EBA REPORT ON THE COMPLETENESS AND APPROPRIATENESS OF THE DEFINITIONS AND PROVISIONS ON CONSOLIDATION UNDER ARTICLE 18(10) OF THE CRR

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Abbreviations

AIF	Alternative Investment Fund
AMC	Asset Management Company
AoA	Articles of Association
ASU	Ancillary Services Undertaking
BCBS	Basel Committee on Banking Supervision
CI	Controlling Interest
CIU	Collective Investment Undertaking
CRD	Capital Requirements Directive 2013/36/EU
CRR	Capital Requirements Regulation (EU) No 575/2013
CRR2	Regulation (EU) 2019/876 amending Regulation (EU) No 575/2013
CRR3	Regulation (EU) 2024/1623 amending Regulation (EU) No 575/2013
CET1	Common Equity Tier 1
EBA	European Banking Authority
EC	European Commission
EEA	European Economic Area
ESA	European Supervisory Authority
FHC	Financial Holding Company
FSE	Financial Sector Entity
G-SII	Global Systemically Important Institution
IFRS	International Financial Reporting Standards
IFRS	Investment Firm Regulation (EU) 2019/2033
MAG	Mixed-Activity Group

MiFID II	Markets in Financial Instruments Directive 2014/65/EU
NACE	Nomenclature of Economic Activities
NCI	Non-Controlling Interest
nGAAP	National Generally Accepted Accounting Principles
NPL	Non-Performing Loans
O-SII	Other Systemically Important Institution
Q&A	Questions and Answers
RTS	Regulatory Technical Standards
SPV-SEC	Other Special Purpose Vehicle for Securitisation
SSPE	Securitisation Special Purpose Entity
SRT	Significant Risk Transfer
STS	Simple, Transparent and Standardised
UCITS	Undertakings for Collective Investment in Transferable Securities

Report on EU prudential consolidation framework under Article 18(10) of the CRR

Introduction and purpose

The prudential consolidation framework is a key pillar of the EU banking regulatory regime. It is fundamental to the effective application of prudential requirements, as it determines the perimeter within which risks are identified, measured and managed across banking groups. By establishing the appropriate scope for consolidated supervision, the framework enables competent authorities to assess the financial soundness and risk profile of banking groups in a holistic and comprehensive manner, thereby preventing double gearing and mitigating opportunities for regulatory arbitrage.

The relevance of the consolidation framework has become even more pronounced in recent years, in light of evolving business models, increasing digitalisation, and the emergence of new types of entities providing financial services or carrying out activities ancillary to banking. These developments may give rise to new interconnections, dependencies, and sources of risk within banking groups, which need to be appropriately captured and supervised at the adequate level of consolidation. A robust and coherent application of the prudential consolidation framework is therefore key to ensuring that such risks are not left outside the regulatory perimeter and that the prudential treatment remains consistent with the underlying economic substance of group structures.

In recent years, the EBA has actively monitored the implementation of consolidation provisions, published opinions and reports offering insights and recommendations to the co-legislators, and developed Regulatory Technical Standards (RTS) to promote supervisory convergence on the methods of prudential consolidation. Following the amendments introduced by the CRR3, the EBA has been mandated to assess the robustness and effectiveness of the revised framework, and provide updates every two years, with the objective of supporting the European Commission in identifying potential areas for further legislative adjustments.

This Report represents the first comprehensive assessment of the EU regulatory framework on prudential consolidation conducted pursuant to Article 18(10) of the CRR. It draws on a detailed data collection exercise involving 70 institutions from 26 EU/EEA countries, including G-SIIs, O-SIIs, and non-systemic banking groups reflecting the diversity of structures and business models in the EU banking sector. The assessment has combined quantitative analysis of balance sheet data with qualitative insights into institutional practices, enabling a robust evaluation of how the consolidation provisions are applied in practice.

The Report is structured around key elements of the consolidation framework, including the scope of consolidation, definitions of undertaking, control and financial institution, treatment of ancillary services undertakings (ASUs), securitisation special purpose entities (SSPEs) and other special purpose vehicles used to set up securitisations (SPV-SECs), collective investment undertakings (CIUs), and the application of the exemption and sub-consolidation regimes. Each section presents the EBA's findings, conclusions, and policy recommendations, with a view to supporting the Commission in identifying potential areas for legislative adjustment. In addition, the Report sheds light on specific elements of the revised framework, thereby fostering harmonisation and supervisory convergence across Member States going forward.

EBA overall assessment and key recommendations

The EBA considers the prudential consolidation framework to be overall robust and fit for purpose. The framework generally enables the inclusion within the prudential perimeter of those undertakings that may pose material financial or ancillary risks to banking groups. Furthermore, the CRR3 amendments to the consolidation provisions and definitions have contributed to enhancing the framework's clarity, consistency, and risk coverage.

Nonetheless, the analysis has identified a number of targeted areas where further clarification, harmonisation, or legislative refinements may be warranted. Such improvements are necessary to close remaining gaps, reduce interpretative divergences, and enhance the framework's efficiency, thereby supporting more effective, consistent, and proportionate application of prudential requirements across institutions and Member States. In this vein, this Report puts forward a set of targeted recommendations and clarifications to further strengthen the prudential consolidation framework and its implementation among institutions, which pursue the following key objectives:

- **Efficiency and proportionality**: to identify areas where prudential requirements could be better aligned with accounting provisions or further streamlined, with a view to reducing unnecessary complexity, enhancing operational efficiency, and ensuring that requirements remain proportionate to the size, complexity, and risk profile of banking groups.

- **Completeness and appropriateness of the CRR framework**: to introduce limited but relevant adjustments to the CRR consolidation provisions and definitions, thereby improving their clarity, internal consistency, and overall completeness within the prudential framework.

- **Harmonised and consistent implementation:** to provide insights on aspects of the consolidation framework that may not require legislative changes but where interpretative divergences or practical challenges have arisen, in order to promote consistent application and supervisory convergence across Member States.

These recommendations are intended to ensure that the consolidation framework remains robust, transparent and capable of addressing both current and emerging risks, while supporting a level playing field and the effective supervision of EU banking groups.

Efficiency and proportionality

SCOPE AND METHODS OF CONSOLIDATION

The EBA's assessment has revealed that, in general, the prudential scope of consolidation is broadly aligned with the accounting perimeter, except for the treatment of insurance undertakings. This evidence may be explained by several factors, including a certain tendency observed among certain institutions to align the prudential and accounting scopes of consolidation, disregarding the application the CRR provisions governing the scope and method of consolidation.

Although such practices are not consistent with the current regulatory framework – which clearly sets out its principles for determining the scope and method of consolidation irrespective of the accounting standards – the EBA suggests broader policy considerations to evaluate whether the benefits associated with simplification and efficiency for institutions may justify some greater degree of alignment in terms of the scopes determined within the two frameworks (e.g. allowing full consolidation of non-financial subsidiaries for which the institution determines the existence of step-in risk).

In the same vein, the EBA suggests assessing whether the alignment of the methods used for accounting and prudential purposes might be justified in certain circumstances, especially when not materially impacting the representation of the financial situation and riskiness on a consolidated basis. This could be valid, for example, in the valuation of certain participations in non-financial institutions under Article 18(7) of the CRR, where the application of the equity method as default treatment could be unduly burdensome and may not provide relevant benefits for the determination of the consolidated situation of a banking group.

EBA Recommendation to the Commission

Recommendation 1. Broader alignment between scope of accounting and prudential consolidation.

The EBA recommends launching a targeted review to assess the feasibility, cost, benefits and potential impacts of a more systematic alignment between the scope two frameworks, while ensuring that the level playing field is maintained.

Recommendation 2. Scope of application of Article 18(7) of the CRR on the valuation method for non-financial investments.

The EBA recommends reviewing the scope of application of the equity method under Article 18(7) of the CRR and assessing the appropriateness of limiting its scope to cases where no book value of the investment in the subsidiary or participation exists for accounting purposes at consolidated level (i.e. limited to those entities fully consolidated under the accounting framework), in order to avoid unnecessary misalignment with the accounting standards and excessive compliance effort. In addition, consideration should be given to allowing competent authorities to require the use of a different method for subsidiaries or participations that are excluded from the scope of prudential consolidation, provided that the accounting method does not adequately reflect the risks posed to the institution and does not result in full or proportional consolidation of that undertaking.

EXEMPTION REGIME UNDER ARTICLE 19 OF THE CRR

Survey responses indicated that the usage of exemptions under Article 19(1) of the CRR is widely applied by institutions, while the application of Article 19(2) of the CRR has been quite limited in practice.

The EBA considers the provision under Article 19 of the CRR, which allows for the exclusion of certain entities from the scope of prudential consolidation, an important flexibility mechanism that facilitates the implementation of the regulatory framework. This exemption regime has proven effective in easing operational burdens for institutions and supporting proportionality in the application of prudential requirements.

Nonetheless, the EBA has identified specific areas where targeted regulatory guidance could enhance the consistency of approaches and simplify the operationalisation of the exemption regime. This includes clarifying its interaction with other elements of the prudential framework (e.g. deduction regime on financial sector entities), thereby contributing to a more coherent and streamlined implementation across institutions and jurisdictions).

While the application of this guidance can already be derived from a systematic interpretation of the CRR text, the EBA proposes targeted amendments to the Level 1 provisions to further improve clarity.

EBA Recommendation to the Commission

Recommendation 8. Application of Article 19 of the CRR.

The EBA recommends specifying within the Level 1 text that:

- *Holdings in institution or financial institutions exempt pursuant to Article 19 of the CRR should be subject to the FSE deduction regime under Article 36(1)(i) of the CRR. Additionally, such holdings should be valued either (i) using the equity method, or (ii) using the valuation method applied for accounting purposes.*
- *For the calculation of the relative materiality threshold under Article 19(1)(b) of the CRR, the percentage of total assets and off-balance sheet items should be determined with reference to the standalone (separate) accounting balance sheet of the parent undertaking or of the undertaking holding the participation*.

SUB-CONSOLIDATION REQUIREMENTS UNDER ARTICLE 22 OF THE CRR

The EBA's assessment has identified a number of practical and interpretative challenges associated with the application of sub-consolidation requirements under Article 22 of the CRR. These challenges may introduce unnecessary complexity into the supervisory framework and impose disproportionate operational burdens on institutions, particularly in cases involving multi-layered group structures with cross-border subsidiaries.

Sub-consolidation is intended to ensure that risks are appropriately captured and measured at intermediate levels of banking groups. However, the current provisions may lead to unintended consequences, such as the multiplication of sub-consolidation layers, inconsistent treatment of third-country subsidiaries, and ambiguity in the calculation of materiality thresholds. These issues can undermine the proportionality and effectiveness of the supervisory regime and may result in duplicative reporting obligations without commensurate prudential benefit.

In light of these findings, although the identified issues can be addressed by a more focused and consistent reading of the CRR, dedicated consideration is provided in this Report to ensure clarity. The EBA also proposes targeted adjustments to the Level 1 text in this regard.

In addition, the EBA observed specific supervisory issues arising from the automatic application of sub-consolidation requirements under Article 22 of the CRR, or from situations where these requirements are triggered by participations that would not be subject to consolidation. To address this, the EBA proposes further targeted adjustments to reduce regulatory burden.

EBA Recommendation to the Commission

Recommendation 9. Application issues of Article 22 of the CRR.

The EBA recommends clarifying within the Level 1 text the following:

- *an undertaking subject to Article 22(1) of the CRR should also comply with Part Two of the CRR in full, and not only with Articles 89, 90 and 91 of the CRR;*
- *in the case of chain of subsidiaries, Article 22 of the CRR should apply to the last (lower) subsidiary institution – or intermediate FHC or intermediate mixed FHC – in the Union that acts as the direct or indirect parent undertaking;*
- *the consolidated requirement at the level of an investment firm pursuant to the IFR does not provide a basis to discharge from applying the sub-consolidated requirement pursuant to Article 22 of the CRR;*
- *any third-country subsidiary that is already captured in a lower layer of sub-consolidation in the Union in accordance with Article 22 of the CRR does not have to be taken into account within the calculation of the 10% threshold;*
- *the calculation of such threshold should be performed on the basis of the standalone (separate) balance sheet of the relevant subsidiary institution, intermediate FHC or intermediate mixed FHC.*

Recommendation 10. Introduction of a derogation regime under Article 22 of the CRR.

The EBA recommends the introduction of a provision in the regulatory framework enabling competent authorities to grant exemptions from the application of Article 22(1) of the CRR on a case-by-case basis.

Recommendation 11. Application of sub-consolidation requirements where only a participation is held.

The EBA recommends limiting the application of sub-consolidation requirements under Article 22 of the CRR to participations that would need to be fully or proportionally consolidated for prudential purposes.

Completeness and appropriateness of the CRR framework

DEFINITION OF 'UNDERTAKING'

The EBA observed that the absence of a clear definition of 'undertaking' in the CRR has led to divergent interpretations across institutions. In particular, survey responses revealed that certain institutions apply a restrictive reading, recognising as parent undertakings only those entities listed in Annexes I and II to the Accounting Directive. As a result, relevant undertakings may not have been consistently identified as part of the prudential group, which poses risks to the accurate determination of the consolidation perimeter and the effectiveness of consolidated supervision.

The EBA is of the view that the concept of 'undertaking', as embedded in the definitions of parent and subsidiary undertakings, should not be limited to entities listed in the Accounting Directive or subject to Regulation (EC) No 1606/2002. Rather, it should encompass a broader range of economic actors capable of exercising control or being controlled. This approach ensures that the existence of control remains the decisive criterion for identifying parent–subsidiary relationships, thereby reinforcing the integrity of the prudential consolidation framework.

EBA Recommendation to the Commission

Recommendation 3. Definition of 'undertaking' for prudential consolidation purposes.

The EBA recommends introducing a clear and operational definition of 'undertaking' in the CRR, for prudential consolidation purposes.

DEFINITION OF 'FINANCIAL INSTITUTION'

The definition of 'financial institution' appears to be generally implemented in a consistent manner across institutions. The EBA acknowledges that this outcome may be partly attributed to the recent amendments introduced under the CRR3, which have addressed previous inconsistencies and broadened the scope of the definition to better accommodate new and evolving financial business models.

Nonetheless, the EBA has identified residual interpretative challenges, particularly in relation to: (i) the determination of an undertaking's 'principal activity'; (ii) the inclusion or exclusion of regulated and unregulated entities in the assessment of whether an undertaking qualifies as a financial institution; and (iii) the qualification of undertakings managing pension fund schemes. In the case of (un)regulated entities, the EBA considers that the current definition is sufficiently robust to support the interpretation that an entity may qualify as a financial institution irrespective of whether it is subject to regulation or supervision under Union or national law. Accordingly, no further amendments to the Level 1 text are deemed necessary in this regard.

EBA Recommendation to the Commission

Recommendation 5. Determination of principal activity under Article 4(1), point (26) of the CRR.

The EBA recommends clarifying within the definition of 'financial institution' how the principal activity of an undertaking should be determined. This could build on the approach already envisaged in the definition of 'financial holding company', thereby promoting consistency and reducing uncertainty.

Recommendation 6. Inclusion of companies managing pension funds under Article 4(1), point (26) of the CRR.

The EBA recommends the inclusion of companies managing pension funds within the definition of 'financial institution' under Article 4(1), point (26)(b)(ii) of the CRR, due to the similarity between their financial activities and associated risks and those of asset management companies.

SCOPE OF APPLICATION OF STEP-IN RISK PROVISIONS

The step-in risk provision under Article 18(8) of the CRR is an important component of the consolidation framework that allows the consolidation of undertakings that are not institutions, financial institutions or (re)insurance undertakings when there is a substantial risk that the institution decides to provide financial support to that undertaking in stressed conditions, in the absence of, or in excess of any contractual obligations to provide such support.

In this regard, the EBA notes that Article 18(8) of the CRR is limited to the cases of 'subsidiaries' and 'participations' but does not cover the cases of undertakings with which the institution has other types of capital ties or significant influence in absence of capital ties. Such cases may be however particularly relevant in the case of special purpose vehicles or similar undertakings. For this reason, the EBA proposes targeted adjustments to the Level 1 text to broaden its scope of application.

EBA Recommendation to the Commission

Recommendation 12. Scope of Article 18(8) of the CRR.

The EBA recommends enlarging the scope of application of Article 18(8) of the CRR to also include relationships other than subsidiaries and participations.

Harmonised and consistent implementation

DEFINITION OF ‘CONTROL’

Responses to the ad-hoc survey indicate that, overall, institutions demonstrate a sound understanding of the notion of ‘control’ as defined in Article 4(1), point (37) of the CRR. The use of this criterion to identify parent–subsidiary relationships is generally considered fit-for-purpose and effective in reducing inconsistencies between accounting and prudential frameworks, particularly for undertakings applying IFRS.

Nonetheless, the EBA has identified specific interpretative challenges that may affect the consistent application of the concept of ‘control’. These include: (i) the national transpositions of Article 22 of the Accounting Directive, which in some cases result in jointly controlled undertakings being treated as fully controlled (i.e. subsidiaries), and (ii) the treatment of severe long-term restrictions that materially limit a parent’s ability to exercise control over its subsidiary, which may not be adequately considered when assessing control under Article 22 of the Accounting Directive.

All in all, the EBA considers that the definition of ‘control’ is deemed suitable for a consistent identification of parent–subsidiary relationships. Limited recommendations are made to the Commission with the aim of providing further clarity to the interpretative challenges observed and to avoid inconsistencies in the determination of the consolidation perimeter.

EBA Recommendation to the Commission

Recommendation 4. Consideration within Article 4(1)(37) of the CRR of situations that prevent the exercise of control.

The EBA recommends clarifying within the definition of ‘control’ that severe-long term restrictions that substantially hinder the parent’s control over its subsidiary should be considered when Article 22 of the Accounting Directive is followed.

ANCILLARY SERVICES UNDERTAKINGS (ASU)

The definition of ASU under Article 4(1), point (18) of the CRR, as amended by the CRR3, represents a significant step forward in addressing the inconsistencies and ambiguities that existed under the previous framework, partly due to conflicts with the former wording of Article 89 of the CRR. The updated definition provides a more coherent basis for determining whether an undertaking qualifies as ancillary, thereby enhancing the clarity and consistency of the consolidation perimeter across institutions and Member States.

To support the consistent implementation of this revised definition, the EBA has issued Guidelines under Article 4(5) of the CRR. These Guidelines provide the criteria to be used for assessing whether an activity constitutes: (a) a direct extension of banking, (b) ancillary to banking, or (c) similar to (a) and (b).

The Guidelines are designed to be operationally simple and adaptable to a wide range of structures, while ensuring that the classification of ASUs remains grounded in prudential relevance. They also aim to reduce interpretative divergences and promote supervisory convergence, particularly in areas where practices have been generally heterogenous.

The changes introduced by the CRR3, combined with the regulatory guidance provided by the EBA Guidelines, are expected to address many of the implementation issues identified through the EBA's survey. These issues resulted in inconsistent classification of undertakings engaged in leasing, real estate services, and other support functions. Going forward, the EBA will continue to monitor its implementation to identify potential residual inconsistencies or emerging challenges.

COLLECTIVE INVESTMENT UNDERTAKINGS (CIU)

The EBA considers the current CRR framework applicable to CIUs as fit-for-purpose and appropriately addressing the specificities of CIUs. Nonetheless, divergent practices have been observed across institutions in determining whether CIUs should fall within the scope of prudential consolidation. Against this background, the EBA considers necessary to ensure that risks stemming from these vehicles are appropriately captured under the prudential framework, without advocating for legislative amendments.

In this context, the EBA reiterates its position, as clarified in the EBA Q&A 2015_2383, that CIUs should not, as a general rule, be regarded as financial institutions or financial sector entities, unlike asset management companies. Accordingly, CIUs should be generally excluded from prudential consolidation, unless the competent authority identifies a substantial risk of step-in and applies Article 18(8) of the CRR.

Nevertheless, this general treatment does not preclude the assessment of cases where CIUs pursue, as principal activity, one or more activities listed under Article 4(1), point (26)(b)(i) of the CRR, such as lending or the provision of guarantees, which would result in the qualification of the undertaking as financial institution and financial sector entity. Similarly, while CIUs would not generally qualify as ASU, as set out in the EBA Guidelines, specific circumstances – such as performing as principal activity the ownership or management of foreclosed assets in the direct or indirect interest of an institution – may justify their classification as such[1].

However, even in these cases, unless CIUs qualify as subsidiaries or are jointly controlled, their prudential consolidation would depend on the assessment of step-in risk by the

[1] In fact, in those specific cases, the activity performed would constitute a direct extension of banking according to Article 4(1), point (18)(a) of the CRR and the criteria provided with the EBA Guidelines on ASU.

competent authority[2]. In this regard, the EBA – consistent with previous clarifications provided[3] – considers that the dedicated treatment established in Articles 132 and 152 of the CRR for exposures in the form of units or shares in CIUs is generally deemed to be appropriate and the risk of step-in may be largely addressed through the application of the EBA Guidelines on limits on exposures to shadow banking entities.

SECURITISATION SPECIAL PURPOSE ENTITIES (SSPE) AND OTHER SPECIAL PURPOSE VEHICLES USED TO SET UP SECURITISATIONS (SPV-SEC)

The explicit non-consideration of SSPEs as financial institutions, introduced by the CRR3, is considered consistent with the nature of the activities carried out by these vehicles and aligned with previous clarifications provided by the EBA Q&A 2014_1530[4] and in the Final Report on the RTS on methods of prudential consolidation.

