Financial Stability Committee

Macroprudential supervision in Poland

institutional and functional framework

Warsaw, May 2016

Contents

Introduction

Macroprudential supervision was established in Poland pursuant to the Act of 5 August 2015 *on macroprudential supervision of the financial system and crisis management* (hereinafter the Act), which entered into force on 1 November 2015. Under this Act, the **Financial Stability Committee** was designated **as the authority responsible for macroprudential supervision in Poland**.

In response to the Recommendation of the European Systemic Risk Board of 4 April 2013 *on intermediate objectives and instruments of macro-prudential policy* (ESRB/2013/1), the Financial Stability Committee adopted this document, which describes the institutional, formal and legal conditions of conducting macroprudential supervision in Poland. This document will be subject to review after a period in which experience and conclusions on the functioning of macroprudential supervision in Poland have been gathered. This will allow to develop the strategy of macroprudential supervision in Poland.

The aim of the document is to:

- present the institutional settings of macroprudential supervision, i.e. of the Financial Stability Committee as the macroprudential supervision authority, including the objective of its establishment,
- specify the ultimate objective of macroprudential supervision by defining the intermediate objectives,
- link the intermediate objectives with macroprudential instruments,
- present the basic principles of applying macroprudential instruments under the provisions of the law,
- define the method of communication of the Financial Stability Committee as the authority of macroprudential supervision.

1. Systemic risk

Pursuant to Article 1 para. 1 of the Act, **macroprudential supervision of the financial system** "*covers the identification, assessment and monitoring of systemic risk arising in the financial system or its environment and actions aimed at eliminating or reducing this risk with the use of macroprudential instruments*". In other words, macroprudential supervision is aimed at counteracting and mitigating systemic risk, whose materialisation could destabilise the financial system and cause the negative spill-overs.

The concept of systemic risk is defined in Article 4 point 15 of the Act as "*the risk of disruption in the functioning of the financial system, which in the case of its materialisation interferes with the operation of the financial system and the national economy as a whole* (…)". The source of systemic risk may include, among others, excessive credit growth, excessive leverage of financial institutions, households or enterprises, or the highly concentrated linkages between financial institutions. Systemic risk may accumulate in various parts of the financial system (structural dimension of systemic risk), and gradually build up over time (time dimension of systemic risk). The consequence of the materialisation of systemic risk may be financial crises that are very costly for the public.

Article 1 para. 2 the Act determines the objective of macroprudential supervision as "*in particular, to strengthen the resilience of the financial system in the event of the materialisation of systemic risk, and in consequence, to support long-term and sustainable economic growth of the country*". Strengthening the resilience of the financial system means directly supporting its stability. Accordingly, when interpreting the content of the Act, one may assume that the ultimate objective of macroprudential supervision is to ensure the stability of the financial system. Financial stability, which is treated as a public good, is also the condition for sustainable economic growth in the long term. In order to define the stability of the financial system, the Financial Stability Committee applies the definition formulated by Narodowy Bank Polski, in accordance with which it is "*a situation when the system performs its functions in a continuous and efficient way, even when unexpected and adverse disturbances occur on a significant scale*".[1]

[1] Financial Stability Report, February 2016, Narodowy Bank Polski, Warsaw, 2016, p. 3.

2. Macroprudential supervision authority in Poland

The Act of 5 August 2015 *on macroprudential supervision of the financial system and crisis management*, which entered into force on 1 November 2015, designates the **Financial Stability Committee as the authority responsible for macroprudential supervision in Poland[2] (FSC-M).**

2.1. Composition

The Financial Stability Committee on macroprudential supervision (FSC-M) is a collegial body comprising of the following members:

- President of Narodowy Bank Polski – Chairperson of FSC-M,
- Minister of Finance,
- Chairman of the Polish Financial Supervision Authority,
- President of the Bank Guarantee Fund.

The collegial formula of the macroprudential authority in Poland stems from the fact that the tasks and powers to maintain financial system stability in the country are assigned by law to four institutions of the financial safety net, i.e. the Ministry of Finance, Narodowy Bank Polski (NBP), the Polish Financial Supervision Authority (PFSA) and the Bank Guarantee Fund (BGF). However, none of these institutions has a mandate or sufficient tools to effectively and individually counteract systemic risk. At the same time, each of the institutions represented in the Committee can make an important contribution to the analysis of systemic risk and can take measures to limit the build-up of risk as well as the effects of its materialisation. Therefore, the collegiality of the Financial Stability Committee allows for synergies in the process of analysis, assessment and prevention of systemic risk.

The table below indicates the activities of the individual institutions represented in FSC-M which are specific from the point of view of financial system stability.

[2] Pursuant to the Act of 5 August 2015 *on macroprudential supervision of the financial system and crisis management*, the Financial Stability Committee has a dual mandate for action. Apart from the macroprudential supervision tasks described in this document, the Committee also performs tasks related to crisis management. The Minister of Finance chairs the work of the Committee on crisis management and support in this area is provided to the Committee by the Ministry of Finance.

