping requirement when both circumstances set out in Article 4 paragraph 1 number 39 points (a) and (b) of Regulation (EU) No 575/2013 are met; in particular, when a single risk between two or more natural and/or legal persons would lead to a chain of contagion ("domino effect"). The concepts of control and economic dependency are based on two different kinds of interconnection to be assessed separately. However, there are situations where these two types of dependencies are interlinked and could therefore co-exist within one GCC in such a way that all relevant natural and/or legal persons constitute a single risk. This happens when a GCC is first established based on a control relationship according to the legal provisions set out in Article 4 paragraph 1 number 39 point (a) of Regulation (EU) No 575/2013, and successively extended by another natural and/or legal person or a second GCC because of some form of economic dependency as set out in Article 4 paragraph 1 number 39 point (b) of Regulation (EU) No 575/2013. In their assessment, institutions should consider each case separately, i.e. identify the possible "domino effect" based on the individual circumstances (see Scenarios [C/E 1](#) to [C/E 4](#) as well as the "comprehensive group" of Scenario E 7 in Section 2.4 below).
35. The introductory wording of Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013, "any of the following", does not necessarily lead to two mutually exclusive grouping requirements. A control relationship establishes a very strong form of dependency among entities (control as legal dependency). Thus, it is also a manifestation of economic dependency and not a separate alternative. In addition, the wording "between whom there is no relationship of control" cannot be interpreted in a way that precludes the establishment of an overall GCC that includes both, economically dependent entities as well as controlled entities.
36. The chain of contagion leading to the possible default of some or all entities concerned is the relevant factor for the grouping, and needs to be assessed in each individual case.
37. Downstream contagion should be assumed when an entity is economically dependent on another client and is itself the head of a "control group" – i.e., a GCC formed on account of the existence of a control relationship in accordance with Article 4 paragraph 1 number 39 point (a) of Regulation (EU) No 575/2013. If the other client is part of a GCC, the control group of the economically dependent entity should then be included in the GCC to which the economic dependency relationship exists. The reason for this is that, to overcome its own pending payment difficulties, the economically dependent entity will most likely withdraw resources from controlled entities, thus extending the risk of contagion downstream (see [Scenario C/E 3](#) in Section 2.4 below).

38. On the other hand, upstream contagion of entities that control the economically dependent entity should be assumed only when the controlling entity is also economically dependent on the entity that constitutes the economic link between the two controlling groups (see [Scenario C/E 4](#) in Section 2.4 below).

## 2.3 Feedback from stock-take amongst competent authorities and industry representatives

39. To develop these draft RTS, the EBA conducted a stock-take amongst competent authorities (CAs) and industry representatives to gather information on past experiences, practical challenges and possible issues regarding the identification of GCCs based on the GL.
40. Overall, both the CAs and the industry representatives perceive that the GL are clear enough to allow their implementation by RTS. No significant changes or burdensome procedures related to the mapping and management of GCCs are expected. In contrast, both the CAs and the industry representatives are expecting a proportionate effort to integrate the RTS requirements in the institutions' internal systems. Most of the respondents recognized also that forming a GCC based on the application of control criteria is easier than establishing interconnectedness based on economic dependencies, as the latter is a more complex area which often depends on expert judgement and thus hampers the use of automated procedures.
41. Some respondents pointed out that more guidance is required for cases in which the reporting institution itself belongs to a GCC and cases in which for a given reporting reference date, the reporting institution does not have exposures to the head of a group, but has exposures to two or more of its subsidiaries. These two issues are currently addressed by the proposed paragraph 1 of Article 1, which sets out the legal provision for cases where the parent of a group prepares a consolidated financial statement, thus including all subsidiaries in a GCC. Another point raised was related to clarifications on the concept of "control relationship" when two or more natural persons are involved – i.e., family members, spouses or where other family ties prevail. Currently, these draft RTS set out legal provisions that apply also to natural persons, including those cases of family ties where these natural persons are legally or economically interlinked. Institutions should assess whether such ties may require forming a GCC. Therefore, these RTS cannot include a specific requirement for family ties as the case needs to be assessed individually.
42. More examples were asked also on how to manage situations of "joint control" – i.e., cases of partners owning 50% or 1/3 each. It has to be highlighted that following the feedback on the GL, it was already clarified that "joint control" does not constitute control within the meaning of Article 4(1)(37) of Regulation (EU) No 575/2013 but a form of economic dependency. [Scenario E 7](#) in Section 2.4 below provides more guidance in the case of two partners owning the same amount of shares, which could lead to a GCC because of economic dependencies. Similarly, clarifications were asked also on how to form a GCC when indirect control is performed through natural persons, concerted actions of minority shareholders, other major investors that are sleeping partners, typically passive investors

or empty shell companies. The EBA notes that, in these cases, institutions shall assess the GCC by considering the ultimate beneficiary owner of the control relationship through the circumstances listed in paragraphs 3 and 4 of Article 1.

43. In both the GL and these draft RTS, the term “significant part” is used in relation to a client’s gross receipts, expenditures, production-output, receivables and liabilities. In the stocktake it was pointed out that the inclusion of this term in the draft RTS could lead to different assessments by institutions. In LEX paragraph 10.16 a quantitative threshold of 50% or more is used instead. The EBA notes that following the consultation feedback received for both the GL in 2017 and these draft RTS, most respondents rejected such a quantitative threshold. It was argued that the interpretation of a “significant part” depends on the specific situation and might involve different percentages. However, while these draft RTS do not introduce such a quantitative threshold, institutions could use the 50% threshold envisaged in LEX 10.16 as a starting point for their investigation of a GCC when assessing the conditions set out in Article 2(1) points (c) to (e) of these draft RTS.
44. More guidance was required for mixed groups, which can include firms operating in several sectors (not only the banking sector). In this case, some respondents argued that the existence of a single risk, especially when the controlling entity is non-EU, might be challenged despite the existence of a chain of control. These draft RTS set out legal provisions that, when met, require forming a GCC. For example, if the parent undertaking consolidates the non-EU subsidiaries, the GCC shall include them; or, if the parent undertaking is established in a third country (i.e., non-EU), Article 1(3) and (4) requires forming a GCC when EU accounting rules do not apply to all entities, but a control relationship exists. Moreover, economic dependencies need to be always considered. This implies that where one natural or legal person experiences financial problems, in particular funding or repayment difficulties that could spill over to the other entities, a GCC shall be formed.
45. Respondents welcomed the provision in paragraph 37 of Section 8 of the GL, which requires institutions to strengthen their investigation on GCCs based on economic dependencies when exposures are above 5% of their Tier 1 Capital. This provision will remain within the GL as guidance for institutions and in order to facilitate the procedures of assessment and management of GCCs based on economic dependencies.
46. While [Scenario C 1](#) in Section 2.4 already provides an example for situations where a single risk does not exist, further guidance was suggested for situations where ring-fencing or bankruptcy remoteness for all borrowers would not result in a GCC. The EBA notes that in these cases institutions shall assess the necessity to form a GCC based on a case-by-case analysis. Situations where a single risk does not exist may also depend on the respective insolvency law of the Member State concerned.
47. Moreover, respondents asked for clarifications around the term “not easily replaceable”, which is used in Section 6 of the GL and is related to interconnectedness based on economic dependency. The draft RTS specify that an economic dependency should be considered when a relationship with a natural or legal person cannot be replaced in a timely manner

without excessively increased costs, thus having the potential to trigger funding or repayment difficulties.

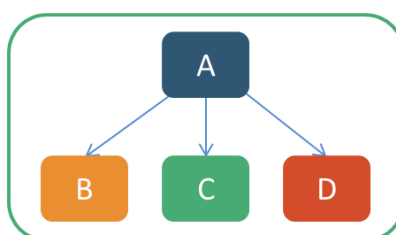
## 2.4 Illustration of scenarios in which the conditions set out in Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013 are met

48. The scenarios included in this section illustrate circumstances in which the conditions for GCCs set out in Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013 are (or are not) met, from the perspective of the reporting institution, for the provisions of the GL that were transferred to the RTS. The examples are unchanged compared to the ones of the existing GL. Three new examples have been added, one with regard to a simple control relationship (baseline scenario), a second with regard to the case of common ownership by two shareholders of three companies that both hold equally 50% of the shares in the respective companies, and a third with regard to the case of a horizontal group (Article 22 paragraph 7 of Directive 2013/34/EU). As the definition of a control relationship in Article 4 paragraph 1 number 39 point (a) relies on a parent-subsidiary-relationship, the example of a horizontal group is discussed under the heading of economic dependencies.

### 2.4.1 Groups of connected clients based on a control relationship

#### Scenario C 0: Baseline scenario “Control relationship”

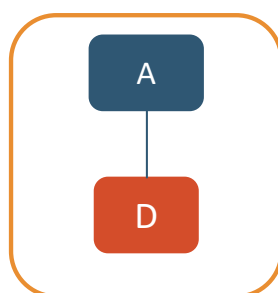
49. In the baseline scenario, the reporting institution has exposures to all entities shown below (A, B, C and D). The parent entity A prepares and publishes the consolidated financial statements according to IFRS, as legally required, including all three subsidiaries. The GCC thus encompasses all entities.



#### Scenario C 1: Exceptional case where no single risk exists despite the existence of a control relationship

50. The reporting institution has exposures to all entities as described in the baseline scenario C 0. Entity A has control over entities B, C and D. The subsidiaries B, C and D are special purpose entities/ special purpose vehicles (SPEs/SPVs).
51. To assess whether the assumption of a single risk can be refuted despite the existence of a control relationship, the reporting institution should assess at least all of the following elements in relation to each of the SPEs/SPVs (entities B, C and D in this scenario):

- i) The absence of economic interdependence or any other factors that could be indicative of a material positive correlation between the credit quality of the parent undertaking A and the credit quality of the SPE/SPV (B, C or D). Among other factors, the absence of a potential reliance on parent undertaking A for funding sources and circumstances of deconsolidation of the SPE/SPV under the applicable accounting rules have to be assessed as potential signs of economic independency.
  - ii) The specific nature of the SPE/SPV, especially its bankruptcy remoteness (based on Article 300 paragraph 1 of Regulation (EU) No 575/2013) – in the sense that effective arrangements exist that ensure that the assets of the SPE/SPV will not be available to the creditors of parent undertaking A in the event of its insolvency – and whether the debt securities issued by the SPE/SPV normally reference assets that are third parties' liabilities.
  - iii) The structural enhancement in a securitisation, and the de-linkage of the obligations of the SPE/SPV from those of parent undertaking A, such as the existence of provisions, in the transactions' documentation, ensuring servicing and operational continuity.
  - iv) The compliance with the provisions under Article 248 of Regulation (EU) No 575/2013 regarding arm's length conditions.
52. Having assessed all of these elements, the reporting institution could conclude that, for example, subsidiaries B and C do not constitute a single risk with parent undertaking A. As a result, the reporting institution would need to consider a GCC composed only of clients A and D. The institution should document these assessments and its findings in a conclusive way.