In this regard, the EBA has noted that the exclusion of SSPEs has generally not affected the scope of prudential consolidation in cases of vehicles involved in securitisations achieving SRT, as the absence of control already results in the non-inclusion of these vehicles in the prudential scope of consolidation.

Conversely, certain challenges have been observed when SSPEs are used in funding-driven securitisations due to the interaction and divergent treatment between accounting practices followed by some institutions and prudential rules. In these cases, some institutions have fully consolidated these vehicles for prudential purposes – despite not meeting the definition of 'financial institution' – to ensure that their consolidated situation reflects only the securitised exposures and avoid potential double counting – relevant for the leverage ratio.

Having considered the above and mindful of the prudential objectives underpinning the consolidation framework, the EBA is of the view that if the transaction does not achieve SRT, only the underlying securitised assets should continue to be recognised in the consolidated situation of the institution, in line with accounting requirements for recognition and derecognition. Additionally, the EBA considers that it is inappropriate to simultaneously recognise, from a prudential consolidation perspective, both the securitised assets and the retained securitisation notes, as it would not appropriately reflect the degree of financial leverage of an institution.

[2] In accordance with Article 18(5); (6)(a); and (8) of the CRR and following the criteria in Commission Delegated Regulation (EU) 2022/676 ("RTS on methods of prudential consolidation").

[3] See feedback table of Final report on draft RTS on methods of prudential consolidation.

[4] See EBA Q&A 2014_1530.

EBA Recommendation to the Commission

Recommendation 7. Interaction between the consolidation and leverage ratio framework in the context of SSPEs.

The EBA recommends conducting a targeted review to assess whether the current prudential framework sufficiently addresses the interaction of the consolidation provision with leverage ratio framework.

OTHER IMPLEMENTATION ISSUES (DANISH COMPROMISE)

The supervisory review of certain M&A transactions has highlighted interpretative challenges in the application of the consolidation framework, particularly in cases where financial institutions – such as asset management companies (AMCs) – are acquired through insurance subsidiaries of banking groups. The key policy question emerging from these cases is whether such indirectly held entities should be included in the consolidated situation of the parent institution, particularly when the institution applies the 'Danish Compromise' under Article 49(1) of the CRR to its insurance holdings.

In some instances, institutions have assumed that AMCs acquired via insurance subsidiaries fall outside the scope of prudential consolidation. This has led to the exclusion of these entities from the consolidated situation, resulting in goodwill not being deducted from CET1 capital and in the application of Article 49(1) of the CRR to the entire investment in the insurance subsidiary, including the AMC.

The EBA's assessment confirms that the current CRR framework already provides the necessary tools to address these situations. Specifically, the definition of 'subsidiary' under Article 4(1)(16) of the CRR explicitly includes subsidiaries of subsidiaries, thereby establishing that a financial institution held through an insurance undertaking qualifies as a subsidiary of the parent institution and must be fully consolidated, irrespective of the nature of the intermediate entity.

The clarifications set out in the EBA Q&A 2021_6211 are therefore not relevant in this context, as they concern the treatment of goodwill arising from investments in FSEs that are not subject to prudential consolidation (e.g. insurance undertakings) pursuant to Article 37(b) of the CRR. Accordingly, the Q&A does not impact the general deduction framework applicable to goodwill recognised directly by the consolidating parent undertaking, including where the goodwill originates from an indirect holding in a financial institution.

From a technical standpoint, the consolidation of indirectly held financial institutions requires appropriate adjustments to the carrying amount of the parent undertaking's investment in the insurance subsidiary, to reflect the consolidation of the financial institution (i.e. AMC) within the parent undertaking's consolidated situation.

Overall, the EBA considers the existing framework sufficiently robust to capture the prudential implications of such transactions. The ‘subsidiary of subsidiary’ principle plays a central role in ensuring that all relevant risks are reflected in the consolidated situation of an institution or (mixed) financial holding company, regardless of the group’s internal structure. Accordingly, no further regulatory changes are deemed necessary at this stage. Institutions are expected to apply the CRR provisions consistently and in line with the considerations within this Report.

Way Forward

The EBA will continue to closely monitor the implementation of the consolidation provisions and definitions. This monitoring will pay particular attention to the application of the revised framework for ancillary services undertakings, in light of the recently published EBA Guidelines, as well as to the framework’s ability to capture new and emerging sources of risk stemming from digitalisation, fintech developments, and evolving group structures. The EBA will also focus on specific areas where room for potential regulatory arbitrage may exist. Findings and policy conclusions of this monitoring activity will be reflected in future updates of the Report, ensuring that the assessment remains current and responsive to market and regulatory developments.

In parallel, the EBA stands ready to support the European Commission in assessing the need for potential legislative amendments in light of the recommendations set out in this Report. This support may include providing targeted technical input and conducting cost–benefit analyses and impact assessments to inform any future revision of the prudential consolidation framework.

The primary purpose of this Report is to inform the Commission’s consideration of possible Level 1 text amendments.

1. Introduction

1.1 Overview of the mandate

1. Article 18(10) of the CRR requires the EBA to submit a report (hereinafter 'Report') to the Commission on the completeness and appropriateness of the definitions and provisions of the CRR concerning the supervision of all types of risks to which institutions are exposed at a consolidated level. In particular, the EBA is requested to assess any possible remaining discrepancies in those definitions and provisions alongside their interaction with the applicable accounting framework, and any remaining aspect that might pose unintended constraints to a consolidated supervision that is comprehensive and adaptable to new sources or types of risks or structures that might lead to regulatory arbitrage.

2. The purpose of this Report is to enable the European Commission (hereinafter 'Commission') to fulfil its mandate of submitting to the European Parliament and to the Council, where appropriate and in the light of the EBA's findings, a legislative proposal to make adjustments to the relevant definitions or the scope of prudential consolidation.

3. In addition, the Report provides transparency on how institutions have implemented and interpret the key provisions and definitions of the consolidation framework under the CRR. Where relevant, it also sheds light on specific elements of the revised framework thereby fostering harmonisation and supervisory convergence across Member States going forward.

4. The report is structured into eight sections, each outlining the EBA's main findings and recommendations on the key elements of the consolidation framework that have been subject to review. *The recommendations are generally set out in high-level terms and might need to be developed further based on a comprehensive impact assessment and cost-benefit analysis. The EBA stands ready to provide the necessary assistance for that purpose*.

5. The initial deadline for the submission of the first report has been deferred to Q1 2026, to ensure alignment with the concurrent issuance of the Guidelines on Ancillary Services Undertakings (hereinafter 'Guidelines'). This has allowed a coordinated assessment of the provisions concerning ancillary services undertakings and their interaction with other elements of the consolidation framework.

6. This Report will be updated every two years, in accordance with the mandate under Article 18(10) of the CRR.

1.2 Methodology and sample of banks

7. The EBA's observations and further analysis of the consolidation framework have been based on a specific data collection addressed to a sample of banks on the basis of their situation as of 31 December 2023, which has been complemented by targeted qualitative questions. This has enabled the EBA to:

   a. assess how those institutions have implemented, in practice, the definitions and provisions related to the prudential consolidation framework under the CRR;

   b. examine differences between the scopes of prudential and accounting consolidation and identify the main factors explaining these differences;

   c. evaluate potential changes due to the CRR3 amendments, and whether remaining gaps in the prudential consolidation framework could prevent a complete representation of risks that banking groups are exposed to at consolidated level;

   d. detect any other potential areas where the current framework might lead to regulatory arbitrage.

8. The data collection comprised both a quantitative and qualitative questionnaire.

9. The quantitative questionnaire built on existing supervisory reporting requirements and comprised two distinct templates. The first template focused on identifying the main drivers of differences between the prudential and accounting scopes of consolidation. It collected both accounting and prudential balance sheet data, along with details of the adjustments (i.e. related to insurance undertakings, exclusions in the scope of prudential consolidation and in the accounting consolidation) made when moving from accounting to prudential balance sheets. The second template examined the treatment of subsidiaries and participation in other undertakings. It was meant to collect, both for accounting and prudential purposes, information on the type of relationship (e.g. subsidiary), the consolidation method (e.g. full consolidation), the CRR classification (e.g. financial institution), the business activity, among other relevant details.

10. The qualitative questionnaire was designed to collect additional information from institutions on consolidation practices. It covered a range of topics through targeted questions, including group structure, the application of the definitions of 'parent undertaking', 'subsidiary', and 'control', and the definition of a 'financial institution'. Additionally, a dedicated set of questions evaluated the treatment of ancillary services undertakings and of special purpose entities and collective investment undertakings. The questionnaire also collected information on the methods applied for prudential consolidation and the application of Articles 19 and 22 of the CRR. Finally, it examined the anticipated effects and potential impacts of changes in provisions under the CRR3.

11. The sample of institutions considered for the data collection encompassed 70 institutions from 26 EU/EEA countries. These institutions were selected to ensure a representative sample, including global systemically important institutions (G-SII), other systemically important institutions (O-SII) and non-OSII banking groups.

12. Additionally, the sample included specific banking actors such as institutions owned by car manufacturers groups (three institutions), or fintech or digital groups (six institutions), which were identified as relevant for the purposes of this Report. Most institutions in the sample served as the consolidating EU parent institution of their CRR group, with a median number of subsidiaries, joint ventures and associates totalling 44 undertakings[5].

Figure 1. Sample of institutions considered for the ad-hoc data collection

	Included in the sample	Considered for the quantitative analyses
Number of institutions	**70**	**69**
Total accounting assets (in EUR bn)		**23,981**
Number of subsidiaries, joint ventures, associates		**9,722**
Of which subsidiaries		8,141
Of which joint ventures		405
Of which participations		1,041
Of which other		135
Of which institutions between 1 and 10		12
Of which institutions between 11 and 50		24

[5] Only one institution not supervised on a consolidated basis was withheld for the data collection exercise, that was identified of relevance for this report. No quantitative data was collected for this institution.

Of which institutions between 51 and 100	7
Of which institutions between 101 and 500	20
Of which institutions between 500 and more	6

1.3 Prudential consolidation framework in the CRR: rationale, objectives and regulatory provisions

13. The prudential consolidation framework is a core element of the EU banking regulatory regime, in line with the principles established by the Basel Committee on Banking Supervision (BCBS). This element is fully embedded in the EU legislation, with the CRR demanding institutions – and (mixed) financial holding companies – to comply with the requirements laid down therein on their individual[6] and/or consolidated situation, when the conditions set out in Articles 6 or 11 of the CRR are met. This dual-level application ensures that risks are appropriately captured at the individual level of institutions as well as across the broader group structure.

14. Prudential consolidation serves as a key supervisory tool to assess the financial soundness and risk profile of banking groups in a comprehensive manner. It enables competent authorities to identify and monitor risks that may arise from intra-group dependencies (e.g. funding, guarantees, or operational interlinkages), reputational dependencies, or structural arrangements that could otherwise remain obscured under individual supervision. It eliminates double gearing – where the same capital is counted across multiple entities – thus preventing an overstatement of the group's capital. It also curbs regulatory arbitrage by discouraging group structures designed to circumvent prudential requirements. Moreover, it ensures to duly reflect the potential responsibilities of a parent over the liabilities of other undertakings of the group, including situations where such obligations go beyond the value of the share of capital held or which are driven by non-capital interdependencies, such as reputational or operational links.

15. The current regulatory framework on prudential consolidation is set out in Chapter 2 of Title II of Part One of the CRR. Its implementation relies fundamentally on the definitions provided in Article 4(1) of the CRR, which establishes key concepts such as 'parent

[6] In accordance with Article 6 of the CRR, 'institutions shall comply with the obligations laid down in Parts Two, Three, Four, Seven, Seven A and Eight of this Regulation and in Chapter 2 of Regulation (EU) 2017/2402 on an individual basis'.

undertaking', 'subsidiary' or 'financial institution', which are instrumental to determine the scope and the method of consolidation of a prudential group.

16. Both the relevant consolidation provisions and the underlying definitions have recently been amended by the CRR3, with the overarching aim of enhancing the clarity, consistency, and effectiveness of the framework, also in the light of past shortcomings that have been highlighted by the EBA Opinion and Report on other financial intermediaries and regulatory perimeter issues.

17. Building on this revised framework, Article 11 of the CRR sets out the general obligation for parent institutions in a Member State[7] to comply with the prudential requirements on the basis of their consolidated situation. In turn, Article 18 of the CRR defines the scope of prudential consolidation – specifying the types of undertakings to be included in the consolidated situation – and the applicable method of consolidation (i.e. how the financial information of the consolidated undertakings is combined for prudential purposes).

18. The determination of the scope and methods of prudential consolidation is based on the assessment of two distinct criteria. The first criterion relates to the classification of the undertaking in terms of its regulatory status. In accordance with Article 18 of the CRR, only undertakings that qualify as institutions, financial institutions – including ancillary services undertakings – may be included within the scope of prudential consolidation. An exception to this rule is provided in Article 18(8) of the CRR, which allows competent authorities to require full or proportional consolidation of subsidiaries or undertakings in which an institution holds a participation that are not institutions or financial institutions (including ancillary services undertakings), where there is a substantial step-in risk and provided that they are not (re)insurance undertakings. The second criterion concerns the nature of the relationship between a parent undertaking and the different type of undertakings belonging to the group. This includes relationships such as subsidiaries, participation, associates (significant influence), or other qualifying links as referred to in Article 18 of the CRR. In accordance with the CRR, full consolidation constitutes the default approach for institutions and financial institutions (including ancillary services undertakings) that qualify as subsidiaries of a parent undertaking, as set out in Article 18(1) of the CRR. In addition, paragraphs 3, 5 and 6 of Article 18 of the CRR confer discretion upon competent authorities to determine the appropriate method of consolidation in cases involving relationships other than those referred to in paragraph 1. Separately, Article 18(4) of the CRR requires the application of proportional consolidation under specific conditions.

[7] For the purposes of Article 11 of the CRR, this shall also refer to: (a) a (mixed) financial holding company approved in accordance with Article 21a of Directive 2013/36/EU; (b) a designated institution controlled by a parent (mixed) financial holding company where such parent is not subject to approval in accordance with Article 21a(4) of Directive 2013/36/EU; and (c) a (mixed) financial holding company or an institution designated in accordance with point (d) of Article 21a(6) of Directive 2013/36/EU.

19. More specifically, Article 18(3) of the CRR addresses undertakings that are managed on a unified basis by virtue of a contract, memorandum, or articles of association; or where the majority of the administrative, management, or supervisory bodies are composed of the same individuals throughout the financial year until the consolidated financial statements are prepared. Article 18(4) of the CRR requires proportional consolidation when institutions or financial institutions are managed jointly with other non-consolidated entities, and each entity's liability is limited to its shareholding. Article 18(5) of the CRR addresses participations or capital ties that do not fall under the scope of paragraphs 1 and 4 of the same Article. Under Article 18(6)(a) and (b) of the CRR, competent authorities are granted discretion to impose prudential consolidation in cases where there is either significant influence without participation or capital ties, or where single management exists without a formal agreement.

20. Additionally, Article 19 of the CRR sets out exemptions from the inclusion of certain undertaking in the consolidation. It allows institutions or financial institutions which are subsidiaries or in which a participation is held not to be included in consolidation, provided that certain conditions are met – for instance, when these undertakings are deemed immaterial. In such cases, alternative approaches, such as the equity method, may be applied. This provision aims to ensure proportionality, avoiding unnecessary burden for institutions where consolidation would not provide meaningful information regarding the risks posed by those institutions or financial institutions from a prudential perspective.

21. The CRR provisions on consolidation are supplemented by Commission Delegated Regulation (EU) 2022/676 with regard to regulatory technical standards specifying the conditions to carry out consolidation under Article 18(3) to (6) and (8) of the CRR (RTS on methods of prudential consolidation[8]), which aims at ensuring a clear, consistent, and harmonised application of prudential consolidation rules for the cases specified therein.

22. More specifically, the abovementioned RTS:

    a. specify the circumstances under which different consolidation methods (e.g. full consolidation, proportional consolidation, aggregation method, or equity method) should be applied when relationships fall outside the scope of full consolidation under Article 18(1) of the CRR.

    b. guide competent authorities in exercising their discretion under Article 18(3), (5), (6), and (8) of the CRR, by defining:

        i. the conditions that justify the use of proportional or full consolidation;

[8] See Commission Delegated Regulation (EU) 2022/676 .

ii. the circumstances in which the aggregation method should be applied (especially for undertakings under unified management);

iii. the situations in which the use of the equity method may be more appropriate.

c. promote convergence of supervisory approaches across Member States, thereby enhancing comparability and level playing field among institutions.

1.4 Past EBA work on prudential consolidation

23. Over recent years, the EBA has monitored the implementation of prudential consolidation provisions, provided recommendations and drafted regulatory technical standards to strengthen the framework, also mindful of evolving group structures and the need for supervisory convergence across Member States.

24. The EBA's work focused on two primary areas: (i) the assessment of the prudential consolidation perimeter, along with potential inconsistencies within relevant CRR definitions and lack of ability to adapt to emerging risks (e.g. mixed-activity groups (MAG)) and (ii) the specification of the methods for consolidating undertakings within that perimeter.

25. In November 2017, the EBA published an Opinion and Report on other financial intermediaries and regulatory perimeter issues under the CRR and CRDIV[9]. There the EBA highlighted inconsistencies in the interpretation and application of key definitions under Article 4(1) of the CRR – particularly, the notions of 'financial institution' and 'ancillary services undertaking' – which are essential in determining the scope of prudential consolidation under Article 18 of the CRR. Such inconsistencies might have affected the inclusion of undertakings within prudential consolidation groups, potentially leading to an underestimation of risks or unjustified exclusions. In this regard, the EBA stressed the need for greater alignment and proposed follow-up measures (i.e. potential amendments to those definitions) to support harmonised interpretations. Building on this work, the EBA published in April 2021 the Final Report on the RTS of methods of prudential consolidation pursuant to Article 18(9) of the CRR[10].

26. Finally, in February 2022, in the joint ESA response to the European Commission's Call for Advice on Digital Finance, the EBA also identified significant challenges posed by MAGs, particularly in the context of digital finance. In this context, the EBA highlighted that existing prudential consolidation rules under CRR/CRD were not designed to adequately address emerging risks posed by groups that combine financial and non-financial activities – such as BigTech conglomerates offering payment, lending, or

[9] See Opinion and Report.

[10] See Final report on draft RTS on methods of prudential consolidation under Article 18 of the CRR.

investment services. It also stressed that the applicable sectoral prudential consolidation rules (pre-CRR3) did not adequately capture the specific nature and inherent risks of new combinations of activities carried out by MAGs, including BigTech. All in all, the issues observed therein were observed leading to insufficient coverage of risks, potential regulatory arbitrage and level playing field issues compared to groups that are already captured through the consolidation frameworks. Several recommendations were provided regarding the need to enhance the prudential consolidation framework in the light of the new digital landscape.

1.5 Structure of the report

27. This Report is structured in the following sections.

a. Scope of prudential consolidation;

b. Definition of ‘undertaking’;

c. Notion of ‘control’;

d. Definition of ‘financial institution’;

e. Ancillary services undertakings (ASUs);

f. SSPEs, SPV-SECs and CIUs;

g. Exemptions and sub-consolidation regimes; and

h. Other implementation issues.

2. Scope of prudential consolidation

KEY TAKEAWAYS OF THIS SECTION

The EBA found that most institutions show strong alignment between accounting and prudential consolidation scopes, with material differences mainly driven by the treatment of insurance undertakings under Article 18(7) of the CRR. Other discrepancies stem from differences in exemption regimes, exclusion of non-financial entities, and different consolidation methods for accounting and prudential purposes (e.g. proportional vs. equity method in the case of joint ventures).

The observed alignment between the two frameworks appears to be also driven by tendency of some institutions to align the prudential scope with the accounting perimeter. While such practices are not compliant with the CRR provisions governing the extent and manner of inclusion of undertakings in the consolidated situation, a policy question arises as to whether a broader alignment could be justified under specific circumstances.

The EBA suggests to the Commission considering a targeted review to assess the feasibility, costs and benefits of aligning the two frameworks more broadly (**Recommendation 1**). This assessment should consider the existing simplification plans and ensure that prudential objectives are preserved.

In the same vein, the EBA sees merit in refining the scope of Article 18(7) of the CRR to eliminate current inconsistencies and reduce undue burdens for institutions and competent authorities (**Recommendation 2**).

2.1 Background

28. Accounting and prudential consolidation frameworks both determine the perimeter of entities to be included in the consolidated situation of a group. Nevertheless, while closely related, the two frameworks pursue distinct objectives and apply different criteria regarding their respective scope and methods of consolidation.

29. From an accounting perspective, consolidation aims to represent a true and fair view of the group's financial position and performance. In this regard, the scope of consolidation is typically defined following the concept of 'control', and encompasses all subsidiaries controlled by the parent undertaking, irrespective of their business activities. Joint arrangements and associates are generally accounted for using the equity method.

30. By contrast, the prudential scope of consolidation framework, set out in Part One, Title II, Chapter 2 of the CRR, is designed to more precisely capture risks relevant to the

banking and financial activities of the institution's group, along with the risks posed by ancillary services undertakings, and serves as the basis for determining capital requirements. For this reason, the regulatory scope generally only includes subsidiary undertakings that qualify as institutions or financial institutions, while excluding insurance or non-financial subsidiaries that do not give rise to comparable risks. The framework also requires proportional consolidation in the case of joint arrangements and the deduction of certain unconsolidated holdings depending on the type of entity concerned.