Table 1. Specific activities of institutions comprising the FSC-M

Institution	Characteristic responsibilities
Ministry of Finance	• legislative initiative – issuing regulations and submitting draft laws • powers regarding tax policy • direct participation in the EU legislative process • analysis of the macroeconomic situation • management of government administration in the field of public finance and financial institutions
Polish Financial Supervision Authority	• supervision of individual entities of the market, including Systemically Important Institutions • collection of statistical information, including information about non-bank financial institutions • qualitative information on the situation of entities under supervision • analysis of the situation of individual financial entities (microprudential analysis) • making proposals for amendments to financial regulations • membership of supervisory colleges for cross-border banking and insurance groups • powers to issue recommendations, among others, to credit institutions and insurance companies • membership of the boards of supervisors of: the European Banking Authority, the European Securities and Markets Authority, the European Insurance and Occupational Pensions Authority and the participation in the European Systemic Risk Board (ESRB)
Bank Guarantee Fund	• protecting deposits in the banking sector and credit union sector (SKOK) • planning and carrying out resolution of banks, credit unions and investment firms (brokerage houses) • membership of the Resolution Committee functioning within the European Banking Authority • membership of the resolution colleges for cross-border banking groups • analysis of risk in the banking sector for the needs of guaranteeing deposits and forced restructuring • financial support for restructuring processes of banks and credit unions
Narodowy Bank Polski	• analysis of macroeconomic situation in Poland and its international environment, including international financial markets • analysis of the stability of the domestic financial system (macroprudential analysis) and its development • collection of statistical information, including information on banks, the economy, the balance of payments, foreign liabilities, and unregulated financial institutions • analysis of the interaction between the financial system and the real economy • macroprudential research • liquidity management in the interbank market (including emergency liquidity assistance for banks) • monetary policy responsibilities • membership of the European Systemic Risk Board and the European System of Central Banks (ESCB)

The above table is for illustration purposes only and does not specify the responsibilities of individual institutions

2.2. Tasks

The Act specifies the catalogue of macroprudential supervision tasks of the Committee. Pursuant to Article 5 of the Act, FSC-M:

1) applies macroprudential instruments, including issuing statements and recommendations;
2) identifies financial institutions creating a significant risk for the financial system;
3) cooperates with the European Systemic Risk Board, other European Union authorities, macroprudential authorities of the Member States or third countries, as well as with international institutions;
4) ensures an adequate flow of information between the members of the Committee enabling it to carry out its tasks.

From the above, it follows that the tasks of the FSC-M can be divided into three groups. The first group of tasks of the Financial Stability Committee serves to identify, assess and monitor the systemic risk arising in the financial system or in its environment.

The second group of tasks of the FSC-M consists in initiating measures aimed at reducing the identified threats to financial stability. To this end, the Committee may issue recommendations addressed to specific institutions or issue a statement.

The third group of tasks consists in ensuring appropriate cooperation in the area of macroprudential supervision at a domestic, international and particularly European level.

2.3. The role of NBP in macroprudential supervision

In accordance with the Recommendation of the European Systemic Risk Board of 22 December 2011 *on the macro-prudential mandate of national authorities* (ESRB/2011/3), the central bank should play the leading role in macroprudential supervision. An important reason for entrusting the central bank with such a role is its experience in analysis of the financial system and its relations with the real economy, which is reflected in regularly published analyses and reports on financial system stability. The central bank is interested in the effectiveness of measures aimed at ensuring financial system stability, since this is a condition for the attainment of its primary objective, which is price stability. Under conditions of a stable financial system, the transmission channels of monetary policy function properly. Therefore, a stable financial system creates the favourable conditions necessary to achieve the primary objective of the central bank, which is low and stable inflation.

The Act of 5 August 2015 *on macroprudential supervision of the financial system and crisis management* imposed on Narodowy Bank Polski specific tasks supporting the work of the Financial Stability

Committee in the area of macroprudential supervision. In particular, the Act assigns the role of chairperson of the FSC-M to the Governor of Narodowy Bank Polski, at the same time giving him the casting vote in the case of an equal number of votes when voting on resolutions of the Committee.

The above-mentioned Act also introduced amendments to the Act of 29 August 1997 *on Narodowy Bank Polsk*, regulating the tasks performed by Narodowy Bank Polski on behalf of FSC-M. **The tasks performed by Narodowy Bank Polski cover the following two areas:**

- **analytical and research support,**
- **organisational and administrative support.**

Within the first area, Narodowy Bank Polski prepares analytical materials, studies and opinions on systemic risk assessment, including periodic NBP Financial Stability Reports and Reports on Macroeconomic Stability of the Polish Economy. Moreover, NBP supplies the Committee with information and data necessary for the assessment of systemic risk. .