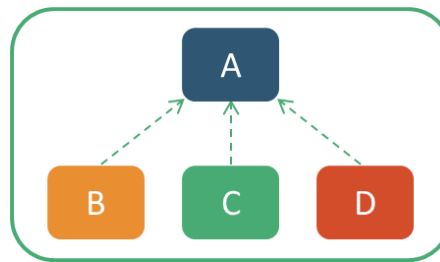


#### 2.4.2 Establishing interconnectedness based on economic dependency

##### Scenario E 1: Baseline scenario “Economic dependency”

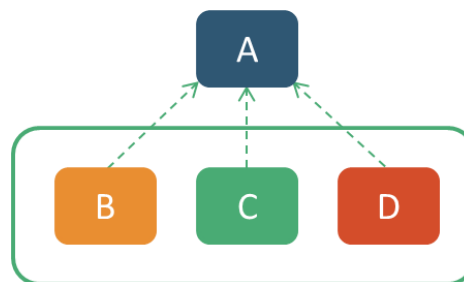
53. The reporting institution has exposures to all entities shown below (A, B, C and D). B, C and D rely economically on A. Hence, the underlying risk factor for the institution is in all cases A. The institution has to form one comprehensive group of connected clients, not three individual ones. It is irrelevant that there is no dependency among B, C and D.





### Scenario E 2: Variation on baseline scenario (no direct exposure to source of risk)

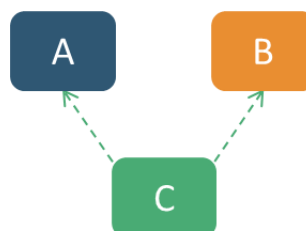
54. There is a grouping requirement even if the reporting institution does not have a direct exposure to A but is aware of the economic dependency of each client (B, C and D) on A. Potential payment difficulties of A would be contagious to B, C and D, i.e. they would all experience payment difficulties, if A gets into financial trouble. Therefore, they need to be treated as a single risk.



55. As in scenario E 1, it does not matter that there is no dependency among B, C and D. A causes the grouping requirement, although it is not a client of the reporting institution.

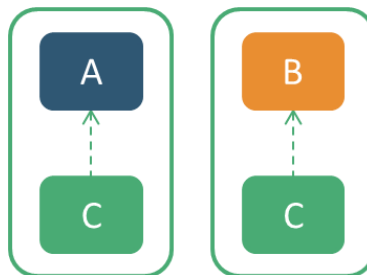
### Scenario E 3: Overlapping groups of connected clients

56. If an entity is economically dependent on two (or more) other entities, it has to be included in the GCCs of both (all such) entities. Note that the payment difficulties of one of the other entities (A or B) might be sufficient to result in C being in difficulty. Also, given that neither A nor B are economically dependent on C, any difficulties of A will not be passed on to B and vice-versa, C has to be included in the GCCs of both (all such) entities:





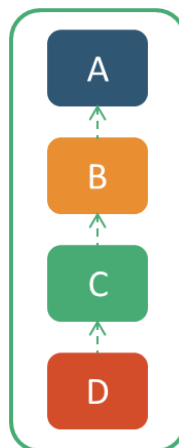
#### Grouping requirements:



57. The argument that the exposure to C will be counted twice is not relevant under the large exposure regime, because the exposure to C is considered a single risk in two separate groups. The large exposure limit applies separately (i.e. the limit applies once to exposures to group A/C and once to exposures to group B/C). As there is no dependency between A and B, no comprehensive group (A + B + C) needs to be formed in this example.

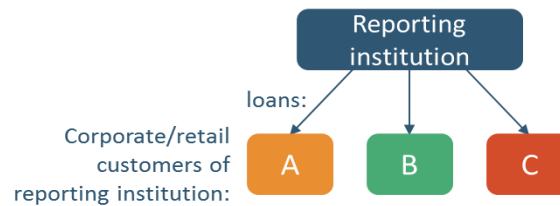
#### Scenario E 4: Chain of dependency

58. In the case of a “chain of dependency”, all entities that are economically dependent (even if the dependency is only one way) need to be treated as one single risk. It would not be appropriate to form three individual groups (A + B, B + C, C + D).



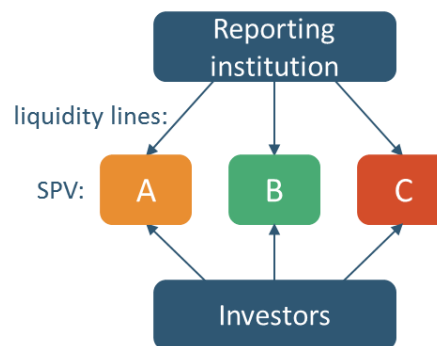
#### Scenario E 5: Reporting institution as source of funding (no grouping requirement)

59. In the following scenario, the reporting institution is the sole provider of funds for three customers. It is not an “external funding source” that connects the three clients and it is a funding source that can be replaced in a timely manner without excessively increased costs. Thus, no GCC needs to be formed.

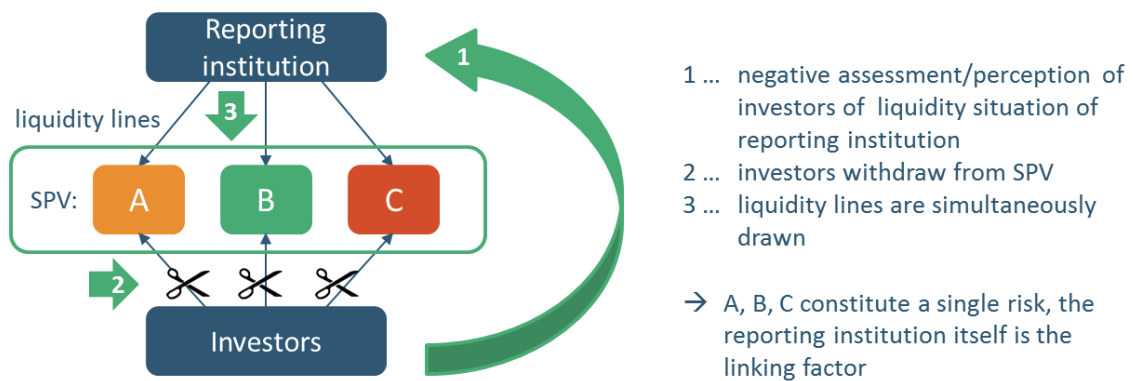


### Scenario E 6: Reporting institution as source of funding (grouping requirement)

60. In the following scenario, the reporting institution is the liquidity provider of three SPVs or conduits (similar structures):



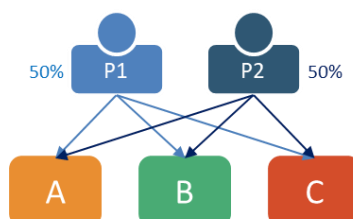
61. In such a case, the reporting institution itself can constitute the source of risk (the underlying risk factor) as recognised in recital 54 to Regulation (EU) No 575/2013 leading to a concerted action of investors:



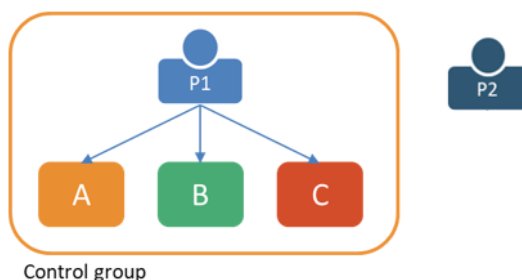
62. In the scenario above, it does not make a difference whether the liquidity lines are directly to the SPV or to the underlying assets within the SPV; what matters is the fact that liquidity lines are likely to be drawn on simultaneously. Diversification and quality of the assets are also not considered in this scenario, nor is the reliance on investors in the same sector (e.g. investors in the ABCP market), as the single risk is created by the use of similar structures and the reliance on commitments from one source (i.e., the reporting institution as the originator and sponsor of the SPVs).

### Scenario E 7: Case of common ownership by two shareholders of three companies that both hold equally 50% of the shares in the respective companies

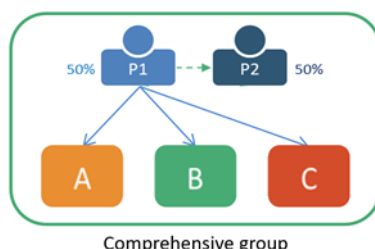
63. In the following scenario, the reporting institution has exposures to three entities (A, B and C) and to their two shareholders (P1 and P2), who own the same amount of shares (i.e., 50/50) of each of the entities.



64. In such a situation, institutions should first assess if one of the two shareholders can exercise a significant influence on the entities concerned. If this is the case (for example P1), a single group comprising of the shareholder that exercises a dominant influence and the entities concerned needs to be formed (in this case, P1 + A + B + C). This would be a case of a control group and the only grouping requirement provided there are no other connections leading to a single risk (e.g., adequate ring-fencing for P2).<sup>9</sup>



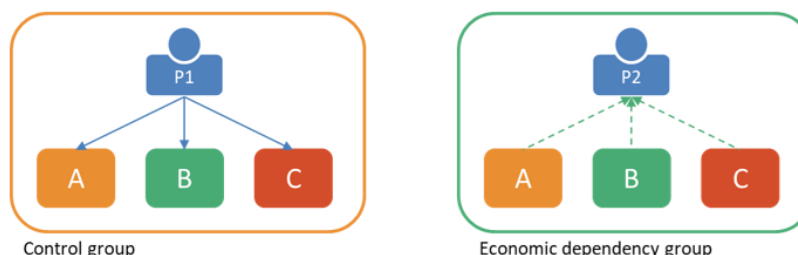
65. Secondly, the reporting institution needs to assess any economic dependencies between the persons concerned. If it cannot be ruled out that there is an economic dependency between P1 and P2, as pictured in the chart, in this case with financial difficulties that could spread from P2 to P1, a single comprehensive group (A + B + C + P1 + P2) needs to be formed (with no separate control or economic dependency groups).



66. In contrast, if it can be demonstrated that P1 and P2 are adequately ring-fenced and/or independent, after forming the control group, the reporting institution has still to assess

<sup>9</sup> Where a shareholder owns less than 50% but still holds a significant stake and has the ability to exercise a dominant influence, institutions need to assess the grouping requirements on the basis of a case-by-case analysis.

whether other economic dependencies could prevail – e.g., whether financial difficulties of the other shareholder (P2) could spread to A, B and C. If this is the case, an economic dependency group comprising of the shareholder that could trigger funding or repayment difficulties and the entities concerned needs to be formed (in this case, P2 + A + B + C) in addition to the control group of P1. There may be also other cases of economic dependencies that would require other grouping solutions.



#### Scenario E 8: Case of horizontal group by means of economic dependencies within the meaning of paragraph 7 of Article 22 of Directive 2013/34/EU

67. In the following scenario, the reporting institution has exposures to three entities (A, B and C), which are managed on a unified basis within the meaning of point a of paragraph 7 of Article 22 of Directive 2013/34/EU. The reporting institution needs to assess any economic dependencies between the three entities (A, B and C). If it cannot be ruled out that there are economic dependencies between A, B and C with financial difficulties affecting all three entities (A, B and C), a single group comprising of the entities concerned needs to be formed (in this case, A + B + C) – see Article 2(1)(i) of these draft RTS.