31. The different prudential objectives may result in certain differences between accounting and prudential consolidation perimeters and methods of consolidation, in particular for more complex group structures involving mixed financial holdings, insurance undertakings, or joint ventures, however ensuring consistency in the measurement of risks and regulatory capital across institutions.

2.2 Observations

32. The EBA assessment has revealed that, in general terms, the prudential scope of consolidation is broadly aligned with the accounting perimeter. Only a small number of institutions reported material divergences between the two frameworks, with the exception of adjustments related to insurance undertakings.

33. The limited level of divergence may be explained by several factors, including the relative non-substantial investments of EU institutions in entities outside the financial sector. Moreover, greater alignment is anticipated due to the broader range of undertakings subject to consolidation following the amendments introduced by the CRR3 – in particular to the definitions of 'financial institution' and 'ancillary services undertaking' under Article 4(1) of the CRR.

34. The survey also revealed a tendency among certain institutions to align the prudential and accounting scopes of consolidation regardless of the specific provisions of the CRR governing the scope and method of consolidation. This practice may have further contributed to the limited discrepancies observed between the two frameworks. For example, some institutions were found to consolidate, for prudential purposes, certain subsidiaries engaged in non-financial or non-ancillary activities or to deviate from the consolidation methods prescribed by the CRR (e.g. proportional consolidation method for joint ventures) in order to align with the approach used for accounting purposes.

35. The graphs below show in more detail the divergences between accounting and prudential consolidation figures for the institutions included in the survey. As already stated above, the main difference observed relates to the non-inclusion – in the prudential scope of consolidation – of insurance undertakings.

36. Beyond the insurance-related adjustments, other differences observed between the accounting and prudential figures stem from:

    a. the different exemption regimes envisaged by the two frameworks[11];

    b. the non-consideration in the scope of prudential consolidation by some institutions of certain real estate companies (e.g. real estate developers), operational leasing undertakings, and certain special purpose entities; or

    c. the different consolidation methods used for specific types of undertakings which are generally accounted under the equity method for accounting consolidation purposes.

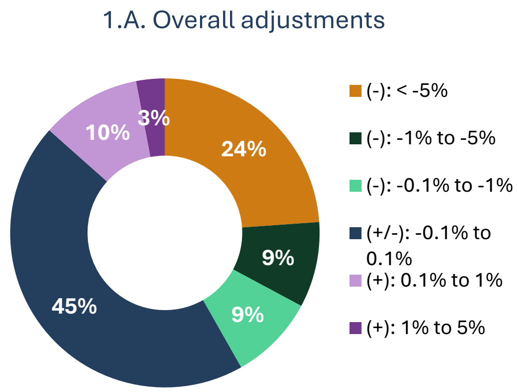
37. Figure 2 presents a breakdown of the different prudential consolidation adjustments and their materiality in terms of total assets. As mentioned before, less than half of the institutions in the sample show significant differences between the two frameworks – i.e. corresponding to situations with more than a 1% total assets difference between the two scopes. This difference seems driven mainly by adjustments for insurance undertakings – concerning around one-third of the institutions. Other adjustments related to the non-consolidation of non-financial undertakings are overall very limited, which were generally related to real estate and operational leasing undertakings[12] (see Section 5) or to special purpose entities[13]. In other limited cases, a relevant impact from the application of the proportional method for prudential consolidation was also reported.

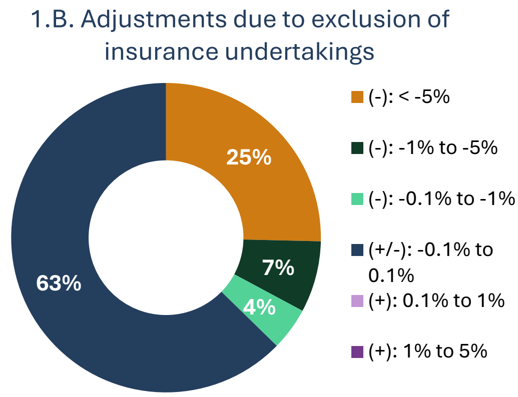
[11] Under Article 19 of the CRR, certain undertakings may be excluded from the scope of prudential consolidation based on specific criteria, such as materiality thresholds or a discretionary decision by the competent authority – provided that predefined conditions are met. These provisions are generally different from the ones envisaged by the applicable accounting standards.

[12] Regarding the non-consolidation of real estate or operational leasing undertakings, in some cases, the reduction in tangible assets (linked to these activities) was also accompanied by an increase in loans and advances. This likely reflects funding provided by institutions to their real estate or leasing subsidiaries to support their operations. As a result, tangible assets are effectively replaced by intragroup loans for prudential reporting purposes.

[13] Concerning SSPEs, some institutions reported an increase in total assets due to the non-consideration of these undertakings in the prudential perimeter. This seems driven by the fact that underlying securitised assets were not derecognised, despite the vehicles not being consolidated. In addition, these institutions also recognised the securitisation notes which led to a double counting effect. This issue is further discussed in Section 6.

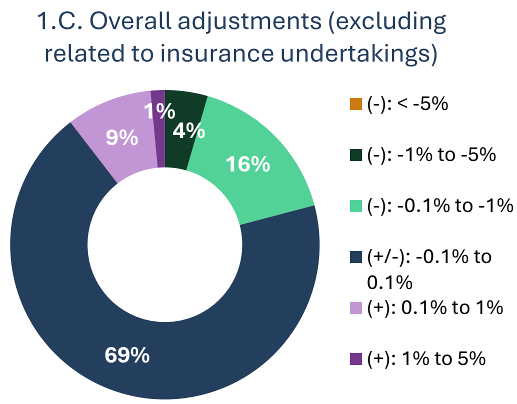
Figure 2. Change in total assets – accounting vs. prudential consolidation

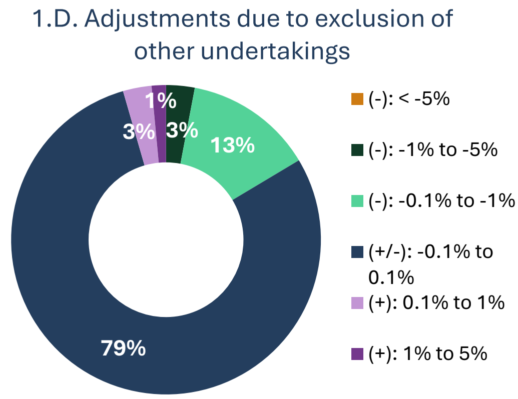




A decrease in the institution's total consolidated assets for prudential purposes (vs. accounting figures) is represented by a negative value.

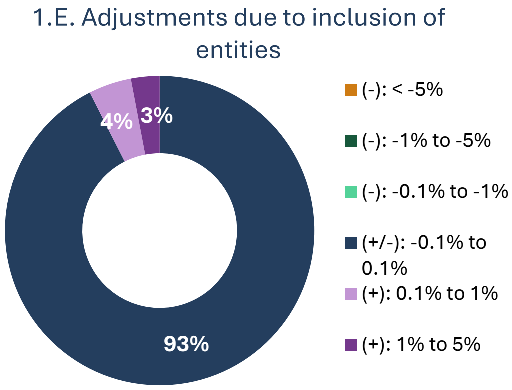
The adjustment for insurance undertakings is the most significant driver of differences between the two frameworks.



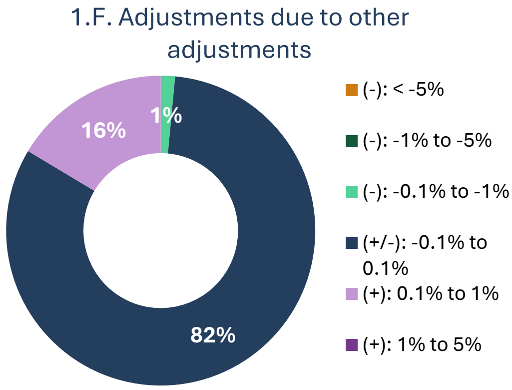


Excluding adjustments for insurance undertakings, significant change is observed for only 5% of institutions. Adjustment for insurance undertakings is made at nominator and denominator level.

Adjustment driven by Article 19 of the CRR and exclusion of non-FSE (in some cases including real estate and operational leasing). Positive adjustment reported due to exclusion of certain securitisation SPVs.



Adjustments driven by the application of the proportional method of prudential consolidation.



Additional correction reported by some institutions related to inclusion/exclusion of entities – e.g. deconsolidation adjustments to equity holdings or intragroup loans due to exclusion of insurance undertakings.

2.3 Conclusion and policy recommendations

38. The analysis appears to confirm the robustness of the prudential framework, which generally ensures that the main types of undertakings that may pose risks to banking groups on a consolidated level are included within the prudential consolidation perimeter. The relative size of undertakings considered under the accounting but excluded from the prudential scope – other than the exclusion of insurance undertakings – is limited and typically justified by the distinct criteria applied in each framework (e.g. exemption regime).

39. A broader coverage of the prudential consolidation perimeter and a more harmonised application of the CRR provisions are also expected following the implementation of the CRR3 and the publication of the Guidelines on ASU. These developments may affect in particular the treatment of certain operational leasing and real estate undertakings, which have so far been excluded from the prudential scope by some institutions.

40. From another perspective, the use of the accounting scope of consolidation also for prudential purposes, as observed in certain institutions, warrants further consideration. Institutions have justified this approach as a means to reduce operational complexity and foster consistency between accounting and prudential reporting processes. Although such practices are not consistent with the current regulatory framework – which clearly sets out its principles for determining the scope and method of consolidation irrespective of the accounting framework – a broader policy discussion may be warranted. This discussion should assess whether the benefits associated with simplification and efficiency for institutions justify a greater degree of alignment between the prudential and accounting framework, both in terms of scope and consolidation methods.

41. Any further alignment of the accounting and prudential scope of consolidation could either be made mandatory or voluntary. Such an approach would allow for the full – or

proportional – consolidation of undertakings that are not institutions or financial institutions, under specific conditions where this would not materially distort the representation of the financial situation and riskiness on a consolidated basis. For example, institutions could be permitted to use the accounting treatment as a reference for consolidating non-financial undertakings, where they consider[14] that there may be the risk of providing financial support in the case of distress (i.e. step-in risk).

42. To ensure consistency of the approach over time, it would be essential to prevent opportunities for regulatory arbitrage or cherry-picking. Moreover, any potential unintended consequences to other elements of the prudential framework – such as the treatment of qualifying holdings in non-financial sector entities – should be carefully taken into account.

43. In the same vein, the EBA sees merit in refining the scope of Article 18(7) of the CRR to eliminate current inconsistencies and reduce undue burdens for institutions and competent authorities. Article 18(7) of the CRR, introduced with CRR2, aimed to establish the equity method as the standard regulatory valuation for subsidiaries consolidated for accounting purposes but not for regulatory purposes (e.g. insurance undertakings). However, the current wording also captures participations non-consolidated in the accounting framework, even when a book value for these investments exists under accounting standards. As a result, smaller entities with valid accounting book values must either apply the equity method for prudential purposes or seek case-by-case exemptions – creating unnecessary divergence and regulatory burden.

Recommendation to the Commission

44. In light of the observed practices and considering the potential benefits in terms of simplification, efficiency and consistency between the two frameworks, the Commission could explore, in the context of future legislative reviews, whether limited adjustments to the Level 1 text may be warranted to allow greater reliance on the accounting scope, provided that the prudential objective of ensuring comprehensive risk coverage remains fully safeguarded.

45. To this end, Commission may consider launching a targeted review to assess the feasibility, cost, benefits and potential impacts of a broader alignment between the scope of the two frameworks (**Recommendation 1**). The EBA stands ready to support the Commission in this exercise.

[14] In the current framework, Article 18(8) of the CRR provides the discretion to require full or proportional consolidation of non-institutions and financial institutions in the case of step-in risk only to the relevant competent authorities.

46. Moreover, to ensure proportionality and consistency, the EBA is of the view that the scope of application of the equity method under Article 18(7) of the CRR should be reviewed to assess the appropriateness of limiting it to cases where no book value of the investment in the subsidiary or participation exists for accounting purposes at consolidated level (i.e. limited to entities that are fully consolidated under the accounting framework) (**Recommendation 2**). This targeted refinement would preserve the original intent of the provision while avoiding misalignment and excessive compliance effort. Notwithstanding, the EBA considers that competent authorities should have the power to require the application of the equity method or another appropriate method where the accounting treatment does not adequately capture the risks that the entity poses to the group. In all cases, the method applied should not result in full or proportional consolidation of the undertaking concerned.

3. Definition of 'undertaking'

KEY TAKEAWAYS OF THIS SECTION

The identification of a 'parent undertaking' and the undertakings which qualify as 'subsidiaries' is essential to determine the scope of prudential consolidation. However, the term 'undertaking' – which underpins both definitions – is not provided by the CRR, leading to divergent interpretations across institutions and Member States.

The definitions of 'parent undertaking' and 'subsidiary' under points (15) and (16) of Article 4(1) of the CRR are linked to the existence of 'control' – within the meaning of point (37) of the same Article – under either Article 22 of the Accounting Directive or the accounting standards to which an institution is subject under Regulation (EC) No 1606/2002. Yet, these frameworks apply only to undertakings that are either listed in Annexes I and II to the Accounting Directive or that are required to prepare consolidated accounts under the applicable accounting framework in accordance with Regulation (EC) No 1606/2002.

In this regard, the EBA survey has highlighted that certain institutions apply a restrictive interpretation and qualify as parent undertaking only the types of undertakings listed in Annexes I and II to the Accounting Directive. Furthermore, in the course of supervisory reviews inconsistent approaches across institutions regarding the qualification of entities without legal personality as subsidiaries have also been observed.

In practice, these approaches may result in the exclusion of certain undertakings – such as partnerships, associations, or foundations – from the prudential consolidation perimeter, even where control exists. This may give rise to inconsistent approaches, where the scope of prudential consolidation is based on undertakings' legal form rather than the (control) relationship between the relevant undertakings.

The EBA considers that a definition of 'undertaking' should be provided for prudential consolidation purposes (**Recommendation 3**). In that regard, a substance-over-form approach would ensure that all undertakings posing material risks to the group are able to be captured, in the manner and form set out by Article 18 of the CRR, within the perimeter of prudential consolidation, enhancing supervisory convergence and reducing the opportunities for regulatory arbitrage.

3.1 Background

47. Overall, the starting point for defining the scope of prudential consolidation and for ensuring compliance on a consolidated basis is the identification of a parent undertaking and its subsidiaries. In this context, the definition and understanding of the term 'undertaking' are fundamental. However, that term is not explicitly defined in the

CRR, leading to potentially inconsistent interpretations across Member States. This may ultimately impact the perimeter of prudential consolidation as well as the level at which consolidated supervision is exercised.

48. In accordance with Article 4(1)(15) and (16) of the CRR, a parent undertaking is defined as an 'undertaking that controls, within the meaning of point (37), one or more undertakings'. And a subsidiary is 'an undertaking that is controlled, within the meaning of point (37), by another undertaking'.

49. Point (37) further clarifies that control refers to 'the relationship between a parent undertaking and a subsidiary, as described in Article 22 of Directive 2013/34/EU, or in the accounting standards to which an institution is subject under Regulation (EC) No 1606/2002 [...], or a similar relationship between any natural or legal person and an undertaking'. This creates two possible bases for assessing the qualification of an undertaking as parent or subsidiary for prudential purposes: (i) control under IFRS 10, for undertakings applying IFRS; or (ii) Article 22 of the Accounting Directive, for undertakings applying national GAAPs (nGAAP). However, certain elements therein raise interpretative uncertainty.

a. Under option (i), Regulation (EC) No 1606/2002 requires companies governed by the law of a Member State to prepare consolidated accounts in conformity with IFRS, as per Article 4 of that Regulation. However, companies that do not fall within the scope of Article 4 are not automatically required to draw up consolidated financial statements, unless such an obligation is introduced by the respective Member State.

b. Under option (ii), Article 1 of the Accounting Directive clarifies that the coordination measures prescribed by that Directive, including Article 22, apply only to the types of undertakings listed in Annexes I and II, provided certain conditions are met.

50. As a result, there might be a risk of interpreting that (i) companies that are not required to prepare consolidated accounts under IFRS, and (ii) entities applying nGAAP and not listed in Annexes I and II to the Accounting Directive, may fall outside of the definition of 'parent undertaking' and 'subsidiary'. This observed misapplication of these definitions might give rise to regulatory arbitrage, whereby banking groups might structure themselves to avoid the consolidation of certain undertakings which, in substance, exercise control over or are controlled by institutions or financial institutions.

51. Risks may thus be shifted to these unconsolidated entities, which at the same time could be incentivised to provide funding to institutions or financial institutions at more favourable terms, ultimately undermining the real capital adequacy and risk profile of the banking group. In addition, key risks factors – such as intragroup relationships, intercompany transactions, embedded leverage or guarantees – may remain outside of the supervision on a consolidated basis, undermining the completeness and accuracy of prudential supervision.

3.2 Observations

52. Data collected by the EBA through its survey on consolidation and questions submitted via the EBA Single Rulebook Q&A tool[15] confirm the lack of clarity on what should be regarded as an undertaking that can be subject to the CRR provisions governing prudential consolidation, in particular for determining whether an undertaking qualifies as parent or subsidiary undertaking.

53. When asked if the qualification as parent undertaking is limited to the types of undertakings listed in Annex I and II to the Accounting Directive, the majority of the institutions included in the sample of the survey responded that the qualification as parent undertaking for prudential purposes should be limited to the types of undertakings listed in those Annexes. Some of the institutions that reported performing this limitation, have a parent undertaking that is included within Annex I and II to the Accounting Directive.

3.3 Conclusion and policy recommendations

54. While the notion of 'undertaking' forms the basis for determining the scope of prudential consolidation, the CRR does not provide a definition of the term. Notably, concepts such as 'parent undertaking' and 'subsidiary' inherently rely on this notion, as they refer to undertakings that either exercise or are subject to control. Accordingly, qualifying as an 'undertaking' is a necessary first step in establishing a parent–subsidiary relationship for CRR purposes.

55. The observations made by the EBA as part of its survey have confirmed the existence of certain implementation issues, largely stemming from divergent interpretations of the term 'undertaking' for prudential purposes, in the absence of an explicit definition in the CRR. This may lead to the exclusion of materially relevant undertakings from the scope of prudential consolidation, even where control exists, which prevents conducting prudential supervision at the proper level of consolidation.

56. The EBA considers that the definitions laid down in points (15) and (16) of Article 4(1) of the CRR are already sufficient to support the interpretation that an undertaking qualifies as a 'parent undertaking' or as a 'subsidiary', irrespective of whether it is listed in Annexes I and II to the Accounting Directive or required to prepare consolidated accounts in accordance with Regulation (EC) No 1606/2002. As emphasised in the Level 1 text, the decisive factor for determining a parent undertaking and its subsidiaries for prudential consolidation purposes is the existence, or absence, of control.

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[15] See EBA Q&A 2021_6082.

57. Nonetheless, the EBA sees merit in providing greater clarity on what constitutes an 'undertaking' for prudential consolidation purposes, as this concept has proven to be a key determinant in identifying which entities fall within the scope of prudential consolidation. In the EBA's view, the concept of 'undertaking' embedded in the CRR definitions should not be limited to entities listed in the Annexes to the Accounting Directive or subject to Regulation (EC) No 1606/2002. Rather, it should encompass a broader range of economic actors which, regardless of their legal form, may effectively exercise or be subject to control.

58. Moreover, assessing whether the introduction of a clear and operational definition of 'undertaking' in the Level 1 text is warranted may be appropriate. Such an explicit definition should be aimed at reducing interpretative divergences across institutions and Member States, thereby enhancing the effectiveness and integrity of consolidated supervision. An activity-based, substance-over-form definition would allow the qualification of parent–subsidiary relationships to be assessed exclusively on the basis of control, ensuring that all entities materially contributing to or bearing risks within a banking group are duly captured in the regulatory perimeter.

59. In this context, expanding the scope of entities captured as undertakings for prudential purposes may also include entities that are not subject to accounting requirements under national law. While this may create practical challenges for carrying out consolidation, the EBA considers that such challenges do not justify excluding these entities from the prudential perimeter, particularly given the different purposes pursued by the accounting and prudential frameworks.

60. Similar cases already exist within the current framework, where entities might be consolidated or required to consolidate despite not being subject to specific accounting requirements (e.g. due to exemption regimes). In such cases, the absence of accounting obligations should not likewise constitute grounds for exemption from prudential consolidation.

61. In view of these implementation challenges, the EBA may consider issuing additional guidance at a later stage to support institutions in carrying out consolidation in a consistent and proportionate manner.

Recommendation to the Commission

62. The EBA recommends that the Commission, in the context of a future legislative review, evaluate whether introducing a clear and functional definition of ‘undertaking’ for prudential consolidation purposes in the CRR may be warranted (**Recommendation 3**). Such definition should ensure that the identification of a parent–subsidiary relationship is triggered by the existence of control, regardless of the legal form of the concerned entities. Such a definition should enable the inclusion in the consolidation perimeter of entities that exercise, or are subject to, control within the meaning of Article 4(1)(37) of the CRR, irrespective of their legal form or the existence of specific accounting requirements.