Within the second area, Narodowy Bank Polski organises meetings of the FSC-M, runs its secretariat and provides legal services, preparing draft resolutions of the Committee. Narodowy Bank Polski also ensures adequate communication about the macroprudential measures undertaken. To this end, NBP has launched on its website a sub-website of the Financial Stability Committee as the body of macroprudential supervision (http://www.nbp.pl/nadzormakroostroznosciowy/index.aspx).

3. Ultimate and intermediate objectives of macroprudential supervision

Pursuant to Article 1 para. 2 of the Act "***the objective of macroprudential supervision** is, in particular, to strengthen the resilience of the financial system in the event of the materialisation of systemic risk, and in consequence, to support long-term and sustainable economic growth in Poland*". Due to the multidimensional nature of systemic risk, effective macroprudential supervision requires the definition of intermediate objectives whose realisation – by applying appropriate macroprudential instruments – helps to achieve the ultimate objective.

3.1. Intermediate objectives of macroprudential supervision

Respecting the Recommendation of the European Systemic Risk Board of 4 April 2013 *on intermediate objectives and instruments of macro-prudential policy* (ESRB/2013/1), and also having regard to the specific nature of the Polish financial system, the following **intermediate objectives of macroprudential supervision** have been specified**:**

- mitigation of risk arising from excessive growth or size of debt or leverage,
- mitigation of risk arising from excessive maturity mismatch of assets and liabilities of financial institutions or of the risk of illiquidity of financial markets,
- mitigation of risk arising from excessive concentration of exposures or their similarity, and the interconnectedness between financial system entities,
- mitigation of risk arising from misaligned incentives influencing the behaviour of financial institutions or their clients,
- ensuring the adequate resilience of the financial infrastructure.

Table 2. Intermediate objectives of macroprudential supervision in Poland

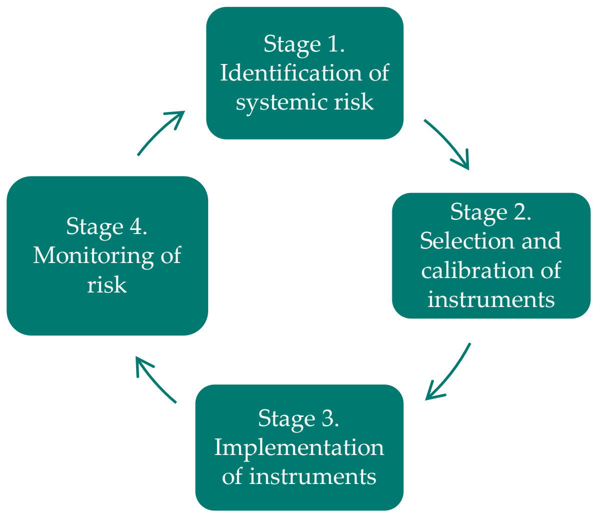
	Intermediate objectives	Description
1	Mitigation of risk arising from excessive growth or size of debt or leverage	**Risk arising from the pro-cyclical behaviour of financial institutions** is reflected in the phenomenon of the credit/financial/debt cycle; this risk is manifested, among others, in the form of excessive leverage, excessive level and growth of debt (including lending), and excessive credit risk, which can be accompanied by price bubbles in asset markets. This risk can also be manifested in the criteria and standards of lending. The above-mentioned issues should be analysed, among others, in the context of the capacity to absorb losses in various phases of the cycle and the profitability of financial institutions (effectiveness, capacity to generate income).
2	Mitigation of risk arising from excessive maturity mismatch of assets and liabilities or of the risk of illiquidity of financial markets	**Risk of unstable funding models** arising from the structure and sources of funding and excessive funding costs. **Liquidity risk** as a result of excessive maturity **mismatch of assets and liabilities (as well as off-balance sheet operations) or the level of their liquidity.** **Risk of illiquidity of the financial markets** as a result of, among others, the materialisation of two of the above-mentioned risk categories and structural changes in financial markets. The above-mentioned issues should be analysed, among others, in the context of the adequacy of the liquidity buffers of financial institutions.