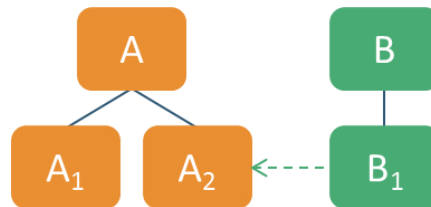


68. There might be other cases of horizontal groups which need to be assessed: e.g. when the reporting institution has exposures to entities having their management body composed for a major part of the same persons within the meaning of point b of paragraph 7 of Article 22 of Directive 2013/34/EU (see Article 2(1)(j) of these draft RTS) or having the same persons holding the majority of voting rights, when they act in a concerted way – e.g., situations of natural persons with family ties; even in cases where these persons are not part of the same management body (see Article 2(1)(k) of these draft RTS).

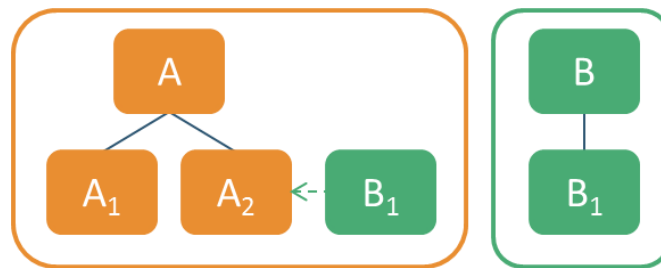
#### 2.4.3 Relation between interconnectedness through control and interconnectedness through economic dependency

#### Scenario C/E 1: Combined occurrence of control and economic dependency (one-way dependency)

69. In the following scenario, the reporting institution has exposures to all entities shown in the diagram below. A controls  $A_1$  and  $A_2$ , B controls  $B_1$ . Furthermore,  $B_1$  is economically dependent on  $A_2$  (one-way dependency):



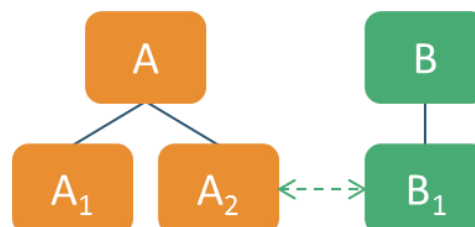
70. In this scenario, the reporting institution should come to the conclusion that  $B_1$  is in any case to be included in the group of connected clients of A (the group thus consisting of A,  $A_1$ ,  $A_2$  and  $B_1$ ) as well as of B (the group thus consisting of B and  $B_1$ ):



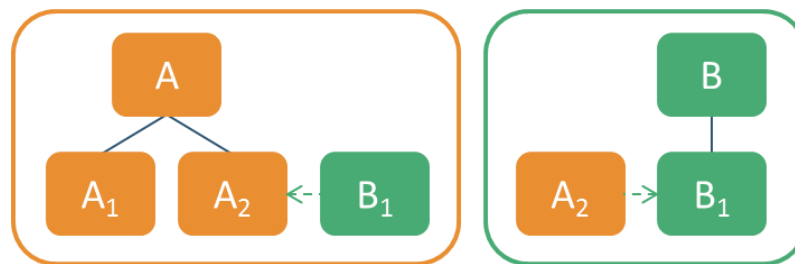
71. In case of financial problems of A,  $A_2$  and ultimately  $B_1$  will also experience financial difficulties on account of their legal ( $A_2$ ) and economic ( $B_1$ ) dependency respectively. The forming of three different groups (A +  $A_1$  +  $A_2$ ,  $A_2$  +  $B_1$ , B +  $B_1$ ) would not be sufficient to capture the risk stemming from A, because  $B_1$ , although dependent on  $A_2$  and thus on A itself, would be carved out of the single risk of group A.

### Scenario C/E 2: Combined occurrence of control and economic dependency (two-way dependency)

72. In this scenario, the economic dependency of  $A_2$  and  $B_1$  is not only one way but mutual:

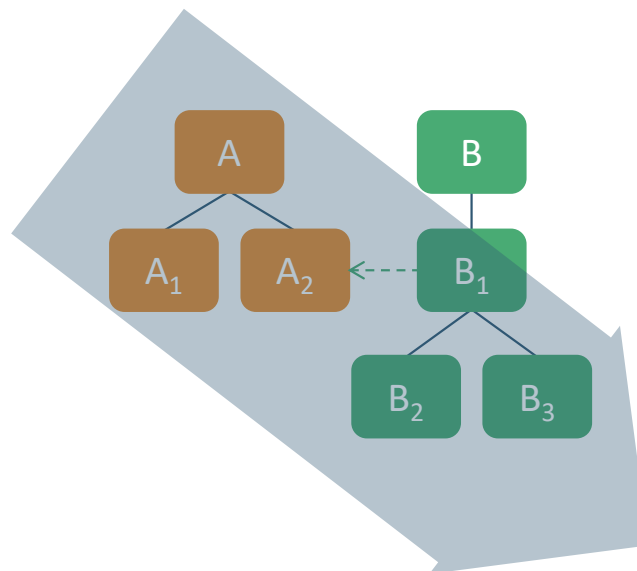


73.  $A_2$  would need to be included additionally in group B, and  $B_1$  would need to be included additionally in group A:

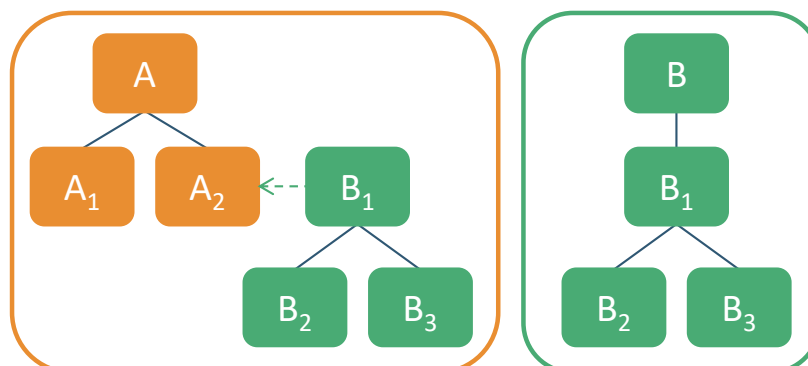


### Scenario C/E 3: Downstream contagion

74. In a variation on scenario C/E 1 above, B<sub>1</sub> also controls two entities (B<sub>2</sub> and B<sub>3</sub>). In this case, the financial difficulties of A will pass through A<sub>2</sub> and B<sub>1</sub> down to the two subsidiaries of B<sub>1</sub> (“downstream contagion”).

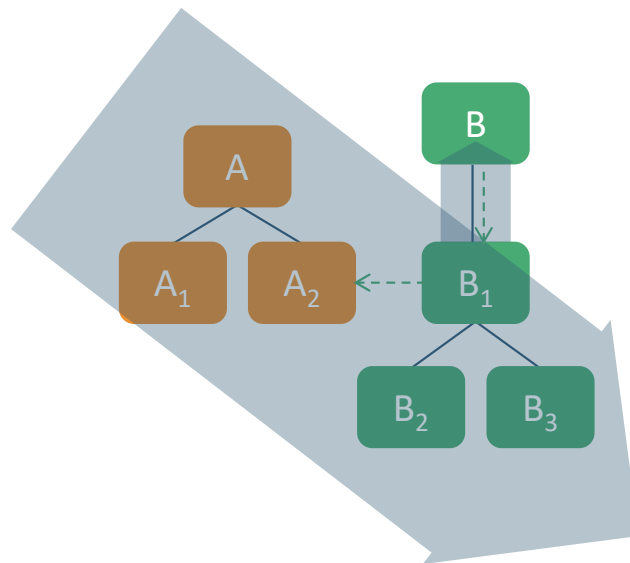


75. In this scenario, the grouping requirement shall be as illustrated below:

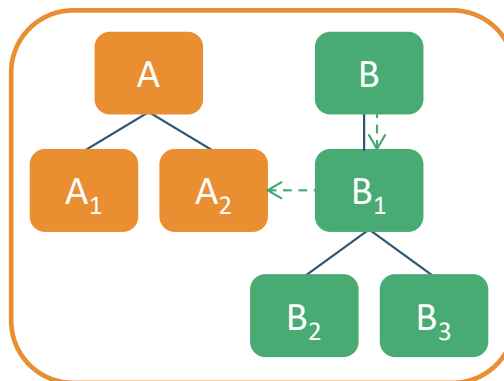


### Scenario C/E 4: Upstream contagion

76. The control relationship between B and B<sub>1</sub> does not automatically lead to including B in the group of connected clients of A, as financial problems for A might not necessarily result in financial difficulties for B. However, the controlling entity B needs to be included in the group of A, if B<sub>1</sub> forms such an important part of group B that B is economically dependent on B<sub>1</sub>. In this case, the financial difficulties of A will proceed not only downwards but also upwards to B, causing payment difficulties for B (i.e., all entities now form a single risk).



77. In this scenario, the grouping requirement shall be as illustrated below:



### 3. Draft regulatory technical standards

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## COMMISSION DELEGATED REGULATION (EU) .../...

of **XXX**

**supplementing Regulation (EU) No 575/2013 of the European Parliament and of the Council with regard to regulatory technical standards for specifying in which circumstances the conditions set out in Article 4 paragraph 1 point (39) of Regulation (EU) No 575/2013 are met**

THE EUROPEAN COMMISSION,

Having regard to the Treaty on the Functioning of the European Union,

Having regard to Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012,<sup>10</sup> and in particular Article 4 paragraph 4 thereof,

Whereas:

- (1) Under the large exposures framework quantitative limits are established to limit the maximum loss an institution can incur from the failure of a client or a group of connected clients. When a number of natural or legal persons are connected with specific relationships and dependencies in a way that a failure of one of the connected persons could lead to cascading failures of the rest they need to be treated as a single risk. This Regulation specifies in which circumstances the conditions set out in Article 4, paragraph 1, point (39) of Regulation (EU) No 575/2013 are met.
- (2) Identifying ‘groups of connected clients’ as per Regulation (EU) No 575/2013 should lead to identify natural or legal persons so closely linked by idiosyncratic risk factors that it is prudent to treat them as a single risk. When it is unclear under which specific category of connections under this Regulation the interconnection between different persons should be classified, a general principle of prudence should prevail leading to the assumption of the existence of a single risk and, accordingly, the circumstances listed under Articles 1 and 2 of this Regulation should be understood as non-exhaustive lists. This should not include cases where natural and/or legal persons are only linked through their dependance to common geographical or sectoral external factors.
- (3) To clarify the circumstances under which the condition of control is met for the purposes of identifying the existence of a single risk, it should be set out in this Regulation that, when two or more legal persons are part of the same financial consolidated statement, the condition of control should be deemed as met, even in the absence of exposures towards the natural or legal person that controls the group.

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<sup>10</sup> OJ L 176 27.6.2013, p. 1.