4. Notion of ‘control’

KEY TAKEAWAYS OF THIS SECTION

The CRR3 defines ‘control’ as the central criterion for identifying parent–subsidiary relationships, which are essential for determining the scope of prudential consolidation under Article 18 of the CRR. Previously, the definitions of ‘parent undertaking’ and ‘subsidiary’ relied heavily on Article 22 of the Accounting Directive, which created some inconsistencies, especially for undertakings applying IFRS.

The revised definition in Article 4(1), point (37) of the CRR now allows to identify control following either (i) Article 22 of the Accounting Directive, for undertakings applying national GAAPs; or (ii) the application of accounting standards to which an institution is subject under Regulation (EC) No 1606/2002, for undertakings applying IFRS, as well as in a similar relationship between any natural or legal person and an undertaking. This dual reference improves alignment between prudential and accounting frameworks, reducing inconsistencies and arbitrage opportunities.

However, interpretative challenges persist, especially regarding: (i) national transpositions of Article 22 of the Accounting Directive, which may lead to jointly controlled undertakings being treated as fully controlled (i.e. subsidiaries), affecting prudential consolidation outcomes; and (ii) the consideration of severe long-term restrictions that substantially hinder a parent’s ability to exercise control over its subsidiary when assessing control under Article 22 of the Accounting Directive.

All in all, the EBA considers that the definition of ‘control’ is deemed suitable for a consistent identification of parent–subsidiary relationships. Limited recommendations are therefore made to the Commission to provide further clarity to address the interpretative challenges observed.

In the EBA’s view, situations that substantially hinder the parent’s control over its subsidiary should be considered within the assessment of control, to prevent recognising as subsidiaries undertakings over which effective rights cannot be exercised (**Recommendation 4**). Moreover, the manner and extent to which an undertaking is included in the consolidated situation shall be carried out in accordance with Article 18 of the CRR and the RTS on methods of prudential consolidation.

CRR3 AMENDMENTS: SECTION HIGHLIGHTS

An important element in determining the perimeter of prudential consolidation is the assessment of a parent–subsidiary relationship, as it is one of the criteria to consider identifying the entities required to be included in the scope of prudential consolidation under the CRR. This identification is based on the notion of 'control', which under the CRR3 is defined as 'the relationship between a parent undertaking and a subsidiary, as described in Article 22 of Directive 2013/34/EU, or in the accounting standards to which an institution is subject under Regulation (EC) No 1606/2002 of the European Parliament and of the Council, or a similar relationship between any natural or legal person and an undertaking'.

Additionally, the CRR3 has amended the definitions of 'parent undertaking' and 'subsidiary' to align these definitions with the control principle. A parent undertaking is now explicitly defined as the undertaking that *controls,* while the subsidiary is the undertaking *being controlled,* as per the meaning of the Accounting Directive or the applicable accounting standards.

4.1 Background

63. Following the changes introduced to the CRR with the last banking package, the notion of 'control' – as defined in Article 4(1)(37) of the CRR – has become the key criterion to establish a parent–subsidiary relationship, which in turn triggers the inclusion of institutions and financial institutions within the scope of prudential consolidation in accordance with Article 18(1) of the CRR.

64. The previous definitions of 'parent undertaking' and 'subsidiary' referred to Article 22 of the Accounting Directive to a larger extent. Accordingly, the identification of a parent–subsidiary relationship was based on the existence of: (i) legal control (i.e. control derived from holding the majority of voting rights or appointment rights), (ii) de facto control (i.e. control exercised in practice, even without a formal majority of voting or appointment rights), or (iii) other cases of effective dominant influence.

65. However, the reliance on the Accounting Directive created practical challenges, especially, for undertakings applying IFRS for accounting purposes, due to divergences from the notion of control embedded in IFRS 10. In fact, IFRS envisages different criteria for identifying control, based on: (i) the power over the investee, (ii) exposure to variable returns, and (iii) the ability to use that power to affect the investor's returns. As a result, the identification of a parent–subsidiary relationship under IFRS did not always coincide with that under prudential rules.

66. To address these issues, the CRR defines 'control' as the relationship between a parent undertaking – i.e. the undertaking that *controls* – and a subsidiary – i.e. the undertaking

that *is controlled* – as described under Article 22 of the Accounting Directive, or under the applicable accounting standards to which the institution is subject to pursuant to Regulation (EC) No 1606/2002. The dual reference is designed to align the prudential and accounting frameworks particularly for institutions applying IFRS, thereby preventing inconsistencies that could arise from relying solely on Article 22 of the Accounting Directive.

67. Despite the changes made by the CRR3 improving the identification of parent undertakings and subsidiaries for prudential purposes, some interpretative challenges remain in the practical implementation of Article 22 of the Accounting Directive when determining control. That Article primarily outlines situations in which a parent–subsidiary relationship exists, and control should therefore be presumed. However, it does not address cases where severe or long-term restrictions prevent a parent undertaking from exercising effective control over a subsidiary. As a result, it may be unclear whether such constraints should also be factored within the assessment of control for prudential purposes, potentially leading to inconsistent applications across institutions.

4.2 Observations

68. Responses to the ad-hoc survey indicate that, in general, there is a clear understanding of the notion of ‘control’ as defined in Article 4(1)(37) of the CRR. The usage of this criterion for identifying a parent–subsidiary relationship is considered more fit-for-purpose and sufficient to eliminate inconsistencies between accounting and prudential frameworks, especially, for undertakings applying IFRS.

69. Interestingly, many institutions remarked that despite the introduction of the control criterion in the revised definition of ‘parent undertaking’ and ‘subsidiary’ within the CRR3, it was already applied in practice. As a result, no major changes were generally expected in the identification of parent undertakings and subsidiaries as the consideration of the existence of control under IFRS 10 was – de facto – already used in practice.

70. Although reported only by a single institution, a specific concern arises in relation to the notion of control embedded in Article 22 of the Accounting Directive and the national transpositions of this provision. In particular, it was noted that, depending on the Member State’s transposition, certain arrangements that are usually considered as joint control may fall under the (national) definition of ‘control’. In practice, this would imply that jointly controlled undertakings would therefore be considered subsidiaries that are fully consolidated under Article 18(1) of the CRR for prudential consolidation purposes. Consequently, the treatment applied to those undertakings differs from the ‘default’ method envisaged by the CRR under Article 18(4) (i.e. proportional consolidation).

4.3 Conclusion and policy recommendations

71. The survey confirms that the definition of 'control' set out in Article 4(1), point (37) of the CRR is considered a sound and appropriate criterion for identifying a parent–subsidiary relationship for prudential purposes. Furthermore, the amendments to the definitions of 'parent undertaking' and 'subsidiary' have contributed to a closer alignment with the accounting framework, thereby reducing opportunities for arbitrage and limiting potential inconsistencies between institutions applying national GAAPs and those applying IFRS.

72. Despite the increased clarity and consistency brought by the reference to control in the definitions of 'parent undertaking' and 'subsidiary definitions', some implementation issues might arise when determining the consolidation perimeter and the applicable method of consolidation, due to potential divergences in the transposition of the Accounting Directive across Member States.

73. In particular, it is unclear whether situations that substantially hinder a parent undertaking's ability to exercise power over a subsidiary should be considered within the assessment of control, particularly for undertakings following Article 22 of the Accounting Directive. That Article provides situations where a parent–subsidiary relationship exists, which are relevant to the determination of control for prudential consolidation purposes. However, unlike IFRS, it does not consider cases where there may be impediments to a parent's effective control over its subsidiary.

74. As a result, control may be presumed to exist in situations where effective rights cannot be exercised (e.g. due to veto or protective rights). This could lead to two types of misrepresentations: (i) from a parent's perspective, an undertaking may be recognised as a parent despite not exercising effective control (e.g. in cases of joint control), and (ii) from a subsidiary's perspective, an undertaking may be classified as a subsidiary even though no entity exercises control over it. In such cases, the consolidated situation of the group may not accurately reflect the underlying economic reality.

75. In addition, specific national transpositions of Article 22 of the Accounting Directive may also affect how the consolidated situation of a group is represented. As observed through the survey, certain jointly controlled undertakings may be classified as undertakings that are controlled (i.e. subsidiaries) for prudential purposes.

76. All in all, the abovementioned situations may:

    a. At the level of the parent undertaking, lead to the representation of full responsibility where the liability is, in fact, proportionate to the share of capital held. Furthermore, it may contribute to classifying the controlling undertaking(s) as parent undertaking for prudential purposes – which may, ultimately, qualify as a (mixed) FHC at the head of a banking group.

b. At the level of the subsidiary, result in its full consolidation by two or more undertakings that do not individually exercise sole control, but rather share it, and where proportional consolidation should be carried out instead.

77. In light of the above, the EBA considers it appropriate to provide further clarity on the consideration of situations that hinder the existence of control for prudential purposes. In particular, the EBA is of the view that such circumstances should be taken into account in the assessment of control to avoid recognising as subsidiaries undertakings over which effective rights cannot be exercised (e.g. due to veto or protective rights).

78. The EBA further reiterates that institutions and (mixed) financial holding companies should be aware that the manner and extent to which an undertaking is included in their consolidated situation shall be carried out in accordance with Article 18 of the CRR and the RTS on methods of prudential consolidation. This implies that even if an undertaking is not considered jointly – but fully – controlled under the national transposition of the Accounting Directive, its inclusion in the scope of prudential consolidation should be determined by Article 18(4) of the CRR, provided that the conditions set out in Article 3 of the RTS on methods of prudential consolidation are met. As such, situations of joint control of an institution or of a (mixed) FHC should not trigger a parent–subsidiary relationship for prudential purposes, that could eventually lead to the qualification of the controlling undertaking(s) as parent (mixed) FHC.

79. The EBA will continue monitoring and further assessing any potential inconsistencies stemming from divergences in the transposition of the Accounting Directive across Member States, in order to evaluate their potential impact on the determination of control under Article 4(1)(37) of the CRR and on the scope of consolidation of banking groups.

Recommendation to the Commission

80. Considering the good implementation among institutions of the concept of 'control' as a relevant criterion for identifying a parent–subsidiary relationship, at this stage the EBA has not identified major potential changes on the prudential framework which may be warranted in this regard. Overall, the definition is considered to be suitable for a consistent determination of the scope of prudential consolidation.

81. The limited implementation issues that have been observed around the definition of 'control' can be generally addressed by a more consistent reading of the current Level 1 text. Notwithstanding, the EBA recommends that the Commission enhance – in the context of future revision of the Level 1 text – the definition of 'control' under Article 4(1)(37) of the CRR to cater for situations where severe long-term restrictions substantially hinder a parent undertaking's ability to exercise rights over its subsidiary (**Recommendation 4**). The revised wording may be articulated as follows: *''control' means the relationship between a parent undertaking and a subsidiary, as described in*

Article 22 of Directive 2013/34/EU, or in the accounting standards to which an institution is subject under Regulation (EC) No 1606/2002 of the European Parliament and of the Council, or a similar relationship between any natural or legal person and an undertaking. <u>For the purposes of this Regulation, when the definition of 'control' set out in Article 22 of Directive 2013/34/EU is applied, control shall be deemed not to exist where severe long-term restrictions substantially hinder the parent undertakings rights over the subsidiary, as laid down in Article 23(9)(c) of Directive 2013/34/EU'.</u>

5. Definition of 'financial institution'

KEY TAKEAWAYS OF THIS SECTION

The definition of 'financial institution' under Article 4(1), point (26) of the CRR is crucial for determining the prudential perimeter of banking groups. It aims to capture a broad range of undertakings engaged in financial or ancillary banking activities that may pose risks to the group. Inconsistent application of the definition could lead to exclusion of undertakings bearing risks to the group, undermining the accuracy of consolidated supervision and allowing for regulatory arbitrage.

The revised CRR3 definition addresses prior inconsistencies and expands the scope to include new or evolving financial business models. These changes aim to promote harmonised application across institutions and Member States.

The EBA notes that despite improvements, some interpretative issues still persist, particularly around: (i) determining the 'principal activity' of a financial institution, (ii) the consideration, or not, of regulated and unregulated undertakings within the assessment of financial institution; and (iii) the qualification of undertakings that manage pension funds as financial institutions.

In light of these findings, the EBA considers opportune that further clarification and guidance is provided to ensure convergence in the following aspects:

- Determination of 'principal activity': a more harmonised approach should be used relying, to the extent possible, on the approach used for financial holding companies. A quantitative assessment based on simple and harmonised indicators could be employed to determine which activity should be considered as prevalent (e.g. indicators such as a predefined share of total assets, revenues, or the personnel). In this regard, the EBA recommends, in the context of a future revision of the Level 1 text, introducing further clarification in the definition of 'financial institution' (**Recommendation 5**).
- Consideration of unregulated undertakings: the definition of 'financial institution' is framed focusing on the activity carried out rather than on the regulatory or supervisory status of the concerned undertaking. The EBA considers that the current definition is already suitable to support the interpretation that an undertaking qualifies as a financial institution regardless of whether it is subject to regulation or supervision under Union or national law.
- Inclusion of companies managing pension funds: the EBA observed uncertainty regarding the qualification of these undertakings as financial institutions under Article 4(1)(26) of the CRR. These undertakings' financial activities and associated risks are not materially different from those of asset management companies already covered by the definition. The EBA therefore recommends their inclusion under Article 4(1), point (26)(b)(ii) of the CRR (**Recommendation 6**).

CRR3 AMENDMENTS: SECTION HIGHLIGHTS

The concept of 'financial institution' is pivotal in shaping the scope of prudential consolidation under the CRR, as it determines which undertakings – along with other institutions – should be included in the consolidated situation of an institution or (mixed) financial holding company subject to the requirements on a consolidated basis in accordance with Article 11 of the CRR. Moreover, the qualification as financial institution also affects the deduction and credit risk regimes under the CRR.

With the CRR3, the definition of 'financial institution' has been refined to better capture the evolving landscape of financial services and to ensure consistency across the regulatory framework. Under the revised framework, an undertaking is considered a 'financial institution' if (i) it qualifies as an investment firm, a mixed financial holding company, an investment holding company, a payment services provider, an asset management company or an ancillary services undertaking, or (ii) if it performs certain financial activities as its principal activity.

In this regard, the CRR3 expands the list of these financial activities to include not only those set out in Annex I of the CRD, but also services or activities referred to in MiFID II, aligning with the existing consideration of investment firms as financial institutions. In addition, activities listed in points 16 and 17 of Annex I to CRD have been included following the changes introduced by Regulation (EU) 2023/1114 on markets in crypto-assets.

At the same time, the CRR3 provides greater clarity by explicitly excluding SSPEs from the definition of 'financial institution', in line with the previous conclusions raised by the EBA in its Consultation Paper of the RTS on methods of prudential consolidation and Q&A 2014_1530. Conversely, ancillary services undertakings, as defined in Article 4(1), point (18) of the CRR, are now directly considered financial institutions, triggering their automatic consideration as financial sector entities, which has direct implications for the deduction and credit risk regimes.

Linked to the revised definition of 'financial institution', the CRR3 has also introduced minor amendments to the definition of financial holding company. The revised definition keeps the reference to a set of thresholds indicators (i.e. 50% of the undertaking's consolidated equity, assets, revenues or personnel) associated with subsidiary institutions or financial institutions, of which, at least one is an institution. Similar to the previous definition, the competent authority may consider other relevant indicators in this regard.

Additionally, a new provision has been introduced whereby on a case-by-case basis, and when decided by the competent authority, an entity may be exempted from the qualification as a financial holding company even if one of those indicators is met. To that end, the CRR3 requires the competent authority to consult the EBA and have due regard of its opinion.

The qualification as financial institution of ASU is not only relevant for the financial sector entity consideration mentioned before, but also in the context of financial holding companies. In this regard, following the CRR3 amendments, ASUs, as financial institutions, may also qualify as financial holding companies where the conditions set out in

Article 4(1)(20) of the CRR are met, as well as compute towards the calculation of the indicators therein when they are subsidiaries.

This change may be particularly relevant for digital or fintech groups that are headed by an undertaking performing activities considered a 'direct extension of banking' or 'ancillary to banking' and that have at least one subsidiary institution. Previously, those undertakings remained generally outside the prudential scope of consolidation but currently, following the CRR3 amendments, undertakings performing these types of activities may fall within the prudential perimeter of consolidation, thereby allowing to better determine the scope and proper level of prudential consolidation, in line with the recommendations highlighted in the Joint ESAs Report on Digital Finance[16].

5.1 Background

82. The definition of 'financial institution' in Article 4(1), point (26) of the CRR is one of key elements for determining the perimeter of prudential consolidation of a banking group. This definition is meant to ensure capturing in the scope of prudential consolidation a wide range of undertakings that are either engaged in financial activities or in providing services ancillary to banking, which ultimately bring risks relevant for a banking group.

83. The link of financial institutions to prudential consolidation is made explicit in Article 18 of the CRR, which requires institutions and (mixed) financial holding companies to consolidate undertakings that qualify as institutions and financial institutions, to the extent and manner laid down therein. An unclear or inconsistent application of this definition may result in the exclusion of undertakings that may pose relevant financial risks, undermining the fair and comprehensive representation of a group's consolidated situation. Therefore, a consistent application should be warranted to reduce any room for potential regulatory arbitrage, preventing groups from transferring risky or highly leveraged undertakings outside the perimeter to avoid their consolidated supervision.

84. Prior to the CRR3, the definition of 'financial institution' was considered prone to inconsistent application across institutions, as already highlighted in the EBA report on other financial intermediaries and regulatory perimeter issues. The amendments introduced were thus aimed at addressing these concerns and promoting a more harmonised application across institutions and Member States. The revised definition has broadened the list of undertakings falling within the scope of consolidation, thereby ensuring the inclusion of new or evolving business models in the financial sector that had previously remained outside its scope.

[16] Joint ESA response to the Commission's Call for Advice on digital finance.

85. Notwithstanding these improvements, the survey results suggest that certain interpretative challenges remain, particularly, within the determination of ‘principal activity’ and the nature or type of undertakings that may qualify as financial institution. These areas may therefore benefit from further clarification, in order to ensure consistent application across institutions and Member States.

5.2 Observations

86. The definition of ‘financial institution’ appears to be generally implemented in a consistent manner, allowing for a proper identification of such undertakings as well as their inclusion the scope of prudential consolidation. Nevertheless, survey responses highlight certain implementation challenges related to specific aspects of the definition, which may undermine the consistent identification of the scope of prudential consolidation, and which warrant further clarification to ensure harmonised practices.

87. For instance, institutions appear to have adopted divergent approaches when determining the ‘principal activity’ of a financial institution. On the one hand, majority of respondents reported relying on quantitative indicators, which in most cases were based on the share of revenues or total assets attributable to a given activity performed by an undertaking. This approach reflects a tendency to align its determination with the indicators provided to identify a financial holding company under Article 4(1)(20) of the CRR. On the other hand, a significant portion of institutions in the sample indicated to rely on qualitative assessments. In these cases, institutions often referred looking at the main business purpose stated in the undertaking’s Articles of Association (AoA), or to its classification within the relevant sector – for instance, through the NACE code – as the basis for determining the principal activity.

88. Another key finding concerns how institutions distinguish between regulated and unregulated activities when qualifying undertakings as financial institutions. In this regard it was observed that the qualification as financial institution was, in some cases, limited only to undertakings that are of ‘regulated’ nature (i.e. those that are to some extent regulated and/or supervised), with the regulatory status generally derived from national law. This creates divergences not only among institutions but also across Member States, leaving room for regulatory arbitrage and a biased assessment of financial institutions.

5.3 Conclusions and policy recommendations

89. Based on the survey results and supporting evidence, the definition of ‘financial institution’ – as amended by the CRR3 – is generally considered appropriate for capturing undertakings engaging in financial activities or ancillary services within the prudential scope of consolidation. Moreover, the amendments have also improved its applicability due to the extension of activities captured therein, including emerging activities such as crypto-related services.

90. However, the application of the definition still leaves room for divergent interpretations, particularly regarding the determination of the 'principal activity' and the treatment of unregulated undertakings. Evidence gathered by the EBA confirms that such divergences may lead to inconsistent consolidation outcomes and potential gaps in the prudential perimeter. Excluding undertakings that, in practice, carry out financial activities as their principal activity, which are comparable to those performed by regulated entities, may result in an incomplete assessment of group-wide risks. Such an approach may also open the door to regulatory arbitrage, incentivising structures that may benefit from more favourable prudential treatment. Taken together, these practices undermine the objectives of Articles 11 and 18 of the CRR, which aim to ensure that prudential consolidation provides a comprehensive and accurate reflection of the risks to which a group is exposed.

91. In light of these findings, the EBA considers opportune that further clarification and guidance is provided on the definition of 'financial institution' under Article 4(1)(26) of the CRR, to promote consistent application and secure a level playing field across institutions and Member States.

Concept of 'principal activity'

92. The EBA considers it appropriate to promote a more harmonised assessment of the principal activity criteria across institutions, relying – to the extent possible – on the approach already established for defining a 'financial holding company' under Article 4(1), point (20) of the CRR.

93. Where an undertaking performs both financial and non-financial activities, a quantitative assessment based on simple and harmonised indicators could be employed to determine which activity should be considered as prevalent. Indicators such as a predefined share of total assets, revenues or the personnel attributable to the different activities could serve as objective criteria, enabling institutions to base their assessments on readily available and verifiable data. This approach would enhance convergence in classification across Member States, improve comparability of supervisory outcomes, and align with the objectives of prudential consolidation. It would also help ensure that undertakings whose business is predominantly financial are appropriately included within the consolidation perimeter.