3	Mitigation of risk arising from excessive concentration of exposures to entities or risk factors, and the interconnectedness between financial system entities	**Risk arising from large exposures** to individual financial and non-financial entities (concentration of exposures to entities) or homogenous exposure groups (concentration of exposures to risk factors). **Risk of contagion** as a result of the existence of a network of mutual exposure or interdependencies of asset prices or similar balance sheet structure of financial institutions (resulting in increased vulnerability of the whole system to disturbances). The above-mentioned issues should be analysed, among others, in the context of the capacity of financial institutions to absorb losses.
4	Mitigation of risk arising from misaligned incentives influencing the behaviour of financial institutions or their clients	**Excessive risk-taking by managers** (management boards, owners) **of financial institutions**, in particular, risks related to the excessive size of financial institutions or the complexity of the business models of financial institutions as a result of their special role and lack of possible substitution of their services (aspect of incentives to increase the size and role in the financial system, aspect of the structure of the market). **Risk of misaligned incentives leading to increased moral hazard among depositors or investors** as a result, among others, of the legal regulations concerning the protection of depositors and certain groups of investors, the lack/inadequate resolution system for financial institutions or financial infrastructure entities, or the lack of supervision over certain sectors. The above-mentioned issues should be analysed, among others, in the context of the adequacy of capital and liquidity buffers for Systemically Important Financial Institutions and their capacity to separate critical functions, as well as in the context of regulations and institutional solutions.
5	Ensuring the adequate resilience of the financial infrastructure	**Risk of instability of entities of the financial market infrastructure:** risk of cessation of key services for many financial institutions (among others, the functioning of payment and settlement systems and clearing houses), inappropriate institutional solutions (e.g. the principle of risk management in clearing houses), inadequate resilience to the materialisation of risk.

3.2. Cycle of macroprudential supervision

The implementation of macroprudential supervision can be described as a series of actions undertaken by the Financial Stability Committee in cooperation with institutions of the financial safety net that are represented in it (see Diagram 1).

Diagram 1. Cycle of macroprudential supervision measures



In simple terms, a macroprudential supervision cycle can be described as a sequence of the following stages:

Stage 1. Covers the **identification of systemic risk in the financial system** on the basis of the analyses prepared by Narodowy Bank Polski and other institutions represented in FSC-M. The subject of analysis is the whole financial system and its relations with the real economy as well as the international environment. Due to the fact that in Poland banks play the dominant role in the financial system, the main focus of the analysis is on the banking sector. The role of the FSC-M consists in assessing whether the identified risk is of a systemic character, and if it is, whether it is necessary to take particular measures. During the identification of the systemic risk's sources, a wide range of indicators illustrating the macroeconomic situation, the level of credit risk, liquidity, capital position of financial institutions etc., are concerned. The concentration of risk in the financial system is analysed as well as the linkages within the financial system. In addition, gaps are identified in the data necessary to conduct effective macroprudential supervision (so-called information gaps). In case the systemic risk is identified and there is a need to mitigate this risk, the cycle proceeds to Stage 2.

Stage 2. Covers the selection of a specific macroprudential instrument which will mitigate the identified systemic risk adequately, having regard to the provisions of Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 *on prudential requirements for credit institutions and investment firms* (hereinafter CRR) and of the Act. If the Financial Stability Committee considers that there is the need for the implementation of a macroprudential instrument, it shall issue a recommendation, which can include the proposed calibration of this instrument. Recommendations might be addressed to member institutions of the FSC. The addressee is then obliged to comply with the recommendation or provide an explanation for non-compliance.

Stage 3. Covers the **application of measures mitigating or eliminating systemic risk through the implementation of the recommendations or measures resulting from the FSC-M's statement.** The implementation of a macroprudential instrument can take various forms depending on the entity (the addressee of the recommendation or statement), which implements it and on the instrument itself or the nature of the recommended measure. If the addressee of the recommendation (PFSA, MF, BGF, NBP) or statement decides to take the measures recommended by the FSC-M, they implement them according to the competences outlined in laws, defining the tasks and powers of these institutions**.** There are three ways to implement the indications of the FSC-M:

- the issuing of a regulation by the Minister of Finance on the basis of the existing laws,
- the issuing of a decision or recommendation by the PFSA, or
- the initiation of the legislative process aimed at preparing a draft act or amending of an existing law in order to implement a new instrument or regulate certain activities in the financial system.

Stage 4. Covers the **monitoring of risk, including the effectiveness of the measures undertaken in Stage 3**. On the basis of the analysis, the FSC-M will be able to formulate conclusions on the effectiveness of a given macroprudential instrument and the mechanisms of its impact. The conclusions can form the basis for the Committee to recommend the maintenance, withdrawal or modification of the parameters of the given macroprudential instrument.

4. Macroprudential instruments

4.1. Catalogue of macroprudential instruments

The objectives of macroprudential supervision are achieved by implementing measures counteracting the emergence of systemic risk and by increasing the resilience of the financial system to its materialisation. The mitigation of systemic risk is achieved by the application of appropriate macroprudential instruments.
These instruments can be divided into two groups:

- **harmonised instruments**, i.e. regulated at the European level in the Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 *on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms* (hereinafter CRD IV) and CRR;
- **non-harmonised instruments,** i.e. other than those indicated by the CRDIV and CRR, which can be applied by the national authorities in accordance with national law.

The first group includes:

- capital buffers:
    - countercyclical capital buffer,
    - systemic risk buffer,
    - Global Systemically Important Institutions buffer,
    - Other Systemically Important Institutions buffer and
- measures provided for in Article 458 of the CRR.[3]

Harmonised instruments can be applied only to credit institutions or investment firms[4], therefore their impact does not cover the whole financial system.