- (4) There is a need to lay down in this Regulation the circumstances, in which a single risk among one or more natural or legal persons on the basis of control exists, even when consolidated financial statements are not being prepared, either because natural persons are involved, or because the legal persons are established in a third country or the legal regime applicable to these persons does not require financial consolidation. In particular, when the natural or legal person holds the majority of voting rights, or has the ability to appoint or remove the majority of the management body or exercises a dominant influence over another person, the conditions of control should be deemed as met.
- (5) In addition, this Regulation should also specify further circumstances in which two or more natural or legal persons may constitute a single risk because one of them, directly or indirectly, has control over the other or others. In particular, where the natural or legal person has the right or ability to decide on the strategy or on important transactions of another person, or has the right or ability to coordinate the management of a person with that of other persons, these circumstances could be seen as having a dominant influence and thus meeting the conditions for a single risk on the basis of control.
- (6) This Regulation should specify those circumstances that at least should be considered when assessing economic dependency for the purpose of determining a single risk. This should not prevent institutions and competent authorities from considering further circumstances, not specifically foreseen by this Regulation. To that end, this Regulation sets out a non-exhaustive list of such circumstances. Economic dependency requires that the relationship with a natural or legal person has the potential to trigger funding or repayment difficulties and cannot be replaced in a timely manner without excessively increased costs – i.e., costs or reduced revenues that could trigger repayment difficulties.
- (7) Furthermore, this Regulation should lay down the circumstances in which the conditions of control and economic dependency coexist. For this purpose, when two or more natural or legal persons constitute a single risk on the basis of control and one or more of them are so closely interlinked and interdependent with another natural or legal person or persons that they are economically dependent, all these persons constitute an overall single risk. When assessing the coexistence of control and economic dependency, institutions should consider each case separately, considering the possible connections based on individual circumstances. Where persons that are part of different control groups are also interconnected via economic dependency, all of these persons need to be grouped into one overall group of connected clients (encompassing the control group, any economically dependent person or persons and any person or persons being controlled by the latter).
- (8) This Regulation should take into account the possibility that the existence of exceptional circumstances might preclude the existence of a single risk. To that end, an institution should be in a position to present adequate evidence, despite conditions of this Regulation being met among two or more natural or legal persons, for these persons to not being treated as a group of connected clients.

- (9) This Regulation is based on the draft regulatory technical standards submitted to the Commission by the European Banking Authority and builds upon the consistent approaches already developed in the EBA Guidelines 2017/15 of 14 November 2017 as regards the implementation of Article 4(1)(39) of Regulation (EU) No 575/2013. Together with the guidance for the alternative approach for exposures to central governments and for the control and management procedures for identifying clients that constitute a single risk included in these Guidelines, it provides the complete framework for the identification of groups of connected clients.
- (10) The European Banking Authority has conducted open public consultations on the draft regulatory technical standards on which this Regulation is based, analysed the potential related costs and benefits and requested the advice of the Banking Stakeholder Group established in accordance with Article 37 of Regulation (EU) No 1093/2010 of the European Parliament and of the Council,<sup>11</sup>

HAS ADOPTED THIS REGULATION:

### *Article 1*

#### *Control relationship*

1. Two or more natural or legal persons shall constitute a single risk because one of them, directly or indirectly, has control over the other or others, and one of them is required to prepare consolidated financial statements including the other or others in accordance with paragraphs 1 and 2 of Article 22 of Directive 2013/34/EU or the International Financial Reporting Standard (IFRS) 10, as laid down in the national law of the respective Member State.
2. Paragraph 1 shall apply also to legal persons not included in the consolidated financial statements due to exemptions or derogations set out in the Directive 2013/34/EU or the IFRS, as laid down in the national law of the respective Member State.
3. When paragraph 1 does not apply, two or more natural or legal persons shall constitute a single risk because one of them, directly or indirectly, has control over the other or others, in the following circumstances:
  - (a) the natural or legal person holds the majority of the voting rights in another person or persons;
  - (b) the natural or legal person has the right or the ability to appoint or remove the majority of the members of the administrative, management or supervisory body of another person or persons;

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<sup>11</sup> Regulation (EU) No 1093/2010 of the European Parliament and of the Council of 24 November 2010 establishing a European Supervisory Authority (European Banking Authority), amending Decision No 716/2009/EC and repealing Commission Decision 2009/78/EC (OJ L 331, 15.12.2010, p. 12).

- (c) the natural or legal person is in a position to exercise dominant influence over another person or persons pursuant to a law or contract, or provisions in memoranda or articles of association.
- 4. When paragraphs 1, 2 or 3 do not apply, two or more natural or legal persons may be deemed to constitute a single risk because one of them, directly or indirectly, has control over the other or others, in any of, but not limited to, the following circumstances:
  - (a) the natural or legal person has the right or ability to decide on the strategy or to direct the activities of another person or persons;
  - (b) the natural or legal person has the right or ability to decide on important transactions, such as the transfer of profits or losses of another person or persons;
  - (c) the natural or legal person has the right or ability to coordinate the management of one or more legal persons.
- 5. In exceptional cases, where an institution is able to demonstrate that no single risk prevails despite the circumstances of paragraphs 1, 2 or 3 of this Article being met with regard to two or more natural or legal persons, these persons need not be treated as a group of connected clients.

## *Article 2*

### *Economic dependency*

- 1. Two or more natural or legal persons constitute a single risk because they are interconnected in a way that, where one of them were to experience financial problems, in particular funding or repayment difficulties, the other, or the others would also be likely to encounter financial problems, in any of, but not limited to the following circumstances:
  - (a) where the insolvency or default of a natural or legal person is likely to result in the insolvency or default of another natural or legal person or persons;
  - (b) where a natural or legal person has fully or partly guaranteed the exposure of another natural or legal person and the exposure is so significant for the guarantor that the guarantor is likely to experience financial problems if a claim occurs;
  - (c) where a significant part of a natural or legal person's gross receipts or gross expenditures is derived from transactions with another natural or legal person that cannot be replaced in a timely manner without excessively increased costs;
  - (d) where a significant part of the goods produced or services offered by a natural or legal person is sold or supplied to another natural or legal person and that relationship cannot be replaced in a timely manner without excessively increased costs;

- (e) where a significant part of the receivables or liabilities of a natural or legal person is to another natural or legal person;
  - (f) where the expected source of funds to repay the loans of two or more natural or legal persons is the same and none of these persons has another independent source of income from which the loan may be serviced and fully repaid, and the expected source of funds cannot be replaced in a timely manner without excessively increased costs;
  - (g) where it is expected that the financial problems of one natural or legal person would cause difficulties for another natural or legal person to fully and timely repay its liabilities, because the persons are legally or contractually jointly liable to the institution;
  - (h) where two or more natural or legal persons rely on the same source for the majority of their funding and, in the event of insolvency or default of that source of funding, that source of funding cannot be replaced in a timely manner without excessively increased costs;
  - (i) where two or more legal persons are managed on a unified basis within the meaning of point (a) of paragraph 7 of Article 22 of Directive 2013/34/EU;
  - (j) where the management body of two or more legal persons consists for a major part of the same persons within the meaning of point (b) of paragraph 7 of Article 22 of Directive 2013/34/EU;
  - (k) where the majority of voting rights in two or more legal persons are held by the same natural or legal persons.
2. In exceptional cases, where an institution is able to demonstrate that no single risk prevails despite one or more of the circumstances of this Article being met with regard to two or more natural or legal persons, these persons need not be treated as a group of connected clients.

### *Article 3*

#### *Combined existence of control relationships and economic dependencies*

1. Without prejudice to Article 1 paragraph 5 and Article 2 paragraph 2, three or more natural or legal persons shall constitute a single risk, when two or more of these persons constitute a single risk by means of control in accordance with Article 1 (control group) and one or more natural or legal persons are connected to one or more of the persons being part of the control group by means of economic dependency in accordance with Article 2.
2. Where the person that is connected by means of economic dependency as referred to in paragraph 1 is part of another group of connected clients, all persons, either being controlled by that economically dependent person or being themselves economically dependent on that person, shall also constitute a single risk with the persons of the control group as referred to in paragraph 1.

3. In exceptional cases, where an institution is able to demonstrate that no single risk prevails despite the circumstances of this Article being met with regard to three or more natural or legal persons, these persons need not be treated as a group of connected clients.

*Article 4*

*Entry into force*

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

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

Done at Brussels,

*For the Commission*  
*The President*

*[For the Commission*  
*On behalf of the President*  
*[Position]*

## 4. Accompanying documents

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### 4.1 Draft cost-benefit analysis / impact assessment

1. These draft RTS revise and partially replace the EBA GL ([EBA/GL/2017/15](#)) on the identification of GCCs under Article 4 paragraph 1 number 39 of amended Regulation (EU) No 575/2013. These GL have been applicable to competent authorities and financial institutions since 1 January 2019. The draft RTS take into account the experience gained by institutions as well as competent authorities through the application of the GL.
2. To develop these draft RTS, the EBA conducted a stock-take amongst NCAs and industry representatives to gather information on past experiences, practical challenges and possible issues regarding the identification of GCCs based on the GL. Overall, both the NCAs and the industry representatives perceive that the GL are clear enough to allow their implementation in form of RTS.
3. The present analysis provides the reader with an overview of the findings as regards problem identification, possible options to address them and their potential impacts. Given the nature and the scope of the RTS, and pursuant to the principle of proportionality, this analysis is high-level and qualitative in nature. Only a qualitative analysis is provided with regard to the potential impact of the options; a quantitative analysis is presented with the aim to provide information on the materiality of the phenomena discussed.
4. The qualitative analysis presents the advantages and disadvantages of different options. Moreover, the quantitative analysis relies on information available through the Supervisory Reporting Templates (i.e., COREP). This way, it was not necessary to collect information from NCAs or directly from the institutions.<sup>12</sup>

#### A. Problem identification and baseline scenario

5. The Large Exposures framework acts as a backstop to limit: i) institution's losses; and ii), the impact that the default of a substantial exposure could have on the stability of an institution and the banking sector in the Union. With the aim to mitigate contagion effects due to persons so interconnected that the financial difficulties of one of them could translate in funding or payment problems for the others, the Large Exposures limits apply not only to single clients, but also to groups of connected clients, which need to be formed in case of a control or economic dependency relationships or when both grouping requirements prevail.
6. According to Article 4 paragraph 1 number 39 of Regulation (EU) No 575/2013, two or more natural or legal persons constitute a single risk because of connections between them based

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<sup>12</sup> Making ad hoc data collections is a costly and time-consuming process. For this reason, it is preferable, whenever it is possible to exploit data that are readily available from statistical agencies and databases.



on a control or an economic dependency relationship. Institutions are required to identify such connections when assessing their clients for the application of the Large Exposures framework. However, this definition needs to be complemented with the draft RTS that define the circumstances in which two or more natural or legal persons shall constitute a single risk.

## B. Policy objectives

7. The concept of a GCC is relevant not only for the application of the Large Exposures regime but also to other areas of that Regulation, namely the categorisation of clients in the retail exposure class for the purposes of credit risk (Articles 123 first subparagraph point (c) and 147 paragraph 5 point (a)(ii)), the development and application of rating systems (Article 172 paragraph 1 point (d)), the criteria for STS securitisations qualifying for differentiated capital treatment (Article 243), the specification of items requiring stable funding for reporting purposes (Article 428 paragraph 1 point (g)(ii)) and the SME supporting factor (Article 501 paragraph 1). Moreover, the concept of GCCs is also referred to in the area of liquidity reporting.
8. To ensure a prudent and harmonized application by institutions in the Union of all requirements of the Prudential Regulation referring to GCCs, an “operational” definition of the circumstances where a GCC shall be formed appears necessary.