Unregulated undertakings

94. Point (i) of Article 4(1), point (26)(b) of the CRR lists the activities that when performed by an undertaking, in a principal manner, trigger its qualification as a financial institution. Such definition is framed focusing on the activity carried out rather than on the regulatory or supervisory status of the undertaking concerned. By referring to activities, rather than to a closed list of regulated entities, the provision ensures that undertakings which, in substance, engage in financial activities comparable to those of

regulated entities are captured within the scope of prudential consolidation. This approach is meant to prevent gaps in the consolidation perimeter while mitigating the risk of regulatory arbitrage, by avoiding situations where groups could conduct financial activities through unregulated undertakings to benefit from more favourable prudential treatment.

95. The EBA considers that the current definition of 'financial institution' is already suitable to support the interpretation that an undertaking qualifies as a financial institution regardless of whether it is subject to regulation or supervision under Union or national law, provided that its principal activity consists in the activities referred to in point (i) of Article 4(1), point (26) of the CRR. However, further clarification could be given within the Level 1 text to ensure a more harmonised implementation of the financial institution definition across institutions and Member States, while providing a sounder basis for supervisory follow-up. The EBA will continue to monitor the implementation of this provision in the course of its ongoing work on prudential consolidation.

Undertakings managing pension funds

96. As part of its monitoring on prudential consolidation provisions, the EBA has observed uncertainty regarding the qualification of undertakings which manage pension fund scheme plans and pension fund services as financial institutions under Article 4(1), point (26) of the CRR. A literal reading of the definition of 'financial institution', which refers to asset management companies as defined in Article 4(1), point (19) of the CRR, would imply that such entities are excluded from the scope of the financial institution definition.

97. However, the EBA considers that there is no clear rational for excluding these undertakings, and that their financial activities and associated risks are not materially different from those of asset management companies already covered by the definition. Therefore, companies managing pension fund schemes and services should qualify as financial institutions for prudential purposes.

Recommendation to the Commission

98. In light of the above, the EBA recommends to the Commission considering, in the context of future revision of the Level 1 text, introducing further clarification in the definition of 'financial institution' in point (26) of Article 4(1) of the CRR, with the aim of better specifying the concept of 'principal activity' embedded therein and the treatment of undertakings that manage pension funds (**Recommendations 5 and 6**).

99. Where such enhancement of the definition of 'financial institution' would be deemed appropriate by the Commission, the revised wording may be articulated as follows:

''financial institution' means an undertaking that meets both of the following conditions:
[...]

(b) it meets one or more of the following conditions:

(i) more than 50% of any of the following indicators are associated, on a steady basis, with the ~~principal activity of the undertaking is to acquire or own~~ acquisition or owning of holdings or with ~~to pursue~~ one or more of the activities listed in Annex I, points 2 to 12 and points 15, 16 and 17, to Directive 2013/36/EU, or to pursue one or more of the services or activities listed in Annex I, Section A or B, to Directive 2014/65/EU in relation to financial instruments listed in Annex I, Section C, to Directive 2014/65/EU:

the undertaking's assets based on its individual situation;

the undertaking's revenues based on its individual situation;

the undertaking's personnel based on its individual situation;

(ii) the undertaking is an investment firm, a mixed financial holding company, an investment holding company, a payment services provider as categorised under Article 1(1), points (a) to (d), of Directive (EU) 2015/2366 of the European Parliament and of the Council, an asset management company, a company managing pension funds or an ancillary services undertaking.

6. Ancillary services undertakings (ASUs)

KEY TAKEAWAYS OF THIS SECTION

The qualification as ASUs plays an important role for defining the regulatory perimeter of a banking group under the CRR. Their inclusion ensures that undertakings performing activities closely linked to banking are reflected in the consolidated prudential situation of a group.

The previous definition of 'ASU' was considered vague and inconsistently applied, partly due to conflicts with the wording in Article 89 of the CRR. These inconsistencies led to unequal treatment of similar undertakings, potential regulatory arbitrage, and lack of comparability across institutions.

The revised definition of 'ASU' under Article 4(1), point (18) of the CRR and simplification of Article 89 of the CRR has address the abovementioned issues. To support consistent implementation, the EBA issued guidelines under Article 4(5) of the CRR. These guidelines provide: (a) criteria for determining a direct extension of banking; (b) clarification of what should be considered ancillary to banking; and (c) a framework for identifying similar activities, ensuring responsiveness to emerging risks.

Results of the survey highlighted divergent approaches when determining ASU, which might be also explained by the lack of guidance in the matter at the time of the data collection.

In the case of operational leasing, undertakings were classified as ASUs depending on two main criteria: (i) the identity of the lessee, and (ii) the reliance on banking services. For ownership or management of property, the classification as ASUs was mainly driven by: (i) the use of properties by the institutions/financial institutions of the group, and (ii) properties being acquired through NPL recovery strategy (i.e. repossessed assets). Divergent treatment was observed in the case of property development and housing promotion, with some institutions classifying those undertakings as ASU due to funding links and integration in the group's value chain. Going forward, the EBA will monitor the implementation, among institutions, of the revised definition under the CRR3, as complemented by the additional guidance provided by the EBA Guidelines.

CRR3 AMENDMENTS: SECTION HIGHLIGHTS

Under the CRR3, the concept of 'ancillary services undertaking' has undergone significant changes that impact their treatment within the prudential framework.

First, the definition itself has been amended to reflect that not only undertakings performing, as principal activity, the ownership or management of property, the provision of data processing services or similar activities should be considered ASU but also those that perform activities that consist of: (a) a direct extension of banking; (b) operational leasing, in addition to the activities mentioned above, insofar as those are ancillary to banking; and (c) any other activity considered similar by the EBA to those referred to in points (a) and (b), whether provided to undertakings inside of the group or to clients outside of the group. These changes have been made to remove inconsistencies between Article 4(1), point (18) of the CRR and the existing wording in Article 89 of the CRR, thereby clarifying the scope of ASU and including a broader reference to non-financial sector entities in Article 89 of the CRR.

To specify the concepts embedded in the ASU definition, the EBA has been mandated under Article 4(5) of the CRR to issue Guidelines specifying the criteria for identifying the activities referred to in points (a), (b) and (b) of Article 4(1), point (18) of the CRR.

Second, while under CRR2 ASUs were already included in consolidation in accordance with Article 18(2) of the CRR, the CRR3 amendments have specified that they qualify as financial institutions. This clarification not only confirms their inclusion in the scope of prudential consolidation but also establishes their qualification as financial sector entities under Article 4(1), point (27) of the CRR.

As a result, their qualification as financial sector entities would no longer be limited to those 'included in the consolidated financial situation of an institution' but also to undertakings outside the perimeter of prudential consolidation of a banking group. This has direct implications for the treatment of exposures towards ASUs under both the credit risk framework and the deduction regime.

6.1 Background

100. In the context of the prudential consolidation framework under the CRR, the classification of ASUs plays a pivotal role in determining the regulatory perimeter of a banking group. Their inclusion ensures that undertakings which, while not institutions themselves, perform activities that are closely linked to core banking functions are fully reflected in the consolidated situation of the group, comprehensively and accurately representing the risks that the banking group is exposed to.

101. The qualification as ASUs is not only relevant within the prudential consolidation framework, but also in the deduction regime and credit risk requirements due to the amendments by the CRR3. This is because ASUs are now directly considered financial

institutions and, as such, financial sector entities (FSEs) in accordance with Article 4(1), point (27) of the CRR.

102. Prior to the CRR3, the definition of 'ASU' under Article 4(1), point (18) of the CRR was considered vague and subject to inconsistent application across institutions. These inconsistencies were partly due to divergences with the definition provided in Article 89 of the CRR, which created uncertainty regarding the scope of undertakings to be included in the scope of this definition. This has led to undertakings performing similar activities being treated differently, leading to potential gaps in the perimeter of consolidation.

103. Such inconsistencies have undermined the level playing field, created regulatory arbitrage and hampered the comparability of prudential requirements. In light of these issues, the EBA stressed the need for greater clarity and convergence in the prudential treatment of ASUs[17].

104. Following the changes introduced by the CRR3, the abovementioned issues have been duly addressed within the updated definition of ASU. Additionally, Article 89 of the CRR has been simplified to cover generically only undertakings which are non-financial sector entities thereby avoiding previous inconsistencies with Article 4(1), point (18) of the CRR.

105. According to the revised Level 1 text, ASUs now include undertakings whose principal activity – whether provided to undertakings inside or to clients outside the group – consists of: (a) a direct extension of banking; (b) operational leasing, the ownership or management of property, data processing services or other activities insofar as those activities are ancillary to banking; and (c) any other activity considered similar by the EBA. This change reflects a more functional and risk-based approach, aiming to ensure that undertakings performing activities that are inherently of financial nature or that are clearly linked or connected to banking operations are appropriately captured within the prudential consolidation perimeter.

106. However, certain concepts within the new definition – such as 'ancillary to banking', 'direct extension of banking', and 'similar activities' – were deemed to require further specification. To address this, the EBA has been mandated under Article 4(5) of the CRR to publish guidelines specifying the criteria for identification of activities referred to in Article 4(1), point (18) of the CRR. These guidelines, as published by the EBA, provide simple and consistent criteria to specify the abovementioned aspects. They aim to harmonise the implementation and identification of ASU, enhance legal clarity, promote convergence across Member States, and allow to capture all relevant risks at consolidated level while adapting to evolving business models.

[17] See the EBA Opinion and Report on regulatory perimeter issues.

107. More in particular, they provide:

a. criteria for identifying activities that constitute a direct extension of banking, such as those that are fundamental to the value chain of core banking services;

b. clarification of what is considered ancillary to banking, including activities that support, complement or rely on banking;

c. a framework for assessing whether other activities are similar in nature and risk profile to those already listed, ensuring responsiveness to emerging sources of risk.

6.2 Observations

108. In light of the revised definition provided by the CRR3 and to better inform the publication of the guidelines on ASUs, the EBA has assessed implementation issues and the key observations derived from it revealed a number of recurring challenges and interpretative divergences, identifying the areas where further clarification may be needed.

Operational leasing

109. One of the most important amendments introduced by the revised definition of ASU under the CRR3 concerns the explicit inclusion of operational leasing among the activities that are relevant to the qualification of an ASU.

110. A majority of institutions indicated that they would generally classify undertakings performing operational leasing activities as ASUs. However, different practices have been observed regarding the criteria and conditions to determine whether such activities are ‘ancillary to banking’. Some institutions reported considering the ancillary requirement to be satisfied on a general basis, while others reported applying specific internal criteria to perform the ancillary assessment. According to the responses received, these criteria included:

a. an assessment of the identity of the lessee, with the ancillary condition considered met when the lessee is the institution itself, other institutions or financial institutions within or outside the group, or the institution’s clients;

b. an assessment of the undertaking’s reliance on banking services, such as creditworthiness assessments, marketing of the products, or the financing of the assets by the institution.

111. Other institutions stressed the use of expert judgment without a structured or documented assessment process. These approaches may also reflect the absence of clear regulatory guidance on the application at the time of the survey.

Ownership or management of property

112. The results of the EBA survey indicated that, following the CRR3 amendments, no significant changes are expected by institutions on the classification of undertakings carrying out, as principal activity, ownership or management of property.

113. The main criteria indicated by institutions to discriminate when the ownership and management of property is considered an ancillary activity, is the existence of a link or connection with the banking business. This link was generally identified when the activity of these undertakings supports the activity of the banking group; this covers situations where:

    a. properties owned or managed by the concerned undertaking are used by the institutions or financial institutions of the group as branch offices or main headquarters;

    b. properties owned or managed by the concerned undertaking are acquired in the course of non-performing loans (NPLs) recovery strategy (i.e. repossessed assets).

114. In the case of undertakings owning or managing properties for development or housing promotion, activities were differently classified across institutions. Some viewed these activities as not directly connected to their banking or financial business, resulting in the application of the equity method to those undertakings, when subsidiaries, in accordance with Article 18(7) of the CRR. In contrast, other institutions recognised the existence of significant funding links between them and the housing development subsidiaries, noting that these undertakings formed part of the group's business value chain as their business were financed by the institution's deposits.

115. More broadly, the observed diversification into real estate-related activities (e.g. property development, transaction intermediation or management of investment properties for customers) seems to be regarded by some institutions as a natural extension to their traditional role as lenders, allowing them to participate in the entire end-to-end real estate acquisition process. The observed diverse treatment of these activities underlines specific interpretative challenges, reflecting the need for clear regulatory guidance.

116. The abovementioned findings therefore highlight the need for further clarification to ensure consistent classification practices, particularly in cases involving non-repossessed assets, but where a significant link or connection to banking exists.

Data processing services

117. Institutions generally demonstrated a clear understanding of how to classify undertakings providing data processing services, with the definition being interpreted broadly to encompass a wide range of IT solutions relevant to their financial activities.

118. Most respondents indicated that such undertakings were directly considered ASUs, reflecting their role in supporting core banking functions. Other institutions applied a more structured approach, using internal criteria to assess whether the services provided met the conditions of being ancillary to banking, as now required by the CRR3. In these cases, the classification varied on the extent to which data processing services directly supported the institution's activity, or more broadly served or contributed to the business operations of institutions, financial institutions or other ASUs (e.g. credit institutions, payment services or portfolio management undertakings) of the group. The processing of data generated as part of institutions' operations was also highlighted as a key factor in the assessment.

119. Importantly, most respondents indicated that the classification as ASU was not limited to undertakings providing services only within the group but also to external clients, provided these services were linked to banking operations, in line with the CRR3 definition.

120. However, while institutions have indicated that the link to banking is a key factor in determining the qualification as ASUs, their responses suggest that many still do not have in place a formalised process to assess this connection. This finding may in any case reflect the lack of regulatory guidance on several aspects at the time of the survey, which should be tackled in the EBA Guidelines on ASU aimed to support a more harmonised and transparent approach when determining if data processing services are ancillary to banking.

Other activities of ASUs

121. Several institutions reported having undertakings, either subsidiaries or participations, whose activities are considered a direct extension of or ancillary to banking but which are not among those specified in Article 4(1), point (18) of the CRR. In general terms, these undertakings were already consolidated under the CRR2, except in the case of participations – subject to the equity method – or when exempted under Article 19 of the CRR.

122. These activities included, among others: (i) support or administrative functions to the institution's financial activities (e.g. bookkeeping, procurement, call centers, in-house consulting, staff training, logistical support, risk management, back-office operations or human resources); (ii) loan management activities including loan processing, collateral management and valuation or distressed debt management; (iii) IT services to the group not classified as 'data processing services'; (iv) real estate support activities such as property appraisal, consulting or transaction intermediation; (v) leasing support activities; (vi) loan or equity-funding brokerage services; (vii) support to payment services such as processing of payments; and (viii) debt collection and related advisory services.

6.3 Conclusion and policy recommendations

123. The qualification as ASUs within the prudential consolidation framework has long been subject to divergent interpretations, particularly regarding the scope of activities considered within the previous definition under Article 4(1), point (18) of the CRR[18]. While undertakings providing data processing services have been generally recognised as ASUs, the qualification of other activities – such as the ownership or management of property – was heterogeneous in practice.

124. With the changes introduced under the CRR3, the scope of ASUs has been enlarged to include not only undertakings engaged in operational leasing, but also any other undertaking that is 'direct extension of banking', ancillary to banking' or 'any other activity considered similar by the EBA'. This change should allow the capture of a wider range of undertakings performing activities that generate risks worth to be reflected in the consolidated situation of a banking group.

125. The inclusion of activities considered as 'a direct extension of banking' in the definition allows to qualify as ASU undertakings that provide services closely integrated to the banking value chain. From another perspective, the introduction of the criterion 'ancillary to banking' serves as an appropriate basis for determining the qualification as ASUs. In this regard, it is worth noting that the revised definition expressly links the ancillary criterion with banking in general, replacing the former approach where it was more narrowly connected to supporting or auxiliary functions vis-à-vis the principal activity of one or more institutions.

126. Anchoring the notion of 'ancillary' to banking ensures capturing not only undertakings providing operational support to a banking group, but also those that complement the banking business or operate with a significant reliance on banking products or services, including relevant sources of funding. This more nuanced understanding of 'ancillary' is more effective in reflecting the evolving business models that may give rise to material risks for banking groups, while ensuring that activities lacking a substantive connection to banking, and thus posing minimal risks to the banking business, are appropriately excluded.

127. Finally, the inclusion of 'similar activity' under point (c) of Article 4(1)(18) of the CRR ensures the necessary degree of flexibility to capture undertakings carrying out activities comparable to those of 'direct extension of banking' and 'ancillary to banking'. This allows for the inclusion of undertakings whose activities, although not expressly

[18] Previous to the CRR3, Article 4(1), point (18) of the CRR provided that an '"ancillary services undertaking' means an undertaking the principal activity of which consists of owning or managing property, managing data-processing services, or a similar activity which is ancillary to the principal activity of one or more institutions'.

captured within the other categories, are relevant in the prudential consolidation of a banking group.

128. Notwithstanding these improvements, certain concepts may still lack sufficient clarity, which could lead to inconsistent classification and uneven implementation across institutions. This, in turn, may result in relevant undertakings being left outside the prudential consolidation perimeter, despite their significance for the banking group's risk profile.

129. In order to mitigate the abovementioned risks and to ensure a consistent application of the definition of ASUs, the EBA has been mandated to develop guidelines to further specify the activities referred to in Article 4(1), point (18) of the CRR. This mandate allows to specify the concepts embedded therein, such as 'direct extension of banking' and 'ancillary to banking'. The guidance introduced by the EBA is intended to address the interpretative challenges that have been observed, building on best practices identified. By providing a more structured and comprehensive framework for the classification of ASUs – including detailed criteria for specific activities and the interpretation of newly introduced concepts – the guidelines aim to promote consistency and transparency in the application of the prudential consolidation framework. A brief overview of the criteria identified by the EBA on these concepts is reported below[19].

Direct extension of banking

130. The Guidelines clarify that undertakings performing activities that are closely integrated into the core banking value chain, such as loan servicing, creditworthiness assessments, and the management of repossessed assets, should be classified as ASUs.

Ancillary to banking

131. The qualification of an undertaking as ASU is not determined solely by the nature of the activity itself, but rather the existence of a clear link or connection with banking. In that regard, the Guidelines establish a test to assess whether the activities are sufficiently connected to banking to be considered ancillary to it, based on whether the activity supports, complements, or relies on banking.

Other similar activity

132. Finally, for other similar activities, the Guidelines set out a process and criteria for identifying emerging or hybrid activities that, while not explicitly listed, may pose

[19] Institutions are expected to rely on the Guidelines on ASU published by the EBA to determine which activities should be considered relevant for the qualification of an undertaking as ASU.

comparable risks or dependencies and should therefore be captured within the ASU perimeter. These clarifications aim to ensure that all undertakings whose activities are materially linked to banking – whether through operational, financial, or strategic dependencies – are consistently and appropriately classified as ASUs across institutions and jurisdictions.

Recommendation to the Commission

133. At this stage, the EBA does not put forward additional recommendations in this area. Going forward, the EBA will monitor the implementation, among institutions, of the revised definition under the CRR3, as complemented by the additional guidance provided by the EBA Guidelines. This will be essential to ensure that the term 'ancillary services undertaking' is applied consistently across institutions and Member States, and that all relevant undertakings are appropriately captured within the prudential perimeter.

7. SSPEs, SPV-SECs and CIUs

7.1 Securitisation special purpose entities (SSPEs) and other special purpose vehicles used to set up securitisations (SPV-SECs)

KEY TAKEAWAYS OF THIS SECTION

Securitisation special purpose entities (SSPEs) are bankruptcy-remote vehicles established solely to undertake securitisation transactions. Institutions may pursue different objectives when entering into such transactions.

(i) Funding-driven transactions, structured primarily for funding or refinancing purposes. In these cases, there is typically no significant risk transfer (SRT), and the originator is required to continue holding regulatory capital against the underlying securitised exposures.

(ii) Capital relief SRT transactions, structured with the objective of achieving regulatory capital relief. In these transactions, a substantial portion of the credit risk associated with the securitised assets is transferred to third-party investors.

Observed consolidation practices for SSPEs indicate that their prudential treatment has generally been influenced by the approach applied for accounting purposes. In transactions meeting the SRT criteria the assets have typically been derecognised, and the SSPEs not consolidated by the originating institutions.

Conversely, for funding-driven securitisations, institutions have generally retained the securitised assets on their balance sheets in accordance with the IFRS recognition and derecognition principles, and have also consolidated the related SSPEs, notwithstanding their classification as non-financial sector entities for regulatory purposes.

Additionally, institutions noted that, in such cases, the non-consolidation of the SSPEs would result in the unusual outcome of recognising both the underlying securitised assets (as the derecognition criteria were not met) and the retained securitisation notes (arising from the deconsolidation of the vehicle). This treatment has a material impact on the leverage ratio, as both exposures are reflected on the prudential reporting figures.

In this regard, the EBA considers the recognition of retained securitisation positions in the consolidated situation of an institution inappropriate in non-SRT transactions. Additionally, it recommends that the Commission conduct a targeted review to assess whether the current prudential framework sufficiently addresses the interaction of the consolidation provision with leverage ratio framework (**Recommendation 7**).

Securitisation special purpose entities (SSPEs)

7.1.1 Background

134. A securitisation special purpose entity (SSPE), as defined in Article 2(2) of the Securitisation Regulation[20], refers to a bankruptcy-remote vehicle that is specifically designed to hold securitised assets and to manage the risks and cash flows associated with them. These entities are central to the securitisation process because they provide the legal and operational structure through which exposures are isolated from the balance sheet of the originator and channelled to investors.