The second group of non-harmonised instruments includes all the remaining instruments which are available in the national legal system, including, for example[5]:

- limits on debt-service-to-income (DSTI) or the debt-to-income (DTI) ratio,
- limits on the loan-to-value (LTV) ratio,
- guidelines on the method of calculation of creditworthiness,
- domestic liquidity standards (M1-M4)[6].

Macroprudential supervision is a new, ever-evolving area of regulatory policy, therefore it is possible to introduce additional instruments in the future, designed especially for macroprudential purposes.

4.2. Powers of FSC-M

The Financial Stability Committee, as the macroprudential supervision authority, has the right to **indirectly influence the financial sector, i.e. it cannot issue acts regulating the activity of the financial market in Poland directly**. This is due to legal circumstances, in particular, the provisions of the Constitution of the Republic of Poland, which define the catalogue of institutions authorised to issue normative acts, among which the Committee is not mentioned. Therefore, **in accordance**

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[3] The design and mechanism of implementation is described in detail later in the document.

[4] The Polish law-maker also excluded from this group investment firms not in possession of a licence to conduct brokerage activities in a selected scope, Bank Gospodarstwa Krajowego and credit unions.

[5] These instruments are presented for illustrative purposes only and do not constitute a closed list of measures that can be used as part of macroprudential measures in Poland.

[6] Until the full entry into force of the standards of LCR and NSFR.

with Article 5 para. 1 of the Act, the Committee may present statements and issue recommendations.

Statements are presented when a high level of systemic risk is identified and the FSC-M finds that it is necessary to inform about the source of this risk and the possible consequences for the financial system. Therefore, the range of addressees of the statement is wide and includes not only the institutions that make up the FSC-M, but also entities of the financial system. The presentation of a statement may serve only as a communication instrument, but it should also encourage the competent authorities or economic agents to take corrective action to limit the build-up of systemic risk.

Recommendations are issued when the FSC-M wants to indicate the necessity to take measures aimed at mitigating the identified systemic risk. Addressees of the recommendations can be only institutions that make up the FSC-M, that is institutions that have the possibility to take supervisory and regulatory measures in order to stabilise the domestic financial system. The list of measures that the FSC-M can recommend is not limited. The Act explicitly specifies that if the Committee deems it advisable to use such instruments as countercyclical capital buffer, systemic risk buffer or national measures provided for in Article 458 of the CRR, then it issues an appropriate recommendation to the Ministry of Finance. However, in the case of the necessity to impose a buffer for Other Systemically Important Institutions on a specific bank or group of banks, the FSC-M addresses to the Polish Financial Supervision Authority a recommendation regarding the systemic importance of such institutions. Recommendations are not legally binding; however, the Act introduced the principle of ***"comply or explain"***, in accordance with which the addressees of the recommendations are obliged to comply or explain the reasons for non-compliance.

4.3. The relation between intermediate objectives of macroprudential supervision and macroprudential instruments

In accordance with the Recommendation of the European Systemic Risk Board of 4 April 2013 *on intermediate objectives and instruments of macro-prudential policy* (ESRB/2013/1), to each intermediate objective of macroprudential supervision at least one macroprudential instrument that helps to achieve the objective, should be assigned. Due to the early stage of development of macroprudential supervision, both in Poland and abroad, limited experience and the diversity of sources of systemic risk, macroprudential instruments and the principles of their use are being developed together with particular needs and as experience is gained.

The defined intermediate objectives are matched with macroprudential instruments which could potentially be used in Poland (see Table 3). It should be stressed that the Act regulates only the use of harmonised instruments, i.e. capital buffers, measures provided for in Article 458 of the CRR and the presentation of statements or issuance of recommendations by the FSC-M. However, the

Committee may consider it necessary to implement a macroprudential instrument that is not mentioned explicitly in the Act. In this case it may address a recommendation with an appropriate instruction to one or more institutions represented in the FSC-M. In this case, the list of non-harmonised macroprudential instruments is open.

Table 3. Intermediate objectives and macroprudential instruments

Intermediate objectives	Selected macroprudential instruments
Mitigation of risk arising from excessive growth or size of debt or leverage	• counter-cyclical buffer • sectoral capital requirements • conservation buffer • own funds requirements • acceptable methods of calculation of creditworthiness • limits on debt-service-to-income ratio (DSTI) • limits on debt-to-income ratio (DTI) • limits on the loan-to-value ratio (LTV) • systemic risk buffer • leverage ratio • risk weights
Mitigation of risk arising from excessive maturity mismatch of assets and liabilities of financial institutions or of the risk of illiquidity of financial markets	• short-term liquidity requirements (LCR, M1, M2) • long-term liquidity requirements (NSFR, M3, M4)
Mitigation of risk arising from excessive concentration of exposures or their similarity, and the interconnectedness between financial system entities	• large exposure restrictions • systemic risk buffer • requirement for settlement of financial transactions through a central counterparty (CCP)
Mitigation of risk arising from misaligned incentives influencing the behaviour of financial institutions or their clients	• Global Systemically Important Institutions buffer • Other Systemically Important Institutions buffer • systemic risk buffer • leverage ratio • additional requirements on the disclosure of information
Ensuring the adequate resilience of the financial infrastructure	• systemic risk buffer • additional disclosure requirements • risk management principles in CCP