### Qualitative Analysis

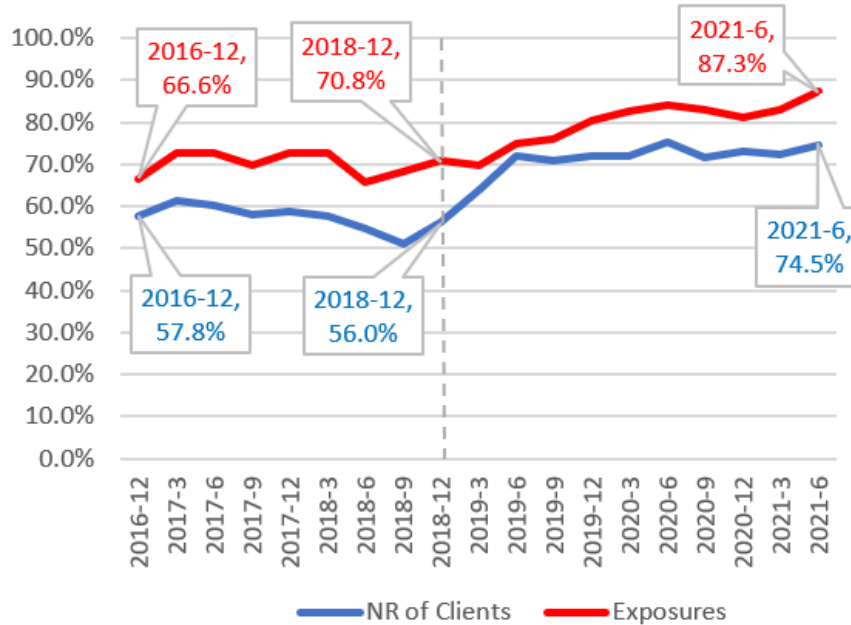
9. These RTS have been preceded by the publication of GL, which allowed to leverage on the experiences accumulated by institutions so far. On the basis of the stock-take conducted by the EBA, it emerged that both the NCAs and the industry representatives perceive the GL as sufficiently clear to allow their implementation by RTS. No significant changes of the procedures related to the mapping and management of GCCs are expected as a consequence.

### Quantitative Analysis

10. According to Article 394 of Regulation (EU) No 575/2013, institutions are required to report on a quarterly basis detailed information about their large exposures.
11. Figure 1 shows the share of clients reported as GCCs, and the relative share of total exposures stemming from them. This figure is based on data from over 200 banks reporting at the highest level of consolidation. Until end-2018, the relative importance of GCCs was constant as % of total reported clients and as % of total exposures. From 2019 (year of entering into force of the GL), an increasing trend can be observed for both ratios. This could be justified by the increased commitment by the institutions to identify interconnected clients.



*Figure 1: Relative share of reported clients with economic connections and relative total exposures associated with these clients.*



Source: COREP C.28 and C.29.

### Scope of application

12. The main options considered regarding the scope of application are the following:
  - (a) No action;
  - (b) Development and publication of a list of GCCs; and
  - (c) Development of RTS for the identification of the GCCs (complemented by GL).
13. As regard the first point – i.e. the typical “zero” option; it should be taken into consideration whenever the costs of the proposed regulation is deemed higher than its benefits. In this specific case, the correct and homogeneous identification of GCCs appears as key element of the application of several provisions in Regulation (EU) No 575/2013.
14. The definition and maintenance of a list of GCCs at the European level could shape considerable costs for both the Regulator and the institutions. Indeed, a detailed data collection at client level would be needed. In any case, the identification of the economic connections between the customers of a bank when made by a party external to the bank would hardly be complete given the importance of soft information that are not generally available.
15. Conversely, the GL and the draft RTS do not impose structural costs, like additional reporting requirements, but set some common principles that help to increase the harmonization among EU institutions.

### Preferred option

Considering both the possible materiality of losses stemming from large exposures and the need to ensure a harmonized application of the Regulation across EU institutions, it is deemed that the benefits of the RTS outweigh the costs. Furthermore, in this specific circumstance, the fact that the RTS have been preceded by the publication of GL, enables to verify ex-post the effectiveness of this initiative, with Figure 1 showing that after the publication of the GL, institutions started to pay more attention to the identification of GCCs.

## 4.2 Feedback on the public consultation

The EBA publicly consulted on these draft technical standards.

The consultation period lasted for 3 months and ended on 8 September 2022. Thirteen responses were received, of which ten on a non-confidential basis that were all published on the [EBA website](#).

This paper presents a summary of the key points and other comments arising from the consultation, the analysis and discussion triggered by these comments and the actions taken to address them if deemed necessary.

In many cases, several industry bodies made similar comments, or the same body repeated its comments in its response to different questions. In such cases, the comments and the EBA's analysis are included in the section of this paper where the EBA considers them most appropriate.

Changes to the draft RTS have been incorporated as a result of the responses received during the public consultation.

### Summary of key issues and the EBA's response

Overall, the respondents agreed in general with the principles underlying these draft RTS. In particular, the respondents supported the policy choices taken in the draft RTS, while suggesting minor amendments to align the content of these draft RTS with the current guidelines on connected clients under Article 4(1)(39) of Regulation (EU) No 575/2013 (GL), which are already implemented by institutions in their IT systems.

There was strong support by the respondents for the proposed approaches to identifying groups of connected clients (GCC), which do not lead to significant changes or burdensome procedures related to the mapping and management of GCCs compared to the GL.

Some respondents pointed out that there might be cases in which economic dependencies exist because: i) the majority of the members of the management body are joint in several persons as per Article 22(7)(b) of directive 2013/34/EU; or, ii) the same natural or legal persons hold the majority of voting rights in two or more legal persons, without being necessarily part of the management body. These two cases have been addressed in points (j) and (k) of Article 2(1) of these draft RTS.

Finally, some technical issues were raised in response to the questions in the Consultation Paper.

### EBA response

The EBA welcomes the support for these draft RTS and agrees that it is important to ensure consistency, where possible, between these draft RTS and the GL.

These draft RTS need to be submitted to the Commission for adoption. Following submission, the RTS will be subject to scrutiny by the European Parliament and the Council before being published in the Official Journal of the European Union and coming into force in the EU. The EBA believes this timeframe provides institutions with sufficient time to implement the draft RTS.

A more detailed presentation of the comments received and of the EBA response is included in the table set out below.

## Summary of responses to the consultation and the EBA analysis

| Comments   | Summary of responses received   | EBA analysis  | Amendments to the proposals |
|--|---|---|-----------------------------|
| <b>General comments</b>                          |   |   |                             |
| <b>Additional clarification for Scenario E 2</b> | One respondent asked for additional explanation on Scenario E 2. In their view, it is not clear what happens when there is only one client of the reporting institution with economic dependency on a non-client.   | The EBA notes that Scenario E 2 remains unchanged compared to the one of the existing EBA GL (EBA/GL/2017/15) and therefore is not part of the consultation process of this RTS. In any case, as also pointed out in <a href="#">Q&amp;A 2019 4525</a> “[...] <i>an institution has to report its large exposures to individual clients and to groups of connected clients (GCC). However, this requires that the institution currently has an exposure to the individual client which itself is a large exposure or which becomes a large exposure by adding together all the exposures to individual clients in a group of connected clients. Members of a group of connected clients to whom the institution does not have any current exposures are not to be reported. [...]</i> ” | No amendments.              |
| <b>Scope of application</b>                      | One respondent deems that there is no extensive elaboration on how the “consolidated” large exposure rules can also be applied on an individual basis toward subsidiaries and if this is the case, what issues emerge when looking at the GCC.<br><br>With regard to intra-group exposures, three respondents consider that it could be useful to add a separate section on how to apply the connectedness at the individual level taking into account the particularities of intra-group situations and relations, instead of applying the consolidated approach to the solo level on a 1:1 basis. | The EBA reiterates that the large exposure framework set out in Regulation (EU) No. 575/2013 (CRR) applies to all institutions as defined in Article 4(3) of the same Regulation. This entails that large exposure limits to single counterparties and GCCs apply to both consolidated and solo institutions.<br><br>As regard intra-group exposures, the EBA underlines that these draft RTS have to be applied to all types of exposure, with no differentiation between intra-group and third-party exposures.<br><br>Finally, these draft RTS address also the case of intragroup exposures, which shall be considered by the institutions as a single risk because the entities  | No amendments.              |

| Comments   | Summary of responses received  | EBA analysis   | Amendments to the proposals   |
|--|--|--|---|
|  | Finally, one respondent likewise suggests clarifying whether it is necessary to form a GCC in the case of an institution itself and its subsidiaries.  | within its own group are part of the same consolidated financial statement. The EBA reminds that after identifying GCCs, institutions may fully or partially exempt these exposures following competent authorities' discretion under Article 400(2) or under the Member State discretion under the transitional arrangements set out in 493(3) of the CRR.  |   |
| <b>Responses to questions in Consultation Paper EBA/CP/2022/07</b>   |  |  |   |
| <p><b>Question 1.</b></p> <p>Could you please indicate, if the approach of sections 4, 6 and 7 of the existing EBA guidelines, now transposed in the Articles of the draft RTS, remains sound and is implementable with no major challenge or unduly high costs. Please elaborate.</p> | <p>Three respondents deem that the requirements of the sections 4, 6 and 7 of the EBA GL (EBA/GL/2017/15), have been tightened in the transposition into the RTS. Specifically, they consider that the wording chosen in Article 2(1) of these draft RTS could bring to the formation of a GCC automatically, without case-by-case assessment. Moreover, with reference to Article 2(2) of these draft RTS, the same respondents deem that it does not fit with the concept of a single risk due to economic dependency and is superfluous. Indeed, in their view there is no scope to refute the single risk where one or more of the circumstances outlined in paragraph 1 is affirmed.</p> <p>More in general, according to the same respondents these RTS would bring implementation costs due to the required technical changes and amendments to the banks' documentation and processes.</p> <p>Two respondents believe that the implementation into the management and systems of section 7 of EBA GL (EBA/GL/2017/15) now transposed in Article 3 of</p> | <p>As a general remark, the EBA wants to draw attention to the legal nature and formal requirements of RTS, which is inherently more prescriptive and stricter than guidelines. That said, although the EBA GL (EBA/GL/2017/15) have been transposed into the RTS without substantial changes, these draft RTS results, by nature, in more stringent requirements than the EBA GL. According to the mandate in Article 4(4) of the CRR, the circumstances in which the conditions set out in point (39) of Article 4 paragraph 1 to form a GCC are met have to be specified. That said, it has to be clarified that Article 2 of these draft RTS sets out a non-exhaustive list of circumstances that should serve as benchmark when assessing economic dependency for the purpose of determining a single risk. This should not prevent institutions and competent authorities to consider further circumstances, not specifically foreseen by this Regulation. It also ensures a greater alignment to LEX Basel Standards (See, LEX 10.17). This implies that institutions have always the possibility to demonstrate that no single risk prevails despite one</p> | <p>Regarding Scenario E 7, labels referred to a single comprehensive group have been corrected.</p> <p>The wording of Article 2(1) of these draft RTS has been amended by replacing "<i>at least</i>" with "<i>in any of, but not limited to</i>" to specify that this Article sets out a non-exhaustive list of circumstances of economic dependencies that, when met with regard to two or more legal persons and unless otherwise demonstrated, justify the identification of a single risk and the treatment as a GCC.</p> <p>Previous paragraph 4 in Article 1 has been moved to</p> |