135. In prudential terms, SSPEs perform a critical function in ensuring that securitisation structures remain robust and resilient to the insolvency of the originator or sponsor. Their proper functioning is particularly important in the context of securitisations designated as 'simple, transparent and standardised' (STS), where the reliability of the SSPE contributes directly to compliance with the STS requirements. For example, the SSPE structure underpins key elements such as the segregation of assets, the enforceability of risk-retention provisions, and the transparency of cash-flow arrangements.

136. In this context, SSPEs are employed in different types of securitisations, which pursue distinct regulatory and economic objectives:

    a. Funding-driven securitisations: in these transactions, the SSPE issues securities that are typically fully retained by the originating institution, or where the senior notes are sold externally but the subordinated and residual notes are retained. The main objective is not to transfer credit risk but to convert illiquid assets (e.g. mortgage portfolios) into securities that can be pledged as collateral for repos or central bank refinancing operations, for external refinancing operations or for internal liquidity management. Since there is no significant transfer of risk to external investors, the originator must continue to hold capital against the underlying exposures, and no capital relief is achieved.

    b. Capital relief (SRT) securitisations: here, the SSPE issues notes that are sold to third-party investors, thereby transferring a substantial portion of the credit risk associated with the securitised assets. The CRR provides, under Articles 243 and 244, that an originator may obtain a reduction in its capital requirements if it can demonstrate that significant risk transfer has been achieved. The SSPE is crucial in this context, as it provides the legal framework to ensure that the transferred risk is genuinely segregated from the originator and enforceable in all circumstances.

[20] Regulation (EU) 2017/2402.

137. As noted, the CRR3 introduced a relevant clarification to the treatment of these entities by explicitly excluding SSPEs from the definition of 'financial institution'. This amendment formally prevented their classification as financial sector entities, with important implications for credit risk treatment, deduction requirements, and the prudential consolidation framework.

7.1.2 Observations

138. The survey highlighted divergent practices among institutions in determining whether SSPEs should be included within the scope of prudential consolidation. In particular, it was noted that the prudential treatment of such vehicles varied based on the underlying purpose of the securitisation, namely whether the transaction is structured as a funding-driven securitisation (with notes fully retained by the originator and/or no significant risk transfer) or as a capital-relief securitisation aimed at achieving significant risk transfer.

139. When a securitisation achieves significant risk transfer (SRT), the originating institution is generally no longer exposed to the risks and rewards of the securitised exposures. As a result, the originator is typically not deemed to control the SSPE under the applicable accounting framework. The absence of accounting control is equally relevant for prudential purposes, since the definition of a parent–subsidiary relationship under the CRR is anchored to the accounting notion of control. This, in turn, leads to the non-consolidation of the SSPE, irrespective of its qualification as financial institution. In such cases, the explicit exclusion of SSPEs from the definition of 'financial institution' under the CRR3 is – *de facto* – less relevant for determining scope of prudential consolidation, which is already driven by the control criterion.

140. In contrast, in funding-driven securitisations, the institution generally continues to bear the risks and rewards of the securitised exposures and may therefore be considered to control the SSPE, leading to its consolidation for accounting purposes. In such circumstances, the prudential relevance of the SSPE qualification as a financial or non-financial institution becomes decisive for determining its inclusion in the scope of consolidation. Under the CRR3 revision, SSPEs are expressly excluded from the definition of 'financial institution', with the result that, despite being consolidated at accounting level, they should not be consolidated for prudential purposes due to their non-financial nature.

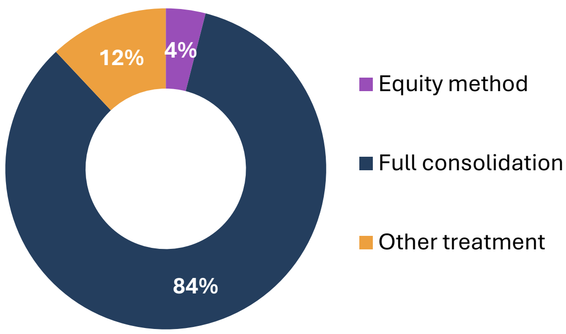
141. Notwithstanding these considerations, it was observed that there was a tendency by many institutions to generally consolidate SSPEs when they are used for funding-driven securitisation, aligning the prudential treatment to the one used for accounting. These practice result in disregarding the specific CRR provisions that require consideration of the financial nature of the undertaking as a condition for inclusion within the consolidation perimeter. This approach was generally aimed at ensuring that, where the originating institution retained substantially all risks and rewards of the securitised

assets (i.e. no SRT criteria met), the related exposures remained reflected in the consolidated situation of the institution.

142. In addition, certain institutions have indicated that not classifying SSPEs as financial institutions may result in a misalignment between the accounting and regulatory scope of consolidation, potentially leading to double counting in the determination of the leverage ratio, in cases where securitisations are conducted without risk transfer, such as those undertaken solely for liquidity purposes.

143. According to these institutions, if the SSPE is consolidated for accounting purposes under IFRS 10 but excluded from prudential consolidation, it would result in the recognition – in the prudential balance sheet of the institution – of both the underlying securitised loans and the notes issued by the SSPE and subscribed by the institution[21]. This double counting may lead to a potential distortion in the fair representation of an institution's leverage ratio.

Figure 3. Prudential treatment of SSPEs in the case of 'control'



7.1.3 Conclusions and policy recommendations

144. The CRR3 exclusion of SSPEs from the definition of 'financial institution' provides clarity on the prudential treatment applicable to such entities with respect to the determination of the scope of prudential consolidation.

145. Specifically, the non-consideration of financial status for SSPEs in the CRR provisions is considered consistent with the nature of the activities carried out by these vehicles, which are exclusively established to hold securitised exposures and issue notes,

[21] Based on responses received, it is assumed that despite the transfer of loans being recognised as a true-sale, the securitised assets would not meet the derecognition criteria under IFRS 9 due to retaining substantially all risks and rewards on these exposures, while the institution would simultaneously recognise the securitisation notes in its balance sheet.

exercising little or no discretion in managing the underlying assets, and not providing other services to third parties, including institutions or other financial institutions. The CRR amendment has also allowed to align the Level 1 text with previous clarifications provided by the EBA in the Q&A 2014_1530[22] and in the Final Report on the RTS on methods of prudential consolidation.

146. Regarding the implementation of such amended definition, it is noted that the exclusion of SSPEs has generally not affected the determination of the consolidation scope for vehicles involved in securitisations achieving SRT. In such cases, the absence of control – resulting from the transfer of significant risks and rewards – led to the non-consolidation of these vehicles, in line with the accounting framework.

147. Conversely, certain challenges seem to arise when SSPEs are used in funding-driven securitisations (i.e. when risk transfer is not achieved), due to the interaction and divergent treatment between the accounting practices followed by some institutions and prudential rules. In these instances, originating institutions may be incentivised to consolidate these vehicles for prudential purposes – despite not meeting the financial nature criterion for prudential consolidation – to ensure that the consolidated situation of the institution reflects only the securitised exposures. This is done to avoid potential double counting – relevant for the determination of the leverage ratio – that could occur if the vehicles were not consolidated. In this regard, the EBA also notes that under the leverage ratio framework, Article 429a of the CRR provides some exemptions to the calculation of the total exposure measure that only addresses cases where SRT is achieved, without providing specific provisions for securitisations that do not meet the SRT criteria.

148. Having considered the above and mindful of the prudential objectives underpinning the consolidation framework, the EBA is of the view that:

a. if the transaction achieves SRT, only the risk stemming from any retained securitisation positions should be reflected from a prudential perspective. In such cases, the exclusion of SSPEs from the definition of 'financial institution' prevents those entities to be eventually considered for consolidation purposes[23];

b. if the transaction does not achieve SRT, the underlying securitised assets should typically continue to be recognised in the consolidated situation of the institution, in line with accounting requirements for recognition and derecognition. Nonetheless, given the explicit lack of financial nature envisaged by the CRR3 for SSPEs, those

[22] See the EBA Q&A 2014_1530.

[23] Due to the achievement of the SRT, these vehicles should generally not be consolidated also for lack of a control situation. In other cases, the application of the criteria for significant risk transfer (SRT) established in Article 244 of the CRR would already mitigate the occurrence of a substantial risk of step-in which may be used to justify the consolidation of the SPPEs under Article 18(8) of the CRR.

vehicles cannot be consolidated for prudential purposes, even if this would be used as practical expedient to avoid double counting issues. In these circumstances, the EBA however considers inappropriate to simultaneously recognise the retained securitisation notes, as doing so would not ensure an appropriate representation of the degree of financial leverage of an institution.

c. in case the institution is not the originator of the securitisation (e.g. it acts as the sponsor or as a relevant investor in the securitisation), the SRT criteria would not be applicable. In such cases, the competent authority should assess, on a case-by-case basis, whether there is a substantial risk of step-in that may justify the application of full or proportional consolidation for prudential purposes, in accordance with Article 18(8) of the CRR.

149. In light of the issues highlighted and divergent approaches observed in the prudential consolidation of SSPEs involved in funding-driven securitisations, the EBA considers appropriate for the Commission to conduct a targeted review to assess whether the current prudential framework sufficiently addresses the interaction of the consolidation provision with leverage ratio framework (**Recommendation 7**). In this regard, the provisions under Articles 247 and 337 of the CRR for determining own funds requirements could serve as a useful reference for developing a consistent policy stance to eliminate any risk of potential double counting in the leverage ratio determination.

Recommendation to the Commission

150. In light of the divergent approaches observed on the prudential consolidation of SSPEs involved in funding-driven securitisations, the Commission may evaluate conducting a targeted review to assess the existence of any potential issues related to the interaction between the prudential consolidation provisions applicable to SSPEs and the leverage ratio framework. This review should assess whether the current framework provides sufficient clarity and consistency, and, where necessary, propose adjustments to prevent any risks of potential double counting in the leverage ratio.

151. The EBA stands ready to support the Commission in this exercise, including through the provision of technical expertise and data analysis, with a view to ensuring that any potential policy response is proportionate, risk-sensitive, and consistent with the overarching objectives of the prudential framework.

Other special purpose vehicles used to set up securitisations (SPV-SECs)

7.1.4 Background

152. SPV-SECs are special purpose vehicles established to set up securitisations but that do not meet the criteria to qualify as SSPEs according to Article 2(2) of Regulation (EU) 2017/2402. Unlike SSPEs, which are established for the sole purpose of

carrying out securitisations, the activities of which are limited to those appropriate to accomplishing that objective and that may benefit from preferential regulatory treatment, SPV-SECs are typically structured in a more complex fashion and for this reason do not allow achieving similar treatment.

153. In particular, institutions often use SPV-SEC structures in the context of more complex securitisation transactions, or where the transaction cannot fully satisfy the regulatory conditions required for capital relief. This may include non-standard securitisations, transactions involving non-STS assets, or cases where the risk transfer is partial and does not meet the relevant SRT criteria.

7.1.5 Observations

154. Survey responses indicate that – similar to the treatment of SSPEs – institutions have generally aligned the prudential consolidation treatment of SPV-SECs with their accounting treatment, consolidating these vehicles when a control relation was established. This approach was often linked to the fact that the related securitised assets were not derecognised for accounting purposes, given the assessment of risks and rewards being retained by the institution. Overall, responses did not suggest a materially different treatment of SPV-SECs compared to SSPEs, as both types of vehicles were typically assessed on a similar basis, despite the potentially more complex structures involved in SPV-SECs.

7.1.6 Conclusions and policy recommendations

155. The survey feedback indicates that institutions generally did not differentiate in their treatment of SPV-SECs as compared to SSPEs. However, unlike SSPEs, the treatment of SPV-SECs is not explicitly addressed in the amended CRR3. As a result, it is worth reminding that institutions should assess on a case-by-case basis whether such vehicles qualify as financial institutions or ASUs, in line with the definitions provided in Article 4(1), point (26), and (18) of the CRR, respectively.

156. This assessment should in particular evaluate any activities performed by the vehicle beyond carrying out securitisation transactions. In that respect:

a. if the entity qualifies as a financial institution or an ASU, the relevant provisions of Article 18(1) to (6) of the CRR would apply, depending on the specific circumstances;

b. in other cases, the undertaking would generally fall outside the scope of prudential consolidation, unless Article 18(8) of the CRR is applied. In such cases, the competent authority may still require full or proportional consolidation where a substantial risk of step-in is identified.

157. Nevertheless, considering that – in the case of SPV-SECs – similar issues may arise to those encountered with securitisation vehicles meeting the SSPE criteria, comparable considerations would also apply in these situations.

7.2 Collective Investment Undertakings (CIUs)

KEY TAKEAWAYS OF THIS SECTION

Different practices have been observed for the treatment of collective investment undertakings (CIUs), which highlights the need for clearer regulatory guidance to ensure risks stemming from these vehicles are adequately addressed in prudential terms.

Particularly, proper classification of CIUs as financial or non-financial entities is crucial, as this classification impacts the application of appropriate prudential treatment, especially when CIUs engage in activities similar as those of institutions or financial institutions.

In this regard, it is important to be reminded that CIUs would not generally qualify as financial institutions under Article 4(1), point 26 of the CRR, and therefore not be included in the scope of prudential consolidation, unless, in the competent authority's opinion, there is a substantial step-in risk and Article 18(8) of the CRR is applied. However, in more specific cases where their principal activity consists in pursuing any of the services or activities of a financial institution listed in Article 4(1), point (26)(b)(i) of the CRR, such as lending or the provision of guarantees, classification as financial institutions would be required to ensure adequately reflecting the underlying risks in the consolidated situation of an institution or a (mixed) financial holding company. In the same vein, while CIUs generally would not qualify as ASU, certain limited circumstances may still justify such classification, such as when they perform an activity which could be considered a 'direct extension of banking' in accordance with Article 4(1), point(18)(a) of the CRR. However, even in these cases, unless CIUs qualify as subsidiaries or are jointly controlled, their prudential consolidation would depend on the assessment of step-in risk by the competent authority[24]. In this regard, the EBA – consistent with previous clarifications provided[25] – considers that the dedicated treatment established in Article 132 and 152 of the CRR for exposures in the form of units or shares in CIUs is generally deemed to be appropriate and the risk of step-in may be largely addressed through the application of the EBA Guidelines on limits on exposures to shadow banking entities.

All in all, the EBA considers the current consolidation framework applicable to CIUs fit-for-purpose but calls for continuous monitoring to evaluate the sound implementation of the framework and its suitability to address new source of risks.

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[24] In accordance with Article 18(5); (6), point (a); and (8) of the CRR and following the criteria in Commission Delegated Regulation (EU) 2022/676 ('RTS on methods of prudential consolidation').

[25] See feedback table of Final report on draft RTS on methods of prudential consolidation.

7.2.1 Background

158. Collective investment undertakings (CIUs) are defined in Article 4(1), point 7 of the CRR as undertakings consisting of either undertakings for collective investment in transferable securities (UCITS) or alternative investment funds (AIFs).

159. These undertakings are particularly relevant to the prudential framework as institutions often hold investments in, or provide lending to, these undertakings, which may significantly impact their risk profile and associated capital requirements. Investments in CIUs may in fact entail market and credit risks linked to the underlying assets, as well as concentration and counterparty risks.

160. In this regard, the CRR framework establishes specific provisions for the prudential treatment of units or shares in CIUs, including look-through approaches to the underlying exposures, as well as standardised treatments where sufficient information is not available. These requirements are intended to ensure that capital requirements are commensurate with the actual risks and to avoid regulatory arbitrage through the use of collective investment structures.

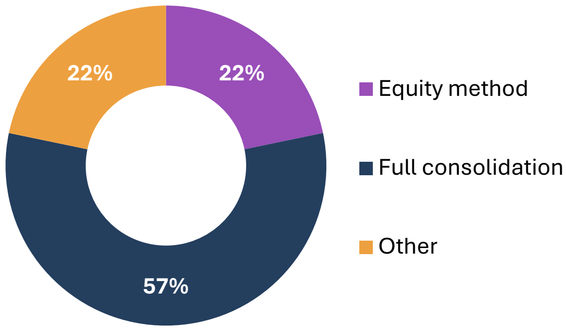
161. Additionally, in some limited cases, CIUs can also perform as principal activity services or activities of a financial nature, such as lending or the provision of guarantees. This may impact the classification of those entities as financial institutions and trigger their inclusion in the scope of prudential consolidation of an institution or a (mixed) financial holding company.

7.2.2 Observations

162. A variety of approaches have been observed regarding the prudential consolidation of CIUs and their qualification as financial institutions. Specifically, around half of the institutions in the sample aligned their accounting and prudential practices, fully consolidating CIUs when a control relation was identified. Conversely, other institutions did not prudentially consolidate these entities in similar situations.

163. While the specific drivers of these different practices could not be determined from the data collected, it appears that some institutions generally preferred to align the two scopes of consolidation and, as a result, did not always carry out a detailed assessment of the underlying activities of these funds to determine the appropriate prudential treatment. The observed heterogeneity in the treatment of CIUs underscores the need for clearer guidance to ensure that the risks associated with these exposures are adequately captured by the prudential framework, either by the application of the dedicated requirements on CIUs provided by the CRR, or by means of a fully-fledged consolidation process.

Figure 4. Prudential treatment of CIUs in the case of 'control'



7.2.3 Conclusion and policy recommendations

164. The EBA acknowledges that Articles 132 and 152 of the CRR already set out a dedicated treatment for exposures in the form of units or shares in CIUs – which requires the application of a 'look-through' approach. This specific prudential treatment ensures that capital requirements appropriately capture the risks arising from indirect exposures to underlying assets that are not held directly by institutions. Accordingly, exposures in the form of units or shares of collective investment undertakings should, as a general principle, be evaluated in accordance with these specific provisions, as they are designed to align prudential requirements with the economic substance of the risks assumed.

165. Nonetheless, it should be noted that the existence of this specific framework doesn't exclude – *a priori* and in limited circumstances – the application of the prudential consolidated provisions and the requirement to assess if a CIU may qualify as financial institution. In some situations, the qualification of a CIU as financial institution and the eventual inclusion in prudential consolidation may, in fact, better address the prudential risks of associated with investments (i.e. holdings or lending) in CIUs.

166. The appropriate qualification of CIUs as either financial institutions or non-financial sector entities, serves, therefore, a dual purpose:

   a. First, it determines the need for consolidation of these undertakings in cases of control. Specifically, while from a capital perspective, the CRR treatment of units or shares in CIUs under the 'look-through' approach would ensure to appropriately represent the bank's share of risk in the fund, in specific situations where the fund engages in activities similar as of banking, the full consolidation may better capture the inherent risk characteristics of the undertaking, including any risk of potential support in the case of distress.

b. Second, where an institution provides debt financing to CIUs (e.g. leveraged funds), the classification as financial sector entities ensures the application of the prudential credit risk treatment appropriate for that asset class. This ensures that the systemic risk profile of lending to entities whose activities closely resemble those of banks is duly taken into account.

167. In this respect, the EBA considers the current CRR framework to well address the specificities of CIUs. In particular, as clarified in the EBA Q&A 2015_2383[26] and other EBA work[27], CIUs are generally not regarded as financial institutions or financial sector entities, unlike asset management companies. Accordingly, CIUs should be, in normal situations, excluded from prudential consolidation, unless the competent authority considers there is a substantial risk of step-in and Article 18(8) of the CRR is applied[28].

168. Nevertheless, the above clarifications do not prevent to assess situations where CIUs pursue, as principal activity, one or more of the activities of a financial institution as provided in Article 4(1), point (26)(b)(i) of the CRR, such as lending or the provision of guarantees, which may lead to the qualification of these CIUs as financial institutions. Such as qualification may arise in very specific situations, for example in the case of a 'loan-originating AIF' as defined in Directive (EU) 2024/92 whose principal activity is the origination of loans. This ensures consistent treatment of these activities irrespective of the legal form of the undertaking performing them and prevents regulatory arbitrage, particularly in cases where CIUs are fully controlled by institutions and traditional banking services are transferred to such funds for the sole purpose of avoiding the inclusion in the regulatory perimeter.

169. In the same vein, it should be emphasised that, while CIUs generally would not qualify as ASU – as noted in the EBA Guidelines on ASUs, certain limited circumstances may still justify such classification. For example, a potential situation in which foreclosed assets are transferred to a fund in the direct or indirect interest of the institution. In such specific cases, the activity carried out would, in fact, effectively amount to a direct extension of banking under Article 4(1), point (18)(a) of the CRR and the criteria provided in the EBA Guidelines on ASU. In this situation, even if the main activity of the undertaking may not be explicitly listed in Annex 1 of the CRD, they may also qualify as ASU. The transfer of certain activities or assets to another entity should not be used as a means to circumvent CRR requirements, and accordingly, in this situation, the competent authority should be able to exercise consolidated supervision over such

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[26] See the EBA Q&A 2015_2383.

[27] See summary of responses to the consultation and the EBA's analysis for RTS on the methods of prudential consolidation.

[28] In this regard, the EBA deems that step-in risk would already be largely mitigated by the specific treatment set out in Articles 132 and 152 of the CRR for exposures consisting of units or shares in CIUs.

undertakings, particularly when the institution remains substantially exposed to its risks.