It should be noted that the use of a single instrument can serve to reach more than one intermediate objective. It is also possible to combine several macroprudential instruments to achieve one intermediate objective if required to effectively prevent the build-up of systemic risk. The decision on the activation of a macroprudential instrument is taken bearing in mind the effectiveness of the instrument, i.e. its effectiveness in preventing or reducing the build-up of the particular risk as well as the costs resulting from its use.

5. The mechanism of implementation of macroprudential instruments by FSC-M

The Financial Stability Committee has been endowed with powers by means of which it can influence the financial sector in an indirect way, i.e. it can issue recommendations addressed to member institutions of the FSC-M and present the statements of a general nature. Therefore, there are two stages in the implementation of macroprudential instruments.

- **In Stage 1,** after identifying the threat to financial stability and establishing the need to counteract it, the Financial Stability Committee issues a recommendation addressed to the relevant institution of the financial safety net (Ministry of Finance, PFSA, BGF or NBP).
- **In Stage 2,** the addressee comply with the recommendation and implements the measures recommended by the FSC-M or explains the reasons for non-compliance with the recommendation.

With regard to the harmonised instruments, the Act defines the detailed division of competences with regard to their application. In accordance with this division, the Minister of Finance decides by way of a regulation on the following:

- the countercyclical buffer rate and recognizes it for a given Member State or third country (reciprocity),
- the systemic risk buffer rate,
- national measures referred to in Article 458 of the CRR.

The PFSA by way of administrative decision defines the following:

- on a consolidated basis, the Global Systemically Important Institutions, assigns them to the relevant category and determines the level of Global Systemically Important Institution buffer,

- on an individual, sub-consolidated or consolidated basis, other than Global Systemically Important Institutions, and imposes on them the Other Systemically Important Institution buffer.

5.1. Countercyclical buffer

The introduction of the countercyclical buffer is motivated by the need to respond to cyclical systemic risk. During the upswing phase of the financial cycle, when the supply of credit grows excessively, imposing a countercyclical capital buffer or raising its level should limit excessive lending, the further growth of which could result in the build-up of imbalances in the financial system, thereby increasing the probability of a financial crisis. At the same time, the higher capital base built up due to the greater requirements should strengthen the resilience of the banking sector to the negative effects of the future downturn phase of the financial cycle. After entering this downturn phase, the countercyclical buffer requirement is reduced or completely removed, thus preventing excessive deleveraging[7].

The obligation to apply a countercyclical capital buffer has been introduced in the EU since 1 January 2016. This means that even if the buffer is not imposed, the publication of information about the zero buffer rate in the Member State concerned is required. Basically, the countercyclical buffer rate is set in a range between 0 and 2.5% of the total risk exposure. Setting the buffer rate within this range entails the recognition of the countercyclical buffer rate by other EU or European Economic Area (EEA) countries based on the principle of reciprocity. If the countercyclical buffer rate exceeds 2.5% of the total risk exposure, the application of the principle of reciprocity is voluntary.

The Financial Stability Committee is obliged to calculate on a quarterly basis the value of the buffer guide and submit to the Minister of Finance recommendations regarding this buffer. Pursuant to Article 24 para. 4 of the Act, in setting the countercyclical buffer rate applied to credit exposure on the territory of the Republic of Poland by way of a regulation, the Minister of Finance takes into account the following:

- the recommendation of the FSC-M on the countercyclical buffer rate,
- the countercyclical buffer guide,
- the recommendation of the European Systemic Risk Board on the setting of the countercyclical buffer rate,
- other variables relevant from the point of view of responding to cyclical systemic risk,
- the results of the quarterly assessment and the need to respond appropriately to cyclical systemic risk.

[7] See: The ESRB Handbook on Operationalising Macro-prudential Policy in the Banking Sector, p. 26.

The Minister of Finance also determines the date from which the institutions apply the countercyclical buffer rate. The institutions have 12 months to prepare to meet the countercyclical buffer requirement. In exceptional circumstances, the Minister of Finance may specify a shorter period.

Pursuant to Article 25 of the Act, every quarter the Committee publishes the following information about the countercyclical buffer rate:

- the level of the applicable countercyclical buffer rate,
- the value of the countercyclical buffer guide,
- the credit to GDP ratio,
- the date as of which the institutions shall apply the above rate – in the case of an increase in the countercyclical buffer rate,
- the expected duration of the reduced rate – in the case of a decrease in the countercyclical buffer.