| Comments | Summary of responses received   | EBA analysis  | Amendments to the proposals  |
|----------|---|---|--|
|          | <p>the draft RTS is challenging as interconnectedness due to economic dependency has to be identified between subsidiaries and this is deemed difficult for small subsidiaries due to the lack of information and centralized databases. Similarly, one respondent points out that with reference to less significant exposures the requirements of the provisions are perhaps too burdensome to be implemented without major challenges and high costs. This respondent noticed that major issues had emerged from the detection of economic dependency, mainly due to the continuous evolution of economic relationships among clients and to the lack of information about economic dependency with traditional instruments. With regard to this, he proposes a threshold for exposures of 0.25% of the institution's Tier 1 capital, to investigate economic dependencies. The same threshold should be also used to investigate the "<i>significant influence</i>". That threshold is deemed useful to reduce discretionary assessments and the related risk of over/under-estimation.</p> <p>Two respondents state that if Article 1(1) of these draft RTS would enter into force in the proposed wording and extent (i.e., "<i>shall constitute a single risk</i>"), it would automatically bring to the formation of a GCC. Moreover, the respondent underlines that time and effort would increase significantly to identify all relevant exposures for the large exposure reporting.</p> <p>Two respondents provide some comments with regard to:</p> | <p>or more of the circumstances of Article 2(1) of these draft RTS being met.</p> <p>With reference to the RTS implementation costs, the EBA notes that the current draft RTS mirror the EBA GL (EBA/GL/2017/15). For this reason, and as expected by both industry and competent authorities, no significant burden in the implementation of this RTS is expected.</p> <p>The EBA recognises the challenges in investigating economic dependency for small entities due to lack of available data. However, the EBA clarifies that – in accordance with Section 8 of the EBA GL (EBA/GL/2017/15), which remains in force – institutions are expected to take an approach that is proportional to the amount of their exposures when investigating economic dependencies. This means that institutions are expected to take reasonable steps and use readily available information to identify economic dependencies. For material exposures (i.e., where the sum of all exposures to one individual client exceeds 5% of Tier 1 capital), institutions are expected to strengthen their investigation of economic dependency, by extensive research of any type of "<i>soft information</i>" as well as information that is not directly derived from the institution's clients.</p> <p>With reference to the proposal to establish a threshold to investigate both economic dependencies and "<i>significant influence</i>", the EBA notes that the mandate in Article 4(4) of the CRR requires the EBA to specify in which circumstances the conditions set out in point (39) of Article 4(1) are met. In this sense, given the constrained scope of the mandate, no</p> | <p>paragraph 2 in order to provide a logical sequence of the paragraphs within this Article in line with the logic provided in the recitals.</p> |

| Comments  | Summary of responses received | EBA analysis  | Amendments to the proposals |
|---|-------------------------------|---|-----------------------------|
| <p>i) Scenario C 1, where it is asked to clarify the word “correlation”;</p> <p>ii) Scenario E 7, where a rewording of the expression “<i>it cannot be ruled out</i>” is suggested. Moreover, it is pointed out that labels in the last diagram under paragraph 65 are incorrect; and</p> <p>iii) Scenario E 8, which is deemed inconsistent with Recital 6.</p> <p>With regard to the implementation date of these draft RTS, one respondent deems necessary an adaptation period of 6 months before the implementation of the RTS. This time is considered useful to review internal procedures and approaches across institutions.</p> |                               | <p>thresholds can be introduced for excluding exposures.</p> <p>As regards Article 1(1) of these draft RTS, it is intended to automatically lead to the recognition of a GCC. As raised in the responses to the stock-take amongst competent authorities and industry representatives (see Section 3), both industry and competent authorities seem to have automatized the formation and monitoring of GCC based on the control criteria, reflected in Article 1(1) of these draft RTS. This shall be the case also where persons are not included in the consolidated financial statements due to exemptions or derogations – see Article 1(2) [former Article 1(4)] of these draft RTS. Moreover, the EBA reiterates that in cases in which Article 1(5) of these draft RTS would apply, a GCC would not need to be formed.</p> <p>With reference to Scenario C 1, the EBA notes that this specific scenario was already subject to a public consultation for the adoption of the EBA GL (EBA/GL/2017/15) and therefore is not part of the consultation process of this RTS. A positive correlation is a relationship between two variables that move in tandem – i.e., in the same direction.</p> <p>Regarding Scenario E 7, the EBA believes that the used wording is consistent with Articles 1(5), 2(2) and 3(3) of these draft RTS, coherent with the EBA GL (EBA/GL/2017/15) that clarify that the burden of proof is on institutions. With reference to the diagram, the EBA clarifies that labels have been corrected.</p> |                             |

| Comments  | Summary of responses received  | EBA analysis   | Amendments to the proposals |
|---|--|--|-----------------------------|
| <hr/>   |  |  |                             |
|   |  | <p>As regards Scenario E 8, the EBA clarifies that there is no inconsistency with Recital 6. Indeed, when two or more entities are managed on a unified basis in accordance with paragraph 7 of Article 22 of Directive 2013/34/EU, these entities shall be considered as a source of a single risk if the latter cannot be ruled out.</p> <p>The final draft RTS will be submitted to the Commission for adoption. Following the submission, the RTS will be subject to scrutiny by the European Parliament and the Council before being published in the Official Journal of the European Union. This should allow sufficient time for institutions and competent authorities to prepare for their full application. Moreover, as specified in the background, the approach taken by the EBA in developing these draft RTS has been to leverage on the existing EBA GL (EBA/GL/2017/15) for the parts that fall under the mandate set out in Article 4(4) of the CRR. For this reason, no significant changes related to mapping and management of GCC are expected.</p> |                             |
| <hr/>   |  |  |                             |
| <p><b>Question 2.</b></p> <p>Have you identified any additional aspect(s) that would require clarification? In this vein, would you see the need for further illustrative examples (and if yes, on which precise situation or specific case)? Please elaborate.</p> | <p>Two respondents believe that further clarification regarding the links between General Partners – SGR – Funds – subsidiaries would be useful as it is not disciplined in the draft RTS nor in the EBA GL (EBA/GL/2017/15). The same respondents propose some criteria that could be considered usable to demonstrate the absence of a single risk between the Funds and their associated companies. Hence, they believe that the relationship between General Partners / SGRs and Funds they manage as well as between Funds (including Private Equity Funds) and</p> | <p>As a general remark, the EBA notes that the scenarios provided are of general nature and do not mean to capture specific business models or entities (e.g., funds, trust and/or UCITS). For this reason, the EBA believes that the current examples could address, if duly adapted, also situations involving collective investment funds. It should also be highlighted that the relationship between general partners/SGRs and funds may vary depending on the contract and/or national legislation. Therefore, these cases shall mostly be subject to a case-by-case assessment in</p>   | No amendments.              |



| Comments  | Summary of responses received   | EBA analysis   | Amendments to the proposals   |
|---|---|--|---|
|   | <p>their related companies (SPVs / subsidiaries) deserve further explanation. Moreover, one respondent sees merit for some clarification with regard to Article 1(5), in particular whether asks if the conditions laid down in Article 1(5) are met in the case of collective investment funds (such as UCITS), since it can be assumed that in these cases the respective company is sufficiently segregated and insolvency proof.</p> <p>Furthermore, one respondent believes that it is unclear whether the personal equality of members of the supervisory board has to be checked in a dualistic system as well. Examples would be required on how personal equalities (basically, no element of control between the owners and the company – no control at all between the management and the company) lead to economic dependencies (i.e., which additional conditions need to be met).</p> <p>One respondent considers the aggregation of exposures of entities economically interconnected as single risk should be done only in those cases when there is a high level of probability of default of the dependent.</p> | <p>order to investigate the existence of control relationships or economic dependencies. If needed, the EBA stands ready to provide further technical clarifications through the Q&amp;A process.</p> <p>The EBA reiterates that RTS establish rules which all institutions have to apply in their assessment irrespective of the corporate governance model of the entities concerned (e.g., dualistic systems).</p> <p>Finally, the EBA recalls that the large exposure framework is aimed to serve as a backstop measure to limit the maximum possible loss an institution could incur if a single counterparty or GCC would suddenly fail thus threatening the institution's survival as a going concern. Therefore, the probability of default of the dependent is not an element to be considered.</p> |   |
| <p><b>Question 3.</b></p> <p>After considering the circumstances set out in Article 1 that constitute a single risk by means of control, could you please indicate if the described circumstances are</p> | <p>One respondent suggests amending Article 1(3)(c) of these draft RTS by using the wording of the EBA GL (EBA/GL/2017/15) in point vi) of paragraph 13. Moreover, two respondents ask for some clarification about the term “<i>management</i>” related to natural persons.</p> <p>One respondent assumes that the use of the phrase “<i>may be deemed</i>” in Article 1(3) of these draft RTS means that the criteria set out in this paragraph</p>   | <p>The EBA notes that the wording of Article 1(4)(c) [former Article 1(3)(c)] of these draft RTS mirrors that of point vi) of paragraph 13 of the EBA GL (EBA/GL/2017/15). However, due to the legal nature of RTS, it cannot be fully aligned. As regards the comments asking for clarification of the term “<i>management</i>” related to natural persons, Article 1(4)(c) [former Article 1(3)(c)] of these draft RTS has been amended in order to remove this incorrect</p>  | <p>Article 1(4)(c) of these draft RTS has been amended as follows: “<i>the natural or legal person has the right or ability to coordinate the management of one or more <del>natural or legal</del> persons.</i>”</p> <p>In points (a) and (b) of Article 1(4) the wording “<i>has the right</i>”</p> |