170. However, even in these cases, unless CIUs qualify as subsidiaries or are jointly controlled, their prudential consolidation would depend on the assessment of step-in risk by the competent authority[29]. In this regard, the EBA – consistent with previous clarification provided[30] – considers that the dedicated treatment established in Articles 132 and 152 of the CRR for exposures in the form of units or shares in CIUs is generally deemed to be appropriate and the risk of step-in may be largely addressed through the application of the EBA Guidelines on limits on exposures to shadow banking entities.

Recommendation to the Commission

171. All in all, the EBA deems the current framework well equipped to address the treatment of CIUs and at this stage no further recommendations are put forward in this regard. Nevertheless, the evolving nature of these activities calls for continued scrutiny and assessment of emerging trends to identify potential new risks or structures that could create opportunities for regulatory arbitrage. The EBA will therefore continue its monitoring on the implementation of consolidation provisions on CIUs also to identify any further needs of regulatory actions.

[29] In accordance with Article 18(5); (6), point (a); and (8) of the CRR and following the criteria in Commission Delegated Regulation (EU) 2022/676 ('RTS on methods of prudential consolidation').

[30] See feedback table of Final report on draft RTS on methods of prudential consolidation.

8. Exemptions and sub-consolidation regimes

8.1 Exclusions from the scope of prudential consolidation under Article 19 of the CRR

KEY TAKEAWAYS OF THIS SECTION

Article 19 of the CRR provides a mechanism to exclude certain undertakings from the scope of prudential consolidation, ensuring that consolidation remains proportionate and risk sensitive.

Survey responses indicate that Article 19(1) of the CRR is widely applied by institutions. On the other hand, the application of Article 19(2) of the CRR has been limited. Overall, the provision to exclude certain entities from the scope of consolidation under Article 19 of the CRR provides institutions with necessary flexibility and eased the implementation of the regulatory framework.

However, the EBA has identified certain areas where further regulatory guidance may be required to promote convergence in the application of Article 19 of the CRR.

The EBA recommends the Commission, in the context of a future legislative review, to consider further clarifying some implementation issues on the application of Article 19 of the CRR (**Recommendation 8**). In this regard, the EBA is of the view that the measurement method for the holdings in undertakings excluded from the scope of prudential consolidation under Article 19 of the CRR is expected to align either with (i) the method used for accounting purposes or (ii) the equity method. Additionally, these holdings would need to be considered for the FSE deduction regime. For the calculation of the relative materiality threshold under Article 19(1)(b) of the CRR, the EBA considers that the percentage of total assets and off-balance sheet items should be determined with reference to the standalone (accounting) balance sheet of the parent undertaking or of the undertaking holding the participation.

8.1.1 Background

172. As highlighted in other parts of this Report, under the CRR framework, institutions and financial institutions belonging to a banking group (i.e. subsidiaries, joint ventures) are required to be included in the consolidated situation of the parent institution or (mixed) financial holding company. This ensures that risks existing within the group are appropriately captured, preventing double gearing or circumvention of prudential rules. However, in certain limited circumstances, consolidation may not be necessary or

proportionate, for instance where the consolidation of the undertaking is of non-material relevance to the group as a whole.

173. To cater for those situations, Article 19 of the CRR sets out exemptions to the inclusion of subsidiaries or participations in institutions and financial institutions within the scope of prudential consolidation. The provision allows a limited and proportionate derogation from the general principle of consolidation set out in Articles 11 and 18 of the CRR, while ensuring that the exclusion does not undermine the effectiveness of the consolidated prudential framework.

174. In this regard, paragraph 1 of Article 19 of the CRR allows the exclusion of non-material subsidiaries or participations in these undertakings from the consolidated prudential scope, provided the relevant thresholds criteria are met. In other words, this provision permits the non-inclusion of undertakings that are of limited size and therefore considered bearing negligible risks to the risk profile of the group on a consolidated basis.

175. Likewise, paragraph 2 of the same Article permits, on a case-by-case basis and at the discretion of the competent authority, the exclusion of subsidiaries or participations in undertakings from the consolidated prudential scope under other specified situations. This may apply where the undertaking is located in a third country and there are legal impediments to obtaining necessary information, where the undertaking concerned is of negligible interest for supervisory purposes, or where consolidation would be inappropriate or misleading for the objectives of supervisions.

176. Overall, Article 19 of the CRR enables a more flexible, risk-sensitive consolidation regime within the CRR, where institutions may avoid operational burdens by not consolidating undertakings that are considered immaterial for the purposes of consolidated supervision.

8.1.2 Observations

177. The survey feedback reveals that Article 19(1) of the CRR has been widely applied, with approximately half of institutions in the sample making use of the exemption provision. Conversely, feedback received indicates that Article 19(2) of the CRR has been used in only a very limited number of cases.

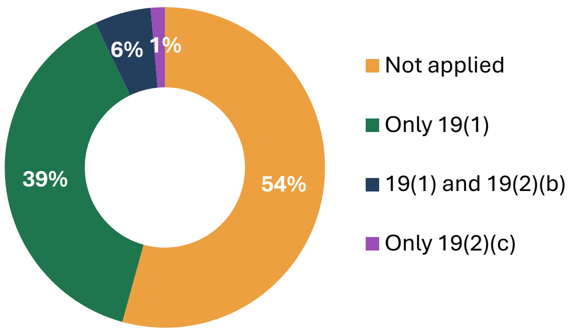
178. As a general observation, institutions' use of Article 19(1) of the CRR seems generally in line with regulatory and supervisory expectations. Many undertakings exempted from consolidation concerned undertakings in run-off with no or limited assets and/or undertakings that were not consolidated for accounting purposes. The total assets of

the undertakings excluded are overall negligible, representing on average 0.07%[31] of the total consolidated assets of the EU parent undertakings.

179. Survey results indicate that Article 19 of the CRR has been generally applied in an appropriate manner by institutions and provided valuable flexibility when implementing the framework. Nevertheless, some heterogeneity of practices on the valuation method and the treatment under the FSE deduction regime of those entities not consolidated under Article 19 of the CRR was observed. In this regard, institutions have reported using different measurement methods (e.g. equity method, fair value measurement, cost) to account for their holdings in entities excluded from consolidation due to the application of Article 19 of the CRR and not always considering these excluded entities for the application of the FSE deduction regime.

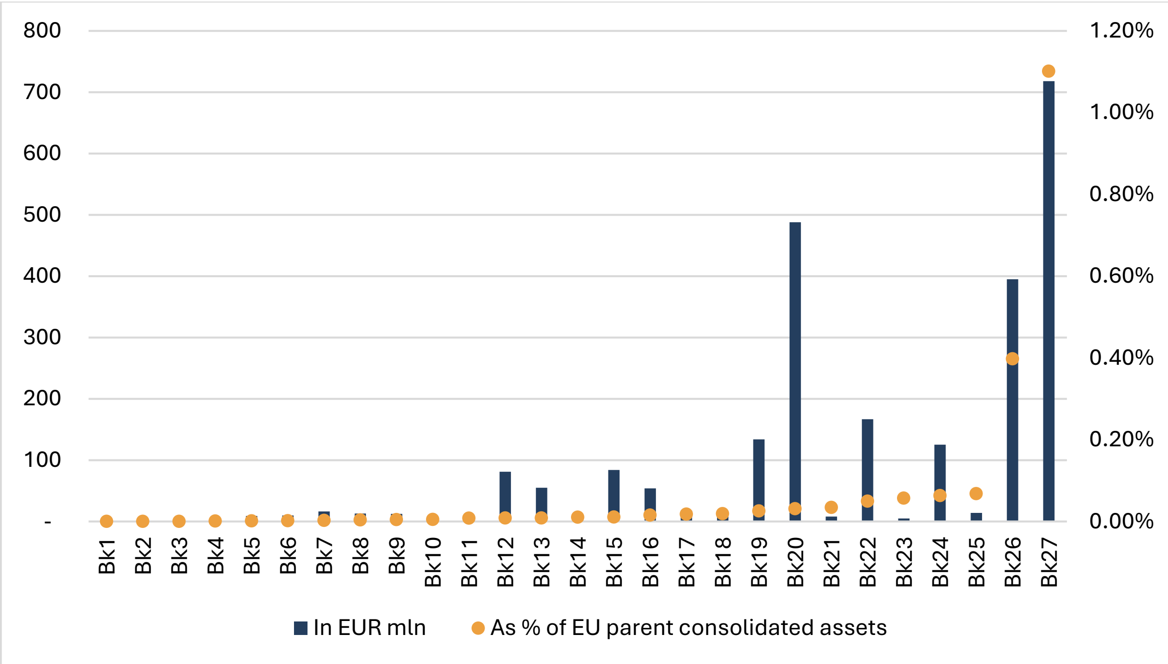
180. In the course of supervisory activities, certain inconsistencies were also observed in how the relative 1% materiality threshold under Article 19(1), point (b) of the CRR is applied – specifically, whether it should be based on accounting or prudential figures, and whether it should be calculated on a standalone or consolidated basis.

Figure 5. Application of Article 19 of the CRR – Exclusion of entities from the scope of consolidation



[31] Two institutions' outlier values are observed corresponding to (i) a potential data quality issue due to reporting a single entity excluded with total asset far exceeding the EUR 10 million regulatory threshold, (ii) exclusion driven by the application of Article 19(2) of the CRR. Average excluded assets reduce to 0.02% adjusting for these two outlier cases.

Figure 6. Size of undertaking(s) excluded from the scope of prudential consolidation under Article 19 of the CRR



8.1.3 Conclusion and policy recommendations

181. Insights obtained by the EBA via the survey highlight that the provision to exclude certain entities from the scope of consolidation under Article 19 of the CRR provides institutions with necessary flexibility and eased the implementation of the regulatory framework.

182. Nonetheless, the EBA has identified certain areas where further regulatory guidance may be required to promote consistent implementation of the consolidation exemption regime, particularly regarding: (i) the measurement of holdings in entities excluded from consolidation for prudential purposes, and (ii) the deduction of such holdings under the FSE deduction regime. Additionally, it is considered warranted providing other clarifications on the practical application of the relative materiality threshold under of Article 19(1), point (b) of the CRR.

183. On the first aspect, it is EBA's view that the valuation metrics to be used for the valuation of holdings in undertakings exempted under Article 19 of the CRR should either consider (i) the equity method, in cases where the exempted entity is consolidated for accounting purposes, or (ii) the valuation method used for accounting purposes in other cases.

184. With respect to the second aspect, the EBA would like to clarify that in the case of exemption from consolidation requirement the holdings in institutions and financial institutions shall be subject to the FSE deduction regime under Article 36(i) of the CRR.

185. On the last aspect, the EBA see merits in further specifying the calculation of the relative materiality threshold under Article 19(1), point (b) of the CRR. In this regard, the EBA considers more appropriate ensuring that institutions use – to calculate the percentage of the total amount of assets and off-balance sheet items – the accounting balance sheet of the parent undertaking or the undertaking that holds a participation. This is because the usage of the prudential figures may be practically unduly burdensome, requiring the application of additional adjustments (e.g. application of Article 19 of the CRR). Additionally, the usage of the standalone (separate) balance sheet of the parent undertaking is considered the most suitable reference, ensuring a simple and consistent application of this provision, and also acknowledging that undertaking may not necessarily be required to produce consolidated accounts for accounting purposes.

186. While the application of this guidance can already be derived from a systematic interpretation of the text of the CRR, targeted amendments to the Level 1 provisions may be considered to further enhance the clarity.

Recommendation to the Commission

187. In light of the findings, the EBA recommends that the Commission, in the context of a future legislative review, consider further specifying explicitly in the Level 1 text that (**Recommendation 8**):

a. Holdings in institutions and financial institutions that are exempted from prudential consolidation pursuant to Article 19 of the CRR should be subject to the deduction regime for holdings in financial sector entities (FSE) under Article 36(1)(i) of the CRR. For this purpose, such holdings should be valued either (i) using the equity method, or (ii) using the valuation method applied for accounting purposes.

b. For the calculation of the relative materiality threshold under Article 19(1)(b) of the CRR, the percentage of total assets and off-balance sheet items should be determined with reference to the standalone (separate) accounting balance sheet of the parent undertaking or of the undertaking holding the participation.

8.2 Sub-consolidation requirements under Articles 11(6) and 22(1) of the CRR

KEY TAKEAWAYS OF THIS SECTION

Sub-consolidation requirements under Articles 11(6) and 22(1) of the CRR ensure that prudential supervision remains comprehensive and effective when risks of a banking subgroup would otherwise not be adequately captured under the general consolidated supervision framework. Moreover, they ensure that subgroups within a banking group are adequately capitalised and subject to appropriate risk management on a sub-consolidated basis. They also enable competent authorities to exercise effective supervision by improving the monitoring of material entities at relevant levels within the group structure.

The EBA survey revealed that those provisions are relevant in a non-negligible number of cases. This confirms the importance of a sound implementation of those provisions. In this regard, the EBA has observed, in the course of ongoing supervisory review, the existence of relevant application issues.

Against this background, the EBA considers relevant providing additional guidance to improve consistency in their application going forwards. To this end, the EBA highlights certain recommendations which the Commission could take into account in the context of a future revision of the Level 1 text (**Recommendations 9, 10 and 11**).

8.2.1 Background

188. Article 22(1) of the CRR requires subsidiary institutions – or intermediate FHC or intermediate mixed FHC – to apply sub-consolidated requirements in cases where they have an institution or a financial institution as a subsidiary in a third country or hold a participation in such an undertaking. Likewise, Article 11(6) of the CRR also envisages the application of sub-consolidation requirements to an institution – at the request of the competent authority – under other specific circumstances.

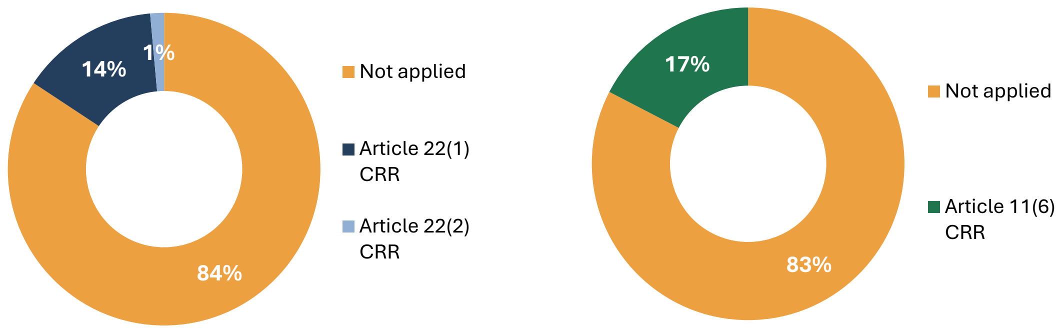
8.2.2 Observations

189. The survey highlighted that sub-consolidation requirements are applied in a non-negligible number of cases, confirming their practical relevance within the prudential framework.

190. Specifically, 14% of the sampled institutions reported applying Article 22(1) of the CRR in relation to entities located in third countries. In this regard, only one institution reported making use of the derogation provided under Article 22(2) of the CRR. In addition, sub-consolidation requirements under Article 11(6) of the CRR were reported

as being applied – following a request of the relevant competent authority – by 17% of institutions, indicating a meaningful level of implementation across the sample.

Figure 7. Application of sub-consolidation requirements under Articles 22 and 11(6) of the CRR



8.2.3 Conclusion and policy recommendations

191. Sub-consolidation requirements are an important feature of the prudential consolidation framework that ensure the application of complementing prudential requirements and the prudential supervision of relevant sub-levels of a banking group.

192. In this regard, the EBA survey revealed that those provisions are relevant in a non-negligible number of cases. This evidence confirms the importance – from a regulatory and supervisory perspective – of a sound implementation of those provisions among the concerned institutions. Nevertheless, the EBA notes the existence of relevant application issues, which have been generally identified by competent authorities in the course of their ongoing supervisory review, in some cases also reflected in outstanding Q&As.

193. Against this background, the EBA considers relevant that additional guidance to concerned institutions may be needed on some specific aspects, to improve consistency in their application going forward. Such guidance can already be derived from a systematic interpretation of the CRR. Additionally, the EBA puts forward a series of recommendations to the Commission, which could be taken into account in the context of a future revision of the Level 1 text, with the aim of clarifying the scope and application of the relevant requirements.

Application of Part Two of the CRR

194. Under paragraph 1 of Article 22 of the CRR, subsidiary institutions or subsidiary intermediate (mixed) FHC ‘shall apply the requirements laid down in Articles 89, 90 and 91, and Parts Three, Four and Seven and the associated reporting requirements laid down in Part Seven A on the basis of their sub-consolidated situation’ if they have an institution or a financial institution in a third country that is their subsidiary or in which they hold a participation. From the wording of that Article, doubts have arisen whether compliance with all other Articles in Part Two of the CRR would be required, as mentioned in the EBA Q&A 2023_6765[32]. However, without the application of Part Two of the CRR in full, an undertaking would not be able to comply with the requirements referred to in Article 22(1) of the CRR.

195. In this regard, the EBA would like to highlight that a systematic interpretation should be applied and, when applying Article 22(1) of the CRR, an undertaking subject to Article 22(1) of the CRR should also comply with Part Two of the CRR in full, and not only with Articles 89, 90 and 91 of the CRR.

Application of Article 22 of the CRR in the case of a chain of subsidiaries

196. The level at which the sub-consolidation requirements are set in Article 22(1) of the CRR is at the situation of the subsidiary institution or subsidiary intermediate (mixed) financial holding company. However, in practice, doubts on the correct application of this provision might arise when dealing with complex group structures. This is because groups may be structured in a chain of successive layers of subsidiaries, where the third-country institution may be (indirectly) held by an EU subsidiary that is not the last (i.e. lowest) subsidiary of that chain[33]. In that case, different interpretations of the level at which Article 22 of the CRR shall be applied have been observed in practice, with some institutions applying multiple ‘sub-consolidation perimeters’ to be carried out and reported. As a result, multiple layers of sub-consolidation are unnecessarily created, which highlights the need to establish the appropriate level of sub-consolidation where risks are supervised.

197. The EBA considers that the application of Article 22 of the CRR in the case of a chain of subsidiaries should not result in undue multiplication in the number of sub-consolidating layers, except when it is justified by supervisory considerations. Therefore, where the structural organisation of the group comprises institutions – or intermediate FHC or intermediate mixed FHC – arranged in a chain of subsidiaries, Article 22 of the CRR should only apply to the last subsidiary institution – or intermediate

[32] See the EBA Q&A 2023_6765.

[33] See the EBA Q&A 2022_6454 and 2019_4711.

FHC or intermediate mixed FHC – in the Union which is the (direct or indirect) parent undertaking.

Sub-consolidation is triggered by the IFR instead of the CRR

198. Issues have also been spotted regarding the interaction between the sub-consolidation requirements envisaged under the CRR and those of Regulation (EU) 2019/2033 (IFR). In particular, questions submitted to the EBA[34] stressed that it is not clear whether the existence of consolidated requirements under Article 7 of the IFR, may be regarded as equivalent to the one under Article 22 of the CRR, providing the possibility to avoid sub-consolidation as required by the CRR.

199. For this reason, the EBA notes that that the sub-consolidated requirement under the CRR and the consolidated requirement under the IFR follow two distinct prudential regimes and cannot be regarded as equivalent. Therefore, the consolidated requirement at the level of the investment firm pursuant to the IFR does not provide a basis to discharge from applying the sub-consolidated requirement pursuant to Article 22 of the CRR.

Treatment of indirect third country subsidiaries for the 10% threshold

200. Another issue identified concerns the calculation of the 10% threshold in Article 22(2) of the CRR to determine whether a group may avoid applying the relevant sub-consolidation requirements. According to Article 4(1), point (16) of the CRR, both direct and indirect subsidiaries should generally be included when assessing the 10% threshold. However, uncertainty arises when indirect third-country subsidiaries have already been sub-consolidated at a lower level within the EU. The issue is whether those same entities should be counted again at a higher level of sub-consolidation for the calculation of the exemption threshold.

201. The EBA considers that that the application of Article 22 of the CRR should not result in an undue multiplication in the number of sub-consolidating layers, except when it is justified by supervisory considerations. For the purpose of determining whether the 10% threshold is exceeded, any third-country subsidiary that is already captured in a lower layer of sub-consolidation in the Union based on Article 22 of the CRR does not have to be taken into account again for the purpose of determining whether the threshold is exceeded for other entities.

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[34] See the EBA Q&A 2021_6274.

Calculation of the 10% threshold under Article 22(2) of the CRR

202. Similarly, the EBA notes that uncertainty arises on how the 10% threshold should be applied – specifically, whether it should be calculated using the subsidiary institution's standalone (separate) balance sheet or its sub-consolidated balance sheet – in order to ensure consistent application across institutions.

203. The EBA is of the view that the 10% threshold under Article 22(2) of the CRR should be calculated on the basis of the standalone (separate) balance sheet of the subsidiary institution – or intermediate FHC or intermediate mixed FHC. This is because the undertaking may not otherwise be required to produce sub-consolidated accounts, and this method would ensure the most simple and conservative application of the provision.

Recommendation to the Commission

Application issues of Article 22 of the CRR

204. Certain aspects of the application of Article 22 of the CRR, as outlined above, have been identified as requiring further clarification to promote greater consistency in their implementation. While a systematic interpretation of the existing provisions would already permit the application of this guidance, the EBA recommends that the Commission consider incorporating some of these clarifications in a future revision of the Level 1 text, in order to ensure more uniform application across institutions (Recommendation 9).