5.2. Systemic risk buffer

The systemic risk buffer is imposed in order to prevent and mitigate the long-term non-cyclical systemic risk which is not covered by the CRR. The introduction of this buffer aims to strengthen the resilience of financial institutions and their capacity to absorb losses in the event of shocks of a systemic or idiosyncratic nature. The systemic risk buffer is an instrument that may be flexibly modified in order to reduce the level of identified systemic risk. In particular, the buffer can be imposed to all or selected financial institutions or their exposure.[8]

The application of the systemic risk buffer is not compulsory in the EU or the EEA. Member States may introduce to their legal system this instrument (however, it is not obligatory). In Poland, the systemic risk buffer has been included in the catalogue of macroprudential instruments by the Act. The buffer rate may be set at the level of at least 1% of the total risk exposure, while the regulations do not define the upper limit of the rate. With regard to the systemic risk buffer, the application of the principle of reciprocity is voluntary.

The Financial Stability Committee may issue a recommendation addressed to the Minister of Finance recommending the introduction of a systemic risk buffer. The recommendation of the FSC-M shall contain a proposal regarding the following:

- the level of the buffer rate,
- the type of exposure which it should apply to,
- the category of institution to which it should apply.

[8] Ibid., p. 80.

Next, the Minister of Finance, by way of a regulation, sets the level of the systemic rate buffer and the range of institutions or type of exposure which this requirement applies to, as well as the duration of the buffer.

When determining the systemic risk buffer, it is necessary to follow the EU notification procedures and relevant decisions taken at the EU level.

- If the systemic risk buffer rate does not exceed 3%, the decision on applying this measure is taken by the Minister of Finance, and the Committee notifies about the intention to impose a systemic risk buffer the following authorities: the European Commission (EC), the European Systemic Risk Board, the European Banking Authority and the competent authorities responsible for macroprudential supervision in the interested Member States.
- If the systemic risk buffer rate exceeds 3% but is lower than 5%, the Minister of Finance, through the Committee, notifies the European Commission, the European Systemic Risk Board, the European Banking Authority and the competent authorities responsible for macroprudential supervision in the interested Member States about the intention to impose a systemic risk buffer, and then waits for the opinion of the EC. The Minister of Finance is not obliged to follow the opinion of the EC, but if it is negative, he should explain the reasons for any non-compliance.
- If the systemic risk buffer rate exceeds 5%, the Minister of Finance, through the Committee, notifies the European Commission, the European Systemic Risk Board, the European Banking Authority and the competent authorities responsible for macroprudential supervision in the interested Member States about the intention to impose a systemic risk buffer, and then waits for the opinion of the EC, which is binding. This means that if the decision of the EC is negative, the systemic risk buffer cannot be introduced from the pre-assumed rate.

5.3. Systemically Important Institution buffers

Within buffers of Systemically Important Institutions, the following are distinguished:

- Global Systemically Important Institution buffer,
- Other Systemically Important Institution buffer.

The mechanism of the functioning of both buffers is the same. Disturbances in the functioning of the Systemically Important Institution may generate risk to the entire financial system.[9] Therefore, the imposition of an additional capital requirement aims to strengthen their resilience, which should reduce the level of the risk indicated above.

[9] Ibid., p. 79.

The identification of Global Systemically Important Institutions proceeds on the basis of 5 criteria, i.e. 1) size, 2) interconnectedness with the financial system, 3) substitutability of services or infrastructure, 4) complexity and 5) cross-border activity. The level of the buffer rate for such institutions is set within the range from 1% to 3.5% of the total risk exposure and depends on the assessment of the global systemic importance of the institution. Nevertheless, due to the fact that no Global Systemically Important Institutions have their head office in Poland, this buffer will have no practical use.

The identification of Other Systemically Important Institutions proceeds on the basis of 4 criteria, i.e. 1) size, 2) importance for the economy of the Republic of Poland or the EU, 3) cross-border activity and 4) interconnectedness with the financial system. This buffer rate may amount to no more than 2% of the total risk exposure, and its individually determined amount depends on the systemic importance of the institution for the country's financial system. When assessing the systemic importance of Other Systemically Important Institutions, the Polish Financial Supervision Authority takes into account, among others, the recommendations of the FSC-M in this regard.

Each time, the Polish Financial Supervision Authority initiates separate administrative proceedings in order to issue a decision on the following:

- identification of the Global Systemically Important Institution and imposition on it of a Global Systemically Important Institution buffer,
- identification of the Other Systemically Important Institution and imposition on it of a Other Systemically Important Institution buffer.

During each of these administrative proceedings, the PFSA asks the FSC-M to issue an opinion on the case. The decisions of the PFSA regarding the identification and imposition of buffers for Systemically Important Institutions are immediately enforceable.