| Comments                                 | Summary of responses received  | EBA analysis   | Amendments to the proposals  |
|--|--|--|--|
| sufficiently clear?<br>Please elaborate. | <p>continue to represent indicators of a control relationship.</p> <p>The same respondents deem that national discretions have to be taken into account in those cases where a consolidation is required based on banking law; with this regard it should be clarified that a “<i>supervisory consolidation</i>” should not be covered under Article 1 (1) of these draft RTS.</p> <p>Another respondent suggests that it would be preferable that Article 1(1) and 1(2) point a) and b) of these draft RTS have to be applied to all types of exposure. Moreover, with regard to Article 1(5) of these draft RTS, the same respondent asks to refer also to paragraph 3.</p> <p>Finally, one respondent likewise suggests to:</p> <ul style="list-style-type: none"> <li>i) amend Article 1(2)(c) of these draft RTS, in order to include a reference to only legal person (and not natural person); and</li> <li>ii) amend Article 1(3) of these draft RTS in order to align the wording consistently with the EBA GL (EBA/GL/2017/15).</li> </ul> | <p>reference. Moreover, to align the impact of Article 1(4) points (a) and (b) of these draft RTS to that of the EBA GL (EBA/GL/2017/15), it has been specified that two or more natural or legal person may be deemed to constitute a single risk because one of them has <u>the right or ability</u> to decide on the strategy or on important transactions of the other person/s.</p> <p>The EBA reiterates that the criteria set out in Article 1(4) [former Article 1(3)] of these draft RTS represent a non-exhaustive list of circumstances relevant for the assessment of the control relationship, which continue representing indicators of a control relationship.</p> <p>The EBA notes that Article 1(1) of these draft RTS refers to paragraphs 1 and 2 of Article 22 of Directive 2013/34/EU, the IFRS 10, and national laws of the respective Member State (i.e., the accounting consolidation). The case of “<i>supervisory consolidation</i>” shall be subject to a case-by-case assessment by the institution taking into account the criteria provided by paragraphs 3 and 4 of the same Article. Moreover, the EBA reiterates that a general principle of prudence should prevail leading to the assumption of the existence of a single risk when there is uncertainty whether the relationship among two or more natural or legal persons fulfils the conditions set out in these draft RTS.</p> <p>The EBA welcomes the comments acknowledging that Article 1(1) and 1(3) points (a) and (b) [former Article 1(2) points (a) and (b)] of these draft RTS have to be applied to all types of exposure. As regards the reference to paragraph 4 [former paragraph 3] in</p> | <p><u>or ability to</u>” has been added when referring to decisions made on the strategy or on important transactions of another person.</p> |

| Comments   | Summary of responses received  | EBA analysis   | Amendments to the proposals   |
|--|--|--|---|
|  |  | <p>Article 1(5) of these draft RTS, as also specified above, the EBA reiterates that the circumstances set out in this paragraph continue representing indicators of a control relationship, which may not necessarily lead to forming a GCC.</p> <p>The EBA notes that Article 1(3)(c) [former Article 1(2)(c)] of these draft RTS is aimed at including all types of relationship that could determine a dominant influence on a person irrespective of its nature (i.e., legal and/or natural person/s). Moreover, while mirroring the EBA GL (EBA/GL/2017/15), due to the legal nature of RTS, the wording used needs to be in line with other EU legal texts.</p> |   |
| <p><b>Question 4.</b></p> <p>Is the additional Scenario C 0 related to the determination of a group of connected clients by means of control, listed in Section 3.4.1 (Groups of connected clients based on a control relationship), sufficiently clear? Would you see need for further illustrative examples of a control relationship?</p> | <p>Three respondents found that the additional scenario is sufficiently clear.</p> <p>Six respondents consider useful to add additional examples for:</p> <ul style="list-style-type: none"> <li>Cases covered by paragraphs 2, 3 and 4 of Article 1; and</li> <li>Structures other than SPE/SPVs with no risk of contagion.</li> </ul> <p>According to one respondent it would be worth moving the EBA GL (EBA/GL/2017/15) and diagrams to an annex of these RTS.</p> | <p>The EBA welcomes the comments acknowledging that the provided list of examples is adequate and sufficient to correctly understand the requirements of these draft RTS. As also specified under “General comments”, due to the legal nature of RTS, examples/diagrams/scenarios cannot be included therein.</p> <p>The EBA reiterates that those examples already included in the Annex of the EBA GL (EBA/GL/2017/15) will remain therein.</p>  | No amendments.  |
| <p><b>Question 5.</b></p> <p>After considering the circumstances set out in Article 2 that constitute a</p>  | <p>Three respondents suggested maintaining the indicative nature of the EBA GL (EBA/GL/2017/15) for Article 2 of these draft RTS (<i>“Institutions should consider, in particular, the following situations when assessing economic dependency”</i>), which guarantees</p>   | <p>The EBA reiterates that Article 2 of these draft RTS sets out a non-exhaustive list of such circumstances that at least should be considered when assessing economic dependency for the purpose of determining a single risk. To specify this aspect, the</p>   | <p>Article 2(1)(j) of these draft RTS has been changed as follows: <i>“where the <del>administrative</del> management or <del>supervisory</del> bodies of two or more legal</i></p> |

| Comments  | Summary of responses received   | EBA analysis  | Amendments to the proposals   |
|---|---|---|---|
| single risk by means of economic dependency, could you please indicate if the described circumstances are sufficiently clear? Please elaborate. | <p>a risk-appropriate case-by-case assessment, instead of the binding criteria established under the RTS. Two of these respondents stated that some of the language used in the RTS (e.g., “significant” or “excessively”) point to a case-by-case analysis in any case and, therefore, should not be construed as a mandatory list. On this direction, these respondents noted the importance of letting institutions justify that, even when the circumstances under Article 2(1) of these draft RTS are met, there is no single risk, as there are situations where the scenario is uncertain and sometimes the assessment is time and resource intensive.</p> <p>On the contrary, two respondents suggested that, given the difficulty to demonstrate in practice that no single risk prevails when the conditions of the RTS are met, it would be better for institutions to establish a rule-based framework based on the list of criteria established in Article 2(1) of these draft RTS and complemented with internal expertise where needed.</p> <p>Two respondents pointed out that the circumstance listed under Article 2(1)(a) of these draft RTS is already embedded in the definition of economic dependency and does not describe a separate type of economic connection but a consequence of the dependency and should therefore be removed or clarified.</p> <p>Moreover, one respondent asked for clarification with regards to the inclusion of the terms “common owners, managers or shareholders” as the term “persons” should already capture the former. The</p> | <p>wording of this Article has been amended by replacing “at least” with “in any of, but not limited to”. This should not prevent institutions and competent authorities to consider further circumstances, guaranteeing a risk-appropriate case-by-case assessment. Institutions shall take reasonable steps and use readily available information to investigate and identify economic dependencies among their clients. Moreover, as explained in paragraph 33 in the background, with the EBA GL (EBA/GL/2017/15) still in place, institutions are expected to strengthen their investigation of economic dependencies among their clients in all cases where the sum of all exposures to one individual client exceeds 5% of Tier 1 capital, by performing extensive research of any type of “soft information” (e.g., other public or private information available).</p> <p>Regarding the proposal for institutions to establish a rule-based framework, the EBA notes that it is rarely possible to implement automated procedures for identifying economic interconnections. Therefore, even if an institution uses a rule-based framework for identifying GCCs, case-by-case analysis and judgement should be used to avoid underestimating the single risk.</p> <p>With regards to the clarification of Article 2(1)(a) of these draft RTS, the EBA notes that the definition of economic dependency, as stated under Article 4(1)(39) of the CRR, differs from point (a) of Article 2(1) of these RTS, which describes a specific circumstance of an economically dependent</p> | <p><i>persons consist for a major part of the same persons within the meaning of point (b) of paragraph 7 of Article 22 of Directive 2013/34/EU.; <del>common owners, managers or shareholders two or more undertakings have for a major part the same common owners, shareholders or managers.</del></i></p> <p>New Article 2(1)(k) has been added to cover cases of economic dependencies where the same natural or legal persons hold the majority of voting rights in two or more legal persons, without participating in the management bodies of these legal persons.</p> |

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|          | <p>respondent also suggests aligning the term “<i>administrative management body</i>” to that used in other legal texts (i.e., “<i>management body</i>”).</p> <p>With regards to some specific commentary, one respondent asked for clarification on whether groups need to be formed for households and noted that Article 2(1)(j) of these draft RTS should not apply to borrowers which have a structure that enables the isolation of the borrower from the bankruptcy of its shareholders (e.g., specialised lending). Another respondent stated that institutions should also not identify a single risk between all the clients whose primary source of income comes from the state budget (e.g., subsidies, fees for health services).</p> <p>Finally, in relation to the examples, one respondent asked for clarification on how Scenario E 6 relates to Article 2(1)(f) of these draft RTS, as there is no information on the concrete flow of funds well as its difference with Article 2(1)(h) of these draft RTS. Another respondent asked for further explanation or an example on Article 2(1)(j) of these draft RTS.</p> | <p>relationship. This same criterion is consistent with the Standards on the supervisory framework for measuring and controlling large exposures issued by the Basel Committee on Banking Supervision in April 2014.</p> <p>As regard the suggestion of replacing the term “<i>administrative management or supervisory bodies</i>” with “<i>management body</i>”, the wording has been amended in Article 2(1)(j) of these draft RTS, with also a reference to point (b) of paragraph 7 of Article 22 of Directive 2013/34/EU.</p> <p>Since there might be cases in which economic dependencies exist because the same natural or legal persons hold the majority of voting rights in two or more legal persons, without being necessarily part of the management body, a new point (k) in Article 2(1) of these RTS has been added. It covers cases when two or more persons act in a concerted way – e.g., situations of natural persons with family ties; even in cases where these persons are not part of the same management body. This shall align the impact of these draft RTS to that of the EBA GL (EBA/GL/2017/15) – see point h) of paragraph 23.</p> <p>Economic dependency between clients can arise in a number of situations, including cases of specialized lending. In relation to specific cases where the borrower can be ring fenced from the bankruptcy of its shareholders, institutions are required to assess these particular circumstances and whether the fulfilment of one or more of the listed situations would lead to a relationship of economic dependency. If institutions are able to demonstrate,</p> |                             |

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|  |  | <p>and document appropriately, that in such specific cases an economic dependent relationship among clients does not lead to the existence of a single risk, there would be no grouping requirement.</p> <p>Regarding the comment that no single risk should be considered when the primary source of income comes from the State budget, Article 4(1)(39) of the CRR states that where a central government has direct control over or is directly interconnected with more than one natural or legal person, the set consisting of the central government and all of the natural or legal persons directly or indirectly controlled by it, or interconnected with it, may be considered as not constituting a GCC. This approach is further developed in Section 5 of the EBA GL (EBA/GL/2017/15).</p> <p>Further clarification with regard to Scenario E 6 has been requested by one respondent. The EBA notes that this scenario is meant to be a simple example whereby investors withdraw from the SPV and therefore the sole provider of funding is the institution via its liquidity lines, which are then drawn by the SPVs simultaneously. Scenario E 6 is not meant to capture complicated situations with different funding flows, which always requires a case-by-case assessment.</p> |                             |
| <p><b>Question 6.</b></p> <p>In point (c) of Article 2(1), would you prefer following a quantitative approach by replacing the term “significant</p> | <p>Eight respondents expressed concerns for including a quantitative threshold. In particular, respondents felt the need for case-by-case analysis rather than a predefined threshold as too often it would not be able to accommodate specific cases. One of these respondents noted that setting a threshold could</p> | <p>The EBA welcomes the feedback on the quantitative threshold for point (c) of Article 2(1) of these draft RTS and has decided not to include such indicators. As noted on the consultation process of the EBA GL (EBA/GL/2017/15), even if the inclusion of a threshold</p>   | <p>No amendments.</p>       |

