

Reforming the structure of the EU banking sector

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The Committee on Economic and Monetary Affairs adopted the own-initiative report by Arlene McCarthy (S&D, UK) on reforming the structure of the EU banking sector.

The report begins by noting that state aid of more than EUR 1.6 trillion (12.8 % of EU GDP) was granted to the financial sector between 2008 and the end of 2011, some EUR 1 080 billion of which went on guarantees, EUR 320 billion on recapitalisation measures, EUR 120 billion on impaired assets and EUR 90 billion on liquidity measures. These state financed bailouts have led to a **massive increase of public indebtedness**, and the OECD has estimated that the value of **implicit state guarantees** in 2012, in terms of cost savings to EU banks, at around USD 100 billion. Members further note that **profits in the financial sector were often privatised while risks and losses were nationalised**. However, in a social market economy, risk and liability must go hand in hand. It is only appropriate for the **state to guarantee essential services** that ensure the smooth running of the real economy, such as payment systems and overdraft facilities. **Non-essential services must be priced by the market**.

In this context, the committee welcomes the report of 2 October 2012 of the High-level Expert Group on Reforming the Structure of the EU Banking Sector (HLEG), and also welcomes the Commission's intention to bring forward a **directive for structural reform of the EU banking sector** in order to tackle problems arising from banks being "too big to fail". It underlines that the directive must be complementary to the existing reforms, which include the Capital Requirements Directives and Regulation, [the Recovery and Resolution Directive](#), the Single Supervisory Mechanism, the Deposit Guarantee Schemes, and the Markets in Financial Instruments Directive and Regulation. Members also want the Commission to bring forward a **legislative proposal on the regulation of the shadow-banking sector** that takes into account the principles of the ongoing banking structure reform.

They consider that the objective of all banking structure reform must be to deliver a stable banking system that serves the needs of the real economy, and stimulates economic growth by supporting the provision of credit to the economy, removes risks to public finances and delivers a change in banking culture. With this in mind, Members set forward certain principles for reform.

Principles for structural reform: the committee states that structural reform must be based on the principles set out in the report, particularly that:

- **excessive risks must be reduced** by providing for the **separate operation** of essential activities, including credit, payment, deposit and non-essential risky activities;
- **corporate governance must be improved** and incentives created for banks to increase accountability and reinforce a responsible remuneration system;
- effective bank resolution and recovery must be enabled by ensuring that when banks become untenable **they can be allowed to fail and/or resolved in an orderly manner without the need for taxpayer bailouts**;
- delivery of essential credit, deposit and payment services must be ensured in a manner **unaffected by operational problems**, financial losses, funding shortages or reputational damage resulting from the resolution or insolvency;

- **risky trading and investment activities must not benefit from implicit guarantees** or subsidies, or the use of insured deposits or tax payer bailouts, and the trading and investment activities (not the credit and deposit activities) must bear the risks and costs associated with those activities;
- adequate capital, leverage and liquidity must be available for all banking activities;
- the separated entities must have different sources of funding, with no undue or unnecessary shifting of capital and liquidity between these activities.

Members stress that banks must have in place credible crisis management frameworks that include sufficient capital for credit, payment and deposit activities, bail-in-able liabilities and liquid assets to enable them, in the event of failure, to maintain depositors' access to funds, protect essential services from the risk of disorderly failure, pay out depositors in a timely fashion and avoid adverse effects on financial stability.

Corporate governance: the report calls on the Commission to:

- consider the proposals set out in the HLEG's report in the area of corporate governance;
- implement the proposals set out in [Parliament's resolution of 11 May 2011 on corporate governance in financial institutions](#);
- include provisions establishing an obligation for all executive board members in an entity of a bank to have responsibility as executive board members only for this entity of the bank;
- include provisions to **strengthen personal accountability and liability for board members**;
- ensure full implementation of the Capital Requirements legislative framework, with particular regard to the provisions on compensation and remuneration, and present an annual report to Parliament and the Council on the implementation and enforcement of the relevant provisions by the Member States;
- make provision for effective, dissuasive and proportionate sanctioning regimes for legal and natural persons, and for the publication of sanction levels and of information on those in breach of the rules;
- **conduct a study** to ensure that accounting standards used by financial institutions give a genuinely true and fair view of banks' financial health, recalling that the loss of prudence in accounting standards as a consequence of the adoption of international financial reporting standards played, and continues to play, a central role in allowing banks to give a view of their accounts that was not, and is not, always true and fair, with particular reference to IAS 39 on loan loss provisioning.

Enhancing fair and sustainable competition: Members stress the importance of effective, fair and sustainable competition to the EU's economy and urge the Commission and Member States to work together to **promote greater diversification** of the EU's banking sector by encouraging **more consumer-oriented banking**, for example through cooperatives and building societies. They underline the need to effectively address the issue of SIFIs ('systemically important financial institution'), which are deemed too big to fail, by **rationalising the scale of the activities of banking groups and by reducing interdependencies within groups**.

Lastly, the report asks the Commission to bring forward measures to promote **accessible websites** that allow consumers to compare the financial strengths of banks, and to assist in improving consumer choice in the banking sector.