Once a year the Polish Financial Supervision Authority conducts a review of Global Systemically Important Institutions and the level of the buffer for Global Systemically Important Institutions imposed on them, and also conducts a review of the adequacy of the buffer rate for Other Systemically Important Institutions.

5.4. National measures provided for in Article 458 of the CRR

Pursuant to Article 458 of the CRR, in the case of the occurrence of systemic risk which may have serious negative consequences for the financial system and the real economy, the Member State may implement an instrument defined in this Article.

In such a situation, the Financial Stability Committee may issue a recommendation addressed to the Minister of Finance in which it indicates the need to apply national measures provided for in Article 458 of the CRR.

Taking into account the EU notification procedures defined in Article 458 of the CRR, the Minister of Finance may issue a regulation introducing a national measure in the following scope:

- level of own funds,
- level of the conservation buffer[10],
- large exposure requirements,
- liquidity requirements,
- risk weights on exposures to the residential and commercial real estate sector,
- financial sector exposures,
- requirements on public disclosures,

which is more rigorous when compared with the standards of the CRR.

Pursuant to Article 458 of the CRR and Article 63 of the Act, in the case of identification of systemic risk that can have serious negative consequences for the financial system or national economy, the Minister of Finance, through the Committee, shall notify the European Parliament, the Council of the European Union, the European Commission, the European Systemic Risk Board and the European Banking Authority of this fact and submit the following information:

- the changes in the intensity of systemic risk,
- the reasons why these changes could pose a threat to the stability of the national financial system,
- the reasons why other macroprudential instruments cannot adequately address the identified risk to the system,
- a proposal of the action that it intends to take,
- an explanation why the proposed measures are considered appropriate, effective and proportionate to resolve the situation,
- an assessment of the likely impact of the proposed measures on the EU internal market.

In the absence of objection to the planned action from the European Commission, the Minister of Finance may implement the planned measures. However, if the EC has negative opinion on the proposed action, it shall submit to the Council (of the EU) a implementing act to reject the proposed national measures. The approval of the Commission's proposal by the Council shall block the implementation of the instruments provided for in Article 458 of the CRR. In turn, the absence of a decision of the Council within one month of the submission of the Commission's proposal

[10] In the Polish legal system the conservation buffer rate is set by virtue of the law at 2.5%.

shall give the Minister of Finance the possibility to implement the proposed measures for a period of two years or until the systemic risk ceases to exist, if it occurs earlier.

6. Communication

Communication with the public and financial market participants is a very important element of the policy of each safety net institution. Also, the Financial Stability Committee considers that the information policy has a significant impact on the effectiveness of macroprudential supervision (the so-called expectation channel). An explanation of the objectives and tasks of macroprudential supervision is important for its success, particularly at the current stage, when it is a new area of regulatory policy which is just developing. The communication policy of the Financial Stability Committee aims to inform about the identified threats to financial stability, explain the decision taken and raise awareness about macroprudential supervision and its importance.

The FSC-M has its own **service on the NBP website**, which serves as a source of information on the measures implemented within macroprudential supervision. This service will be gradually updated with new information and analyses so that public opinion will have the opportunity to get acquainted with various aspects of conducting macroprudential supervision.

Under the Act, the Financial Stability Committee may disclose the resolutions, and in particular, it is required to provide information about the countercyclical buffer.

After each meeting of the Financial Stability Committee a **press release** is published delivering information on the subject discussed at the meeting and the decisions taken by the FSC-M.

Furthermore, pursuant to the Act, the Chairperson of the FSC-M **presents to the Polish Parliament annual information on the activities of the Committee on the implementation of the tasks related to macroprudential supervision**. The annual report is also published on the website of the FSC-M.

7. Review of the document

The aim of this document is to inform the public and financial market entities about the principles of the functioning of the Financial Stability Committee as the macroprudential authority in Poland. Therefore, it should contribute to building up its credibility, which in turn is a condition for the effectiveness of the activities carried out by the FSC-M.

Due to the key role of banks in financing the economy and their significant share in the financial system, in the first period of its activities, the Financial Stability Committee will concentrate on risks characteristic for this sector and phenomena that have an impact on this sector. In the medium term, the FSC-M intends to take measures to:

- fill in the information gaps, which is necessary to better identify sources of systemic risk, particularly outside the credit institutions sector and outside the regulated sector,
- develop analytical tools in the identification and assessment of systemic risk,
- develop research necessary to conduct macroprudential supervision,
- develop the concept of the use of macroprudential instruments, including those that can be applied behind the banking sector.

In accordance with the Recommendation of the European Systemic Risk Board of 4 April 2013 *on intermediate objectives and instruments of macro-prudential policy* (ESRB/2013/1), the Financial Stability Committee will also review the intermediate objectives of macroprudential supervision and the set of instruments and assess whether they are sufficient to effectively fulfil the tasks of the Committee.

Taking into account the experience gained in macroprudential supervision, this document will be subject to review after 2 years.