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| <p>part” with a threshold of “50% or more” as envisaged in point 1 of LEX 10.16? What would be the advantages or disadvantages? Please elaborate.</p>   | <p>result in economic dependencies not being assessed below the threshold. Others stated that there are some cases where, even when more than 50% of a person’s gross receipts or expenditures is derived from another person, there is no economic dependency between them due to substitutability. All in all, respondents felt that the conclusions reached in the consultation paper of the EBA GL (EBA/GL/2017/15) still hold.</p> <p>Four respondents see merit in establishing a more precise definition of “<i>significant part</i>”. For some of these, a quantitative approach would ensure consistency. However, the same respondents stated that it should not be a mandatory criterion as institutions should be allowed of assessing cases on an individual basis. Finally, another respondent pointed out that a threshold could be useful as trigger to undertake further investigation.</p> <p>One respondent suggested including the contribution to operating income as indication of economic dependency, which in their experience has shown to form economic dependent groups.</p> | <p>in some situations may facilitate the assessment, it is still recognised that the interpretation of a “<i>significant part</i>” will depend on the specific situation and might involve different percentages. Nevertheless, institutions should note that the threshold of 50% can serve as an indicator to further analyse its clients.</p> <p>The EBA reiterates that Article 2 of these draft RTS provides a non-exhaustive list of situations that should be considered by institutions when assessing economic dependencies. Even if the specific reference to “<i>operating income</i>” is not reflected on point (c) of Article 2(1) of these draft RTS, it does not mean it would not be captured by it.</p> | <p>No amendments.</p>       |
| <p><b>Question 7.</b></p> <p>What is your view on the wording “<i>that cannot be replaced in a timely manner without excessively increased costs</i>” compared to the wording used in the GL “<i>that cannot be easily replaced</i>”? What do you think about this change, is it more</p> | <p>Six respondents prefer the new wording as it is more comprehensible. Of which:</p> <ul style="list-style-type: none"> <li>- One respondent asked for further specification on the meaning of “<i>timely</i>”, suggesting that this should mean sufficient time to avoid bankruptcy.</li> <li>- Two respondents welcomed the wording as it still enables for a case-by-case analysis and highlighted that it should be construed</li> </ul>  | <p>The EBA welcomes the support received for the new wording. With regards to the comment to specify further the meaning of “<i>timely</i>” the EBA reiterates that based on a case-by-case assessment, institutions should consider a period short enough to avoid potential funding or repayment difficulties.</p> <p>The EBA does not see a need to refer to “<i>significant financial difficulties</i>” as a consequence of excessively increased costs as this is already captured in the definition of economic dependency as laid down in</p>   | <p>No amendments.</p>       |



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| comprehensible? elaborate.   | <p>Please</p> <p>as an indicative, not as proof, of economic dependency.</p> <ul style="list-style-type: none"> <li>- On the same vein, two respondents asked to reference the fact that in some cases, even when the cost of replacing is excessive, no single risk prevails because it would not lead to significant financial difficulties. Thus, it was suggested to amend the wording by including <i>“without excessively increased costs leading to significant financial difficulties”</i>.</li> </ul>  | <p>Article 4(1)(39)(b) of the CRR. Therefore, institutions already need to take this specific aspect into account when assessing the effect of the increased costs.</p>   |   |
| <b>Question 8.</b>   |   |   |   |
| <p>Is the additional Scenario E 8 related to the determination of a group of connected clients by means of economic dependencies, listed in Section 3.4.2 (Establishing interconnectedness based on economic dependency), sufficiently clear? Would you see need for further illustrative examples of an economic dependency relationship? Please elaborate.</p> | <p>Two respondents believe the example reported in Scenario E 8 is clear and complete.</p> <p>Three respondents asked for more clarity on Scenario E 8. In particular, they argue that it is not totally clear in which group the single risk should be allocated and how it should be reported.</p> <p>One respondent believes that the reference to Article 22(7) of Directive 2013/34/EU leads to confusion as the example refers to control and not economic dependence.</p> <p>Finally, one respondent stated that Scenario E 8 is too simplified. For this reason, this respondent proposes to add another case where the majority of the members of the management body are joint in several entities as per Article 22(7)(b) of directive 2013/34/EU.</p> | <p>The EBA welcomes the comments acknowledging that Scenario E 8 is clear and complete. However, to provide more clarity, and as requested by three respondents, further guidance has been included in Scenario E 8.</p> <p>As regard the reference to Article 22(7) of Directive 2013/34/EU in Article 2(1)(i) of these draft RTS, the EBA notes that this paragraph intends to mirror point h) of paragraph 23 of the EBA GL (EBA/GL/2017/15), which also refers to circumstances of economic dependencies. Furthermore, Scenario E 8 is also listed under Section 2.4.2 (Establishing interconnectedness based on economic dependency), which provides guidance to cases for forming a GCC based on economic dependency.</p> <p>The EBA notes that Scenario E 8 refers to Article 2(1)(i) of these draft RTS, which exclusively covers the situation where two or more legal persons are managed on a unified basis according to point (a) of paragraph 7 of Article 22 of Directive 2013/34/EU.</p> | <p>Further guidance has been included under Scenario E 8, with also a reference to points (j) and (k) of Article 2(1) of these draft RTS.</p> |



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|   |  | <p>Following the amendments in Article 2(1)(j) of these RTS, which now refers to the management body of two or more legal persons consisting for a major part of the same persons, a reference to point (b) of paragraph 7 of Article 22 of Directive 2013/34/EU has also been added. Further guidance with a reference to this case as well as the new Article 2(1)(k) of these RTS, which covers cases where the same natural or legal persons hold the majority of voting rights in two or more legal persons, without participating in the management bodies of these legal persons, has been provided.</p>  |                             |
| <p><b>Question 9.</b></p> <p>After considering the circumstances set out in Article 3 that constitute a single risk by means of the combined existence of control and economic dependencies, could you please indicate if the described circumstances are sufficiently clear? Please elaborate.</p> | <p>Five respondents acknowledged that Article 3 of these draft RTS as supported with scenarios providing additional insight in combined occurrence of control and economic dependency (C/E 1 One – way dependency; C/E 2 Two – way dependency; C/E 3 Downstream contagion; C/E 4 Upstream contagion) is sufficiently clear; of which:</p> <ul style="list-style-type: none"> <li>Two respondents suggested to present general principles more than describing the combined existence of control relationships and economic dependencies only in technical terms. In particular, directions are quite clear and easily implemented on simple groups, while for large groups most cases are not straightforward.</li> <li>One respondent argued that it remains unclear why a rejection of the existence of a single risk within the meaning of Article 1 or Article 2 of these draft RTS should be</li> </ul> | <p>The EBA welcomes the comments acknowledging that the conditions for combined existence of control relationships and economic dependencies set out in Article 3 of these draft RTS are deemed sufficiently clear.</p> <p>As regards the request for presenting the combined existence of control relationships and economic dependencies through more general principles, it is EBA's view that the proposed approaches in these draft RTS were designed to be compatible with both simple and large groups. Moreover, the EBA reminds that the combined existence of control relationships and economic dependencies needs always to be assessed on a case-by-case analysis, without limiting the cases of combined occurrence of control and economic dependency to those described in Section 2.4.3.</p> <p>The EBA notes that, as specified also in Recital 7, and in line with the comment received, when assessing</p> | <p>No amendments.</p>       |

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|   | <p>disregarded. Institutions should be able, as before, to first determine which clients are connected by virtue of a control relationship and which are connected by a virtue of economic dependency and then assess whether the identified clients should form a GCC.</p> <p>Finally, one respondent considers the implementation into the management and systems of Article 3 of these draft RTS challenging as interconnectedness due to economic dependency has to be identified also between subsidiaries. In particular, it is difficult to identify this type of interconnectedness for small subsidiaries due to the lack of information. In addition, when identifying an economic dependency at subsidiary level, the potential support of each group to its subsidiaries in case of financial difficulties should be also considered.</p> | <p>the coexistence of control and economic dependency, institutions should consider each case separately, considering when two or more natural or legal persons constitute a single risk on the basis of control and one or more of them are so closely interlinked and interdependent with another natural or legal person or persons that they are economically dependent.</p> <p>Finally, the EBA reiterates that institutions should consider the non-exhaustive list of situations in Article 2(1) of these draft RTS when assessing connections due to economic dependencies. When assessing those cases, it shall be underlined that according to the EBA GL (EBA/GL/2017/15), institutions should take reasonable steps and use readily available information to investigate and identify economic dependencies. As regards the potential support of each group to its subsidiaries, the EBA reiterates that upstream contagion shall also be assessed when determining GCCs.</p> |                             |
| <p><b>Question 10.</b><br/>Is the additional Scenario E 7 related to the determination of a group of connected clients by means of the combined existence of control and economic dependencies, listed in Section 3.4.3 (Relation between interconnectedness through control and interconnectedness through economic dependency),</p> | <p>Three respondents pointed out that the additional Scenario E 7 is sufficiently clear. These respondents highlighted that it shall be clear in the future that the coexistence of control and economic dependency remains decisive for GCC formation and cannot be replaced by single cases.</p> <p>One respondent requested to provide more details in footnote 9 regarding Scenario E 7 in:</p> <ol style="list-style-type: none"> <li>1. defining of quantitative threshold for the term “significant stake”; or</li> </ol>  | <p>The EBA welcomes the comments acknowledging that the additional Scenario E 7 is sufficiently clear. Moreover, it reminds that the interaction between control and economic dependency is the decisive factor in determining whether a GCC should be formed, and that this assessment cannot be replaced by individual scenarios.</p> <p>As regards providing more details related to the term “significant stake”, the EBA reiterates that when assessing cases such as that described in Scenario E 7, institutions need to assess the grouping requirements</p>  | No amendments.              |

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| sufficiently clear? Please elaborate. | <p>2. providing additional descriptive guidelines regarding an easier identification of a “significant stake”.</p> <p>One respondent suggested to add a more complicated scenario whereby (starting from Scenario E 7) P1 and P2 are also connected with other own group of companies. In this specific case, the respondent seek clarification on whether groups of P1 and P2 need also to be included in a single GCC.</p> <p>One respondent argued that the approach introduced under Scenario E 7, could entail undue costs and major effort in the GCC identification process. As a consequence, the exclusion of less significant exposures from the provisions at issue (by means of the adoption of a threshold for expert assessment – e.g., 0.25% of Tier 1) could be considered.</p> | <p>on the basis of a case-by-case analysis, considering that a “significant stake” leading to a combined existence of control and economic dependencies could be dependent on Member State specificities.</p> <p>Furthermore, the EBA does not consider an additional example necessary (starting from Scenario E 7, in the case P1 and P2 are also connected with other own group companies). With Scenario C/E4, the EBA GL (EBA/GL/2017/15) already provide an example for a “comprehensive group”. If needed, the EBA stands ready to provide further technical clarifications through the Q&amp;A process.</p> <p>Finally, the EBA notes that the mandate in Article 4(4) of the CRR requires the EBA to specify in which circumstances the conditions set out in point (39) of Article 4(1) of the CRR are met. This implies that no thresholds can be introduced for excluding exposures. However, with the EBA GL (EBA/GL/2017/15) still in place, the EBA considers that institutions are expected to strengthen their investigation of economic dependencies among their clients in all cases where the sum of all exposures to one individual client exceeds 5% of Tier 1 capital.</p> |                             |