Derogation to the application of Article 22 of the CRR

205. The EBA evaluated whether the automatic application of sub-consolidation requirements under Article 22 of the CRR was in all situations necessary to achieve supervisory objectives. The evaluation highlighted that the mandatory and automatic nature of this requirement may, in some cases, prevent competent authorities exempting institutions from that obligation when sub-consolidated requirements do not provide additional supervisory insight or are not proportionate to the risks involved.

206. In particular, the assessment noted that for certain groups the sub-consolidated requirements may generate limited added benefits relative to the administrative and reporting burden imposed on both institutions and supervisors.

207. In light of these findings, the EBA recommends to the Commission the introduction of a provision in the regulatory framework enabling competent authorities to grant exemptions from the application of Article 22(1) of the CRR requirements on a case-by-case basis, where such application would be disproportionate or of limited relevance to the effectiveness and efficiency of supervision (**Recommendation 10**).

Application of sub-consolidation requirements where only a participation is held

208. According to the wording of Article 22 of the CRR, sub-consolidation requirements are triggered if subsidiary institutions or intermediate (mixed) financial holding companies 'have an institution or a financial institution as a subsidiary in a third country, or hold a participation in such an undertaking'.

209. The EBA holds the view that the reference to participations here is only meant to include participations, that are, at a higher group level, fully or proportionally consolidated for prudential purposes. Otherwise, the introduction of a specific obligation to sub-consolidate would not be meaningful.

210. Accordingly, the EBA recommends to the Commission that it clarifies this aspect in the Level 1 text to ensure sub-consolidation requirements are not applied in cases where the participation would not be consolidated (**Recommendation 11**).

9. Other implementation issues

9.1 Subsidiary of subsidiary principle and interaction with Danish compromise

KEY TAKEAWAYS OF THIS SECTION

The supervisory review of certain M&A transactions has revealed interpretative challenges in the application of the CRR's consolidation framework, particularly in cases where financial institutions – such as AMCs – are acquired through insurance subsidiaries of banking groups. These cases have raised questions about whether such indirectly held entities should be included in the consolidated situation of the parent institution, especially when the parent applies the so-called 'Danish Compromise' under Article 49(1) of the CRR to its insurance holdings. Institutions had, in some instances, originally assumed that AMCs acquired by insurance subsidiaries fall outside the scope of prudential consolidation, thereby excluding them from the group's consolidated situation. This assumption may have implications as it may result in goodwill not being deducted from CET1 capital and in the application of a 250% risk weight[35] to the entire investment, including the AMC, under Article 49(1) of the CRR. Such treatment could lead to regulatory arbitrage, where group structures are designed to place financial institutions under insurance subsidiaries to benefit from more favourable capital treatment or avoid deductions.

The EBA's assessment confirms that the current CRR framework already provides the necessary tools to address these situations. The definition of 'subsidiary' under Article 4(1), point (16) of the CRR explicitly includes subsidiaries of subsidiaries, meaning that a financial institution held through an insurance undertaking qualifies as a subsidiary of the parent institution. As such, it must be fully consolidated, regardless of the nature of the intermediate entity. From a technical standpoint, the consolidation of an indirectly held financial institutions requires addressing some specific features, including adjusting the carrying amount of the parent's investment in the insurance undertaking to reflect the consolidation of the financial institution in the parent entity.

All in all, the EBA is of the opinion that the current framework is sufficiently robust to address the prudential implications of such type of transactions. The 'subsidiary of subsidiary' principle plays a central role in ensuring that all relevant risks are reflected in the consolidated situation of an institution, or a (mixed) financial holding company, regardless of the group's internal structure. For these reasons, no further regulatory changes are deemed necessary at this stage and a consistent application of the CRR provisions by institutions and competent authorities is expected going forward.

[35] Subject to the application of the provisions laid down in Article 495a of the CRR.

9.1.1 Background

211. The supervisory assessment of certain M&A transactions has revealed some implementation issues concerning the definition of 'subsidiary' under Article 4(1), point (16) of the CRR, particularly in relation to undertakings held indirectly through other insurance subsidiaries.

212. The cases reviewed by supervisors concerned, in particular, the acquisition of asset management companies (AMCs) by insurance subsidiaries of bank-led financial conglomerates, where the parent credit institution applied to its participation to the insurance undertaking the so-called 'Danish Compromise' under Article 49(1) of the CRR. In these instances, institutions initially assumed that the acquired AMCs would not be subject to prudential consolidation within the (banking) group under the CRR – as they were acquired by an undertaking (insurance) that is excluded from the prudential consolidation perimeter. As such, any goodwill arising from those acquisitions was considered non-deductible from the consolidated CET1 of the parent institution.

213. Although the prudential treatment applied to the transactions in question has already been duly enforced by the relevant competent authority, the EBA considered appropriate to conduct a comprehensive assessment of the applicable consolidation provisions and their interaction with the Danish Compromise in this context.

214. The primary objective of such an assessment is to determine whether the current framework adequately addresses the prudential risks and implications arising from these types of transactions and evaluate the existence of any potential loopholes within the CRR provisions and definitions which may compromise the objectives of the consolidation framework.

215. In particular, the key policy question is whether the current framework clearly establishes an obligation to consolidate subsidiaries of subsidiaries, even if the intermediate entity is an insurance undertaking – or another non-financial entity – excluded from consolidation, or whether the presence of such an intermediate entity impedes the consolidation of other (financial institution) subsidiaries controlled.

MORE INFO: What are the risks associated to institutions envisaged prudential treatment to AMCs acquired by insurance undertakings?

The non-consideration of AMCs – or other financial institutions – indirectly held via an insurance subsidiary undertaking from the consolidated situation of a parent institution that benefits from the application of Article 49(1) of the CRR would result in extending the benefits of the 'Danish compromise' also to those indirect (AMCs) holdings.

More specifically, in such circumstances, the investment in the AMCs would be implicitly subject to the same risk-weighting treatment foreseen for insurance holdings under Article 49(1) of the CRR. This is because the value of the holding that the institution has in the insurance undertaking, included in its consolidated situation, would reflect, at the same time, the investment in the AMCs.

This reading of the relevant provision in the CRR could pave the way for potential regulatory arbitrage. Specifically, the exemption from deducting participations in insurance subsidiary undertakings under Article 49(1) of the CRR may incentivise the creation of group structures in which financial institutions subsidiaries are placed under the insurance subsidiary. This restructuring could be aimed at circumventing stricter prudential requirements – particularly when these exceed the risk weight applied to insurance holdings – or avoid other capital deductions.

For example, one potential incentive which might arise in the case of the acquisition of AMCs (or other financial institutions) through the insurance subsidiaries of the group is the possibility of not deducting the goodwill emerging from these transactions. In fact, under the assumption that the AMCs are excluded from the consolidated situation of the parent institution – because they are acquired by an entity excluded from the scope of prudential consolidation (i.e. insurance subsidiary) – any goodwill arising from their acquisition would be recognised solely at the level of the insurance undertaking.

In such scenario, the parent institution would be required to deduct the goodwill associated to its significant investments in a financial sector entity (i.e. the insurance subsidiary undertaking) according to Articles 36(1)(i) and 43 of the CRR. Nonetheless, institutions could argue that this deduction does not include subsequent goodwill arising at the insurance subsidiary level from the acquisition of the AMC ('second level goodwill'). This reading might seem justified by specific clarifications provided by the EBA in a Q&A published in 2023[36] which seems – at first glance – to cater to such situations.

[36] See the EBA Q&A 2021_6211.

9.1.2 Observations and EBA assessment

216. The determination of whether an undertaking must be included in the consolidated situation of a parent institution is based on two distinct criteria:

    a. the nature of the relationship between the parent undertaking subject to consolidation requirements and the undertaking concerned. Article 18 of the CRR requires the consolidation of undertakings that are subsidiaries, participations, significant influence, or other qualifying links specified therein, provided that certain conditions are met;

    b. the type of undertaking concerned. In accordance with Article 18 of the CRR, only undertakings that qualify as institutions, financial institutions may be included within the scope of prudential consolidation[37].

217. For the purposes of applying these two criteria, the definitions set out in Article 4(1) of the CRR are relevant, both to the nature of the relationship (e.g. subsidiary, participation) and for assessing the qualification of the undertaking in a specific class (e.g. financial institution).

218. To ensure a consistent and comprehensive application of the prudential consolidation framework, institutions are required to assess the nature of the relationship for all undertakings linked to the consolidating entity, irrespective of their nature and inclusion in the scope of prudential consolidation. Similarly, the qualification of that undertaking in a specific regulatory class becomes subsequently relevant to determine whether the undertaking should be included in – or excluded from – the scope of consolidation. This sequencing is essential to ensure an appropriate determination of the scope of prudential consolidation.

219. In this context, the determination of whether an undertaking qualifies as 'subsidiary' should be based on the definition provided in Article 4(1), point (16) of the CRR, which provides the following: 'subsidiaries of subsidiaries shall also be considered to be subsidiaries of the undertaking that is their original parent undertaking'. This definition relies exclusively on the existence of a control relationship and is independent of the nature or regulatory classification of the subsidiary. Therefore, the 'subsidiary of subsidiary' notion should exist also in cases where the type of intermediate subsidiary does not trigger its inclusion in the scope of prudential consolidation, for example, because it is an insurance subsidiary undertaking.

[37] Subsidiaries or participations that are not an institution or financial institution may be consolidated, when decided by the competent authority, if there is a substantial risk of step in, provided that the conditions laid down in Article 18(8) of the CRR are complied with.

220. On this basis, undertakings that qualify as subsidiaries of an institution's insurance subsidiary should be treated as subsidiaries of the parent undertaking (i.e. indirect subsidiaries). Whether they are to be included in the consolidated situation of the parent undertaking, should be then assessed based on their classification as an institution, financial institution within the meaning of Article 4 of the CRR.

221. When applying these considerations to the case of an AMC (or another financial institution) acquired through an institution's insurance subsidiary, it becomes evident that the acquired AMC qualifies as a subsidiary of the parent institution, by virtue of being a subsidiary of a subsidiary and, as a financial institution, it is required to be fully consolidated.

222. The consolidation technique to be used in such case can be derived from accounting principles. The carrying amount of the participation in the insurance subsidiary held by the parent institution can be split, accounting-wise, in two components: (i) the carrying amount related to the 'pure' insurance subsidiary, and (ii) the carrying amount attributable to the financial institution (e.g. AMC). The carrying amount related to the 'pure' insurance group would be risk weighted in accordance with Article 49(1) of the CRR. On the other hand, carrying amount related to (ii) above, would be reflected in the consolidated situation of the parent undertaking, following a normal consolidation process. Such process may give rise to goodwill and other intangibles to be deducted pursuant to Article 36(1) of the CRR.

223. The clarifications set out in the EBA Q&A 2021_6211 are therefore not relevant in this context, as they concern the treatment of goodwill arising from investments in FSEs that are not subject to prudential consolidation (e.g. insurance undertakings) pursuant to Article 37(b) of the CRR. Accordingly, the Q&A does not impact the general deduction framework applicable to goodwill recognised directly by the consolidating parent undertaking, including where the goodwill originates from an indirect holding in a financial institution.

9.1.3 Conclusion and policy recommendations

224. Given the potential implications for the prudential consolidation framework arising from divergent interpretations of the relevant CRR provisions, institutions are expected to adopt a consistent approach when assessing whether indirectly held financial institutions qualify as subsidiaries and are therefore subject to full consolidation by the (original) parent institution. This assessment should be carried out in full alignment with Articles 11 and 18 of the CRR, and with reference to the definitions set out in Article 4 of the same Regulation.

225. Overall, the current consolidation framework is considered sufficiently robust to accommodate the prudential implications associated with the acquisition of indirect holdings in financial institutions, including those transactions that interact with the

application of Article 49(1) of the CRR. In particular, the ‘subsidiary of subsidiary’ principle embedded in the CRR definition of ‘subsidiary’ serves as a key safeguard within the prudential consolidation framework. It ensures that risks arising from financial activities conducted by undertakings within a banking group are appropriately reflected in the consolidated situation of the institution, irrespective of such undertakings being directly or indirectly held. This mechanism supports a fair representation of the group’s overall risk profile and underpins a sound and consistent determination of its capital position.

226. Moreover, the ‘subsidiary of subsidiary’ principle plays a critical role in mitigating regulatory arbitrage, by limiting incentives from groups to structure themselves in a way that places financial activities outside the scope of prudential consolidation.

227. Notwithstanding the implementation challenges observed in specific cases, no further regulatory intervention is considered necessary at this stage. The existing provisions on prudential consolidation and the relevant definitions under the CRR are deemed sufficiently clear to address the issues identified during supervisory review. For these reasons, no further regulatory changes are deemed necessary at this stage and a consistent application of the CRR provisions by institutions and competent authorities is expected going forward.

Method of prudential consolidation of an indirectly held institution or financial institution

228. A financial institution (or institution) held indirectly via an insurance undertaking should be fully consolidated from a prudential perspective if the subsidiary of subsidiary condition is met.

229. This means that the institution should consolidate the financial institution as if it was its direct (controlled) subsidiary (i.e. recognising in full assets and liabilities). Non-controlling interests attributable to third-party investors would follow prudential rules concerning minority interest recognition. In the same vein, the recognition of any goodwill stemming from the acquisition of the financial institution at stake would follow the usual accounting process, being determined by the difference between the consideration transferred and the fair value of the net assets acquired – and, as such, recognised in the consolidated accounting figures of the institution. For prudential purposes, its treatment should follow existing CRR rules and be deducted.

230. In practical terms, the investment in the subsidiary insurance undertaking should be accounted for via the equity method in accordance with Article 18(7) of the CRR. Therefore, the equity holding of the insurance subsidiary in the financial institution would need to be concurrently subtracted from the equity holding of the parent institution in the subsidiary insurance undertaking, reflecting the consolidation treatment applied.

MORE INFO: How to account for indirectly held institutions or financial institutions

An institution holds a 100% ownership stake in an insurance undertaking, which in turn acquires an 80% stake in an AMC. The carrying amount of the holding in the insurance undertaking is 10bn. The institution and the insurance company are part of a conglomerate subject to supplementary supervision and the institution applies the 'Danish Compromise' to its investment in the insurance undertaking.

The acquisition price for the 80% interest in the AMC is EUR 6 bn. The fair value of the AMC net identifiable assets is 4 bn. The institution recognises the goodwill from the transaction in accordance with the accounting principles as follows: (a) consideration transferred 6.0 bn + (b) amount of non-controlling interests in the AMC 0.8 bn (based on proportionate share of fair value of net assets acquired) – (c) fair value of net assets acquired 4.0 bn = 2.8 bn.

Full consolidation of the AMC results in incorporating all its assets and liabilities and accounting for the non-controlling interests (NCI) in the AMC (i.e. 20%). As a consequence, the CRR framework applies.

- The goodwill of 2.8 bn is deducted from CET1 capital;
- Non-deducted assets are risk weighted;
- The recognition of NCI from a prudential perspective (i.e. minority interests) is limited to the amount that is eligible from a prudential perspective according to Articles 81 to 88b of the CRR.

The institution's indirect holding in the AMC is equal to 6 bn. The carrying value of the holding in the insurance undertaking of 10 bn shall be reduced by 6 bn and be subject to the 250% risk weight.

All in all, this implies:

Subsidiary assessment	Institution: 100% in the insurance undertaking Insurance undertaking →: 80% in the AMC If the subsidiary of subsidiary principle is met, the AMC qualifies as subsidiary of the institution.
Acquisition price	EUR 6 bn for 80% in AMC
Fair value of the AMC net assets	EUR 4 bn
Carrying amount of the holding in the insurance undertaking	EUR 10 bn

Carrying amount of the holding in the insurance undertaking related to the pure insurance business	EUR 10 bn – EUR 6 bn = EUR 4 bn to be subject to 250% RW pursuant to Article 49(4) of the CRR
Consolidation	AMC fully consolidated CI in AMC = 80% NCI in AMC = 20%
Goodwill related to the acquisition of the AMC	EUR 2.8 bn Calculated in accordance with the accounting principles and shown in the consolidated financial statement Deducted from prudential standpoint
Minority Interest recognition	Calculated according to the CRR rules
Carrying amount of the indirect holding in the AMC	EUR 6 bn subtracted from the carrying amount of the holding in the insurance undertaking

MORE INFO: What did the EBA Q&A 2021_6211 clarify?

The EBA Q&A 2021_6211 addresses the treatment of goodwill included in the valuation of significant investments in insurance undertakings, for the purposes of CET1 capital deductions under Articles 36(1), point (b) and 37(b) of the CRR. The question was raised by a competent authority in response to divergent practices among institutions and potential differences in supervisory approaches across jurisdictions.

The Q&A comprised two distinct inquiries. The first concerned the calculation of goodwill included in the valuation of significant investments in insurance undertakings, relevant for the deduction regime under the CRR. Specifically, the question was whether the goodwill to be deducted should:

- be limited to the initial goodwill recognised at the time of acquisition by the credit institution (i.e. the difference between the purchase price and the investor's share of the net fair value of identifiable assets and liabilities – referred to as 'first-level goodwill'), or
- also include any additional goodwill subsequently recognised at the level of the insurance undertaking ('second-level goodwill').

The second inquiry concerned the interaction between the goodwill deduction regime and the application of the Danish compromise (Article 49 of the CRR). In particular, it sought to clarify whether the application of the Danish regime permits the risk-weighting, rather than the deduction, of the goodwill associated with significant investments in insurance undertakings.

In response to those questions, the EBA clarified that the goodwill included in the valuation of significant investments in insurance undertakings – typically accounted for using the equity method for prudential purposes – should be determined in accordance with the applicable accounting framework. Accordingly, the amount to be deducted should reflect the first-level goodwill only – i.e. the difference between the acquisition cost of the investment and the credit institution's share of the net fair value of the investee's identifiable assets and liabilities. Any second-level goodwill, subsequently recognised at the level of the insurance undertaking and disclosed in the consolidated financial statements of the parent institution, should be therefore disregarded and not included in the amount to be deducted from CET1 capital.

As regards the second question, the Q&A confirmed that the deduction of first-level goodwill also applies in cases where the Danish compromise is used. While Article 49(1) of the CRR provides, subject to competent authority approval, an alternative to full deduction of the investment, it does not waive the requirement to deduct goodwill as established under Article 37(b) of the CRR.

The rationale for the first clarification (i.e. the deduction of first-level goodwill only) was the consideration that insurance undertakings are explicitly excluded from the prudential scope of consolidation. Therefore, requiring the deduction of second-level goodwill was considered in practice reflecting the effects of a consolidation of the insurance undertaking, at least for the amount of goodwill to be deducted. This result would be equivalent to that applied in the case of invested institutions, which are subject to prudential consolidation, and would therefore be inconsistent with Article 18(7) of the CRR, which mandates that insurance undertakings qualifying as subsidiaries be accounted for using the equity method by default. Such a treatment would entail a sort of 'look-through' approach, limited to goodwill recognition, which is not foreseen under the CRR. Moreover, the EBA further considered that, even if not deducted by the parent credit institution, any second-level goodwill is subject to Solvency II requirements, under which such goodwill is typically valued at zero and, as a result, the lack of loss absorbency of that item is already recognised at insurance group level.

With regard to the second clarification, the EBA further noted that Article 15j of Commission Delegated Regulation (EU) No 241/2014 allows institutions not to separately identify goodwill when determining the applicable deduction amount for insignificant investments (Article 46 of the CRR). However, the EBA considered that this provision does not apply to significant investments, and therefore cannot override the treatment established in Article 37(b) of the CRR, which requires the deduction of goodwill from CET1 capital in such cases.

9.2 Scope of application of step-in risk under Article 18(8) of the CRR

9.2.1 Background

231. Step-in risk provisions are designed to capture situations where an institution may decide to provide support to an unconsolidated undertaking in the absence of a contractual or legal obligation to do so.

232. In this regard, the regulatory framework provides specific mechanics to address such situations, including the possibility for competent authorities to require the application of prudential consolidation for such undertakings under Article 18(8) of the CRR.

233. This provision grants competent authorities the power to require full or proportional consolidation of a subsidiary or an undertaking in which an institution holds a participation where that subsidiary or undertaking is not an institution, a financial institution or a (re)insurance undertaking, when there is there is a substantial risk that the institution decides to provide financial support to that undertaking in stressed conditions, in the absence of, or in excess of any contractual obligations to provide such support.

9.2.2 Observations and EBA assessment

234. Article 18(8) of the CRR currently applies only to cases involving subsidiaries or undertakings in which an institution holds a participation and therefore does not extend to undertakings with which the institution has other types of capital ties or significant influence in absence of capital ties.

235. Such a limitation has raised specific supervisory concerns regarding the effective scope of application of the provision, as in many situations – for instance in the case of special purpose vehicles or similar undertakings – the risk of step-in may not primarily stem from a control relationship or the holding of a participation, but may also arise from other capital ties, influence, sponsorship or implicit expectation of support.

9.2.3 Conclusions and policy recommendations

Recommendation to the Commission

236. In light of the above, the EBA recommends the Commission, in the context of future revision of the Level 1 text, to enlarge the scope of Article 18(8) of the CRR to also include relationships other than subsidiaries and participations (Recommendation 12).

237. Where such enhancement of the step-in risk provision in Article 18(8) of the CRR would be deemed appropriate, the revised wording may be articulated as follows: '*Competent authorities may require full or proportional consolidation of a subsidiary or an undertaking in which an institution holds a participation, other capital ties or on which the institution exercises significant influence where that subsidiary or undertaking is not an institution or a financial institution and where all of the following conditions are met: […]*'